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THIRD REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA, AND REQUEST FOR AN ARRANGEMENT UNDER THE RESILIENCE AND SUSTAINABILITY FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR CABO VERDE

In the context of the Third Review Under the Extended Credit Facility Arrangement, Request for Modification of Performance Criteria, and Request for an Arrangement Under the Resilience and Sustainability 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 December 11, 2023, following discussions that ended on November 2, 2023, 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 November 22, 2023.
- A **Debt Sustainability Analysis** prepared by the staff[s] of the IMF and the International Development Association.
- A **World Bank Assessment Letter for the Resilience and Sustainability Facility**
- A **Statement by the Executive Director** for Cabo Verde.

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IMF Executive Board Concludes the Third Review of the Extended Credit Facility Arrangement and Approves US$31.45 Million under the Resilience and Sustainability Facility for Cabo Verde

FOR IMMEDIATE RELEASE

- The IMF Executive Board completed the third review under the 36-month Extended Credit Facility (ECF) arrangement with Cabo Verde, providing the country with access to SDR 4.5 million (about US$6 million), and approved an 18-month arrangement under the Resilience and Sustainability Facility (RSF), in the amount of 100 percent of quota (SDR 23.69 million, about US$31.45 million).
- Performance under the economic reform program is strong, and the authorities are taking steps to further strengthen the program. Post-Covid economic activity recovered as tourism returned to the islands.
- The RSF will support the government's effort to implement macro-critical climate reforms and catalyze private finance for climate adaptation and transition.

Washington, DC – **December 11, 2023:** The Executive Board of the International Monetary Fund (IMF) completed the Third Review of Cabo Verde's performance under the 36-month Extended Credit Facility (ECF) arrangement that was approved on June 15, 2022, and approved the request for an 18-month arrangement under the Resilience and Sustainability Facility (RSF). The completion of the review allows the authorities to draw the equivalent of SDR 4.5 million (about US$6 million). The arrangement under the RSF is in the amount of 100 percent of quota (SDR 23.69 million, approximately US$31.45 million).

In completing the third review, the Executive Board approved the authorities' request for modification of the end-December 2023 and end-June 2024 performance criteria.

Cabo Verde's performance under the ECF is strong. The economy rebounded strongly in 2022 with real GDP growing 17.1 percent but is projected to moderate to 4.5 percent in 2023 as export growth normalizes. Inflation is projected at 3 percent by end 2023, as fuel and food prices decline. The current account deficit is expected to widen in 2023 as exports of goods and services, tourism and remittances grow more slowly than imports. The 2024 budget is aligned with the ECF-supported program. The Banco de Cabo Verde (BCV) tightened monetary policy further to narrow the interest rate differential with the European Central Bank (ECB) to protect the peg.

The RSF will support the government's effort to implement macro-critical climate reforms and catalyze private finance for climate adaptation and transition. The program will support the authorities' reform measures in five areas: (i) strengthening climate change policy governance; (ii) improving physical and fiscal resilience; (iii) strengthening mitigation and resilience through promoting energy efficiency and transition to renewables; (iv) promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts; and (v) strengthening financial sector resilience to climate change.

The outlook is uncertain and subject to downside risks which could emanate from weakened demand in major tourism markets and external price shocks. Fiscal risks could also stem from the failure to advance State-Owned Enterprise (SOE) reforms or reduced fiscal consolidation efforts. The effects of climate change—a key medium-term risk—are evidenced in the recent years of drought. The country's high risk of overall debt distress is a source of vulnerability and thus concessional financing to limit debt servicing cost is important. On the upside, stronger tourism growth could lead to higher overall economic activity.

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

"Economic activity has recovered rapidly in Cabo Verde post-COVID and the near-term outlook is favorable despite downside risks. Inflation decelerated faster than anticipated at the time of the second review, despite the ripple effects from the war in Ukraine on food, fuel, and transportation costs. Risks to the outlook remain, including, from potential lower external demand from major tourism markets and climate change shocks.

Program performance and ownership has been strong. All performance criteria were met, and all program-supported structural reforms were also met.

Fiscal policy is anchored by an appropriate balance between fiscal consolidation to put debt on a downward path, while protecting the vulnerable and investing in key priority projects for future growth. The medium-term fiscal objectives are dependent on the progress in domestic revenue mobilization, streamlining tax exemptions, increasing the effectiveness of public investment projects, and improving debt management. Steady progress on SOE reforms remains critical for reducing fiscal risks and improving services.

The monetary policy appropriately remains focused on safeguarding the peg. The financial sector remains stable from a medium-term perspective. Banks' profitability has been positive and NPLs maintained the downward trend since 2016. The authorities are advised to continue working with banks to facilitate resolution of NPLs. Measures to improve the autonomy, governance and accountability framework of the central bank and strengthen the AML/CFT framework and its effectiveness remain crucial.

The authorities are encouraged to continue with their ambitious structural reform agenda to adapt to the challenges posed by climate change, reduce the cost of doing business and accelerate public enterprise reforms. The Cabo Verdean authorities are encouraged to pursue their strong package of reforms measures under the RSF arrangement, and to leverage synergies with other official financing and catalyze further public and private financing for climate mitigation and adaptation efforts."

Cabo Verde: Selected Economic Indicators, 2020-28

	2020	2021	2022	2022	2023	2023	2024	2025	2026	2027	2028
			SR ECF 2nd review	Act.	SR ECF 2nd review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Annual percent change)										
National accounts and prices 1/											
Real GDP	-20.8	5.6	17.7	17.1	4.4	4.5	4.7	4.7	4.6	4.6	4.5
GDP deflator	0.7	-0.3	6.4	7.7	4.5	4.7	2.0	2.0	2.0	2.0	2.0
Consumer price index (annual average)	0.6	1.9	7.9	7.9	5.2	4.0	2.0	2.0	2.0	2.0	2.0
Consumer price index (end of period)	-0.9	5.4	7.6	7.6	5.2	3.0	2.0	2.0	2.0	2.0	2.0
External sector											
Exports of goods and services	-58.7	-7.5	120.6	120.6	3.7	3.2	8.7	9.5	9.4	8.7	8.1
Of which: tourism	-69.1	-16.4	225.4	225.4	7.7	6.5	10.1	8.8	9.4	8.7	8.7
Imports of goods and services	-23.2	0.8	33.7	33.7	7.8	10.2	9.8	7.0	5.4	6.0	4.9
	(Change in percent of broad money, 12 months earlier)										
Money and credit											
Net foreign assets	-6.6	2.9	1.2	1.2	3.4	4.8	2.8	0.9	0.0	0.0	1.6
Net domestic assets	10.3	0.1	4.6	4.6	4.9	4.6	4.3	4.5	4.8	4.9	3.6
Net claims on the central government	-1.3	2.4	3.1	3.1	0.8	0.0	-0.1	-0.1	0.2	-0.4	-0.6
Credit to the economy	2.9	4.2	3.9	3.9	3.9	4.5	4.4	4.5	4.5	5.2	4.2
Broad money (M2)	3.8	3.0	5.8	5.8	8.3	9.4	7.2	5.4	4.8	4.9	5.3
	(Percent of GDP, unless otherwise indicated)										
Savings and investment											
Domestic savings	8.8	28.3	41.7	34.7	18.7	21.4	18.1	17.5	13.7	10.3	12.4
Government	-7.6	-5.3	-0.4	0.8	0.5	0.2	1.1	2.4	2.5	3.1	3.1
Private	16.4	33.6	42.1	33.9	18.2	21.2	17.0	15.1	11.2	7.2	9.3
National investment	24.1	40.5	45.3	38.4	24.3	27.3	24.2	23.8	19.5	15.7	17.0
Government	3.4	2.3	1.9	1.9	4.2	3.2	3.9	4.0	3.2	3.5	3.6
Private	20.7	38.2	43.4	36.4	20.0	24.1	20.2	19.8	16.3	12.2	13.4
Savings-investment balance	-15.3	-12.2	-3.6	-3.7	-5.6	-5.9	-6.1	-6.3	-5.8	-5.4	-4.6
Government	-11.0	-7.6	-2.2	-1.1	-3.8	-3.1	-2.8	-1.6	-0.7	-0.4	-0.5
Private	-4.4	-4.6	-1.3	-2.6	-1.8	-2.9	-3.3	-4.6	-5.1	-5.0	-4.1
External sector											
External current account (including official transfers)	-15.3	-12.2	-3.6	-3.7	-5.6	-5.9	-6.1	-6.3	-5.8	-5.4	-4.6
External current account (excluding official transfers)	-18.0	-14.7	-4.9	-5.1	-5.9	-6.2	-6.9	-6.9	-6.4	-6.0	-5.1
Overall balance of payments	-4.7	0.6	1.1	1.1	3.0	4.4	2.7	0.9	0.1	0.1	1.5
Gross international reserves (months of prospective imports of goods and services)	7.8	6.0	5.9	5.7	6.1	6.1	6.2	6.0	5.7	5.5	5.5
Government finance											
Revenue	25.2	23.9	21.6	22.4	24.6	25.5	27.6	26.0	25.3	25.9	25.8
Tax and nontax revenue	21.9	21.8	20.7	21.5	22.7	23.6	25.2	24.6	24.5	24.7	24.7

Grants	3.3	2.1	0.9	0.9	1.9	1.9	2.3	1.5	0.7	1.2	1.1
Expenditure	34.5	31.6	25.7	26.7	29.0	28.9	30.9	28.2	26.4	26.3	26.4
Primary balance	-6.6	-5.4	-1.9	-2.0	-2.2	-1.1	-1.1	0.0	1.0	1.0	1.0
Overall balance (incl. grants)	-9.3	-7.7	-4.1	-4.3	-4.4	-3.4	-3.4	-2.1	-1.2	-0.4	-0.5
Net other liabilities (incl. onlending)	-1.2	0.9	-0.1	-0.1	0.7	-0.5	-0.2	-0.1	-0.1	0.0	0.0
Total financing (incl. onlending and capitalization)	9.8	6.8	4.2	4.3	3.7	4.0	3.6	2.3	1.3	0.4	0.5
Net domestic credit	3.1	1.7	2.3	2.4	1.4	-0.1	-0.2	-0.2	0.3	-0.7	-1.0
Net external financing	6.7	5.1	1.9	2.0	2.3	4.0	3.8	2.4	0.9	1.0	1.5
Public debt stock and service											
Total nominal government debt	142.6	152.0	121.2	127.1	112.6	119.9	116.2	111.2	105.4	99.4	93.9
External government debt	105.1	108.2	84.0	88.0	79.8	82.7	81.9	79.4	75.1	71.3	68.8
Domestic government debt	37.5	43.8	37.1	39.1	32.8	37.2	34.3	31.8	30.3	28.1	25.1
External debt service (percent of exports of goods and services)	14.8	20.2	11.5	15.2	12.4	12.3	11.9	10.9	10.5	9.8	9.1
Present value of PPG external debt											
Percent of GDP (risk threshold: 55%)	70.3	57.2	53.5	53.5	50.9	54.2	53.3	52.0	49.5	47.4	46.1
Percent of exports (risk threshold: 240%)	335.9	197.4	159.1	163.8	156.6	161.4	156.1	148.6	137.8	129.5	124.1
Present value of total debt											
Percent of GDP (benchmark: 70%)	92.4	104.3	91.3	97.1	84.0	90.8	87.5	83.7	79.9	75.6	71.2
Memorandum items:											
Nominal GDP (billions of Cabo Verde escudos)	176.8	186.2	244.3	235.0	266.6	257.1	274.7	293.4	313.1	333.9	356.0
Gross international reserves (€ millions, end of period)	582	595	626	626	699	728	794	819	823	827	875

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

November 22, 2023

THIRD REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA, AND REQUEST FOR AN ARRANGEMENT UNDER THE RESILIENCE AND SUSTAINABILITY FACILITY

EXECUTIVE SUMMARY

Context and Outlook. Cabo Verde has weathered the recent shocks well, and the authorities have been successful in maintaining macro-financial stability, supported by international partners. Despite a challenging global environment, Cabo Verde's economy rebounded strongly in 2021 and 2022 and continues its strong macroeconomic performance in 2023.The near-term growth outlook is favorable despite some downside risks. Inflation is decelerating. The country is politically stable. However, Cabo Verde still faces substantial vulnerabilities. The public debt-to-GDP ratio though declining is still above pre-pandemic levels. Climate change poses a major threat, as Cabo Verde is one of the most water-scarce countries in the world.

Program Performance. All quantitative performance criteria (QPCs) for end-June 2023 were met. The indicative targets (ITs) for end-March and end-June 2023 were met. Regarding structural benchmarks (SBs), the authorities met the ones for end-June, end-July, and end-September 2023. The ECF will expire in June 2025. A new set for end-December 2024 PCs and end-September 2024 ITs is proposed. The authorities request the modification of the PC on the PV of new external debt for end-December 2023 and a modification of the PCs on net other liabilities for end-December 2023 and end-June 2024.

RSF Request. The proposed RSF arrangement (SDR 23.7 million, 100 percent of quota) will support the government's effort to implement macro-critical climate reforms and catalyze private finance for climate adaptation, and transition. The program will support the authorities' reform measures in five areas: (i) strengthening climate change policy governance; (ii) improving physical and fiscal resilience; (iii) strengthening mitigation and resilience through promoting energy efficiency and transition to renewables; (iv) promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts; and (v) strengthening financial sector resilience to climate change.

Approved By
Costas Christou (AFR) and Peter Dohlman (SPR)

The discussions in Praia took place during October 24-November 2, 2023. The in-person team consisted of Justin Tyson (head), Jose Sulemane, Nombulelo Gumata, Daniel Cunha, Didier Tabaro and Tomas Picca (all AFR), Nicoletta Feruglio and Katja Funke (both FAD), and Rodrigo Garcia-Verdu (Res. Rep.). Bruno Saraiva (OED) also participated in the mission. The mission met with Prime Minister Ulisses Correia e Silva, Vice Prime Minister and Minister of Finance and Business Development Olavo Correia, Central Bank Governor Oscar Santos, other government and central bank officials, representatives of the private sector, and development partners. Lester Magno (AFR) assisted in the preparation of this report.

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CONTEXT

1. **Economic performance under the program supported by the Extended Credit Facility (ECF) has been strong**. Post-Covid economic growth recovered rapidly as tourism returned to the islands. The economy rebounded growing at 6.4 percent in 2021 and 17 percent in 2022.[1] The fiscal deficit narrowed, the debt-to-GDP ratio declined to 127.1 percent in 2022, the current account deficit narrowed, and international reserves increased. The authorities' policy responses supported the recovery and the most vulnerable.

2. **Sustained efforts are critical to keep Cabo Verde on a stable growth trajectory**. The country remains vulnerable to economic and climate-related disruptions, and the gains achieved need to be sustained beyond the medium-term horizon to preserve economic stability, build resilience, and promote inclusive growth. Given Cabo Verde's vulnerability to climate change, advancing climate reforms is critical to build resilience, reduce future BOP needs, and safeguard the gains made in reducing debt. The country also needs to reduce its vulnerability to external economic and domestic shocks. These priorities are built into the new five-year Strategic Plan for Sustainable Development 2022-2026 (PEDS II) that was launched end-2022.

3. **The authorities have requested support under the Resilience and Sustainability Facility (RSF) to help address climate vulnerabilities, risks, and challenges**. The RSF would increase concessional financing and substitute more expensive domestic financing, which will help implementation over time of the authorities' climate-related investments and reforms. These will help catalyze financing for climate change mitigation and adaptation strategies. The Nationally Determined Contribution (NDC) estimates the total funding required to support climate adaptation and mitigation activities at USD 2 billion between now and 2030, equivalent to about 6.1 percent of GDP per year.

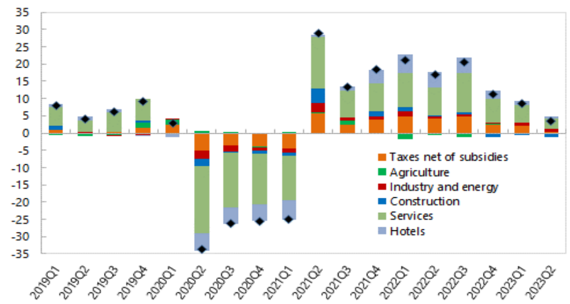
RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

4. **Macroeconomic performance continued strongly in the first part of 2023**.

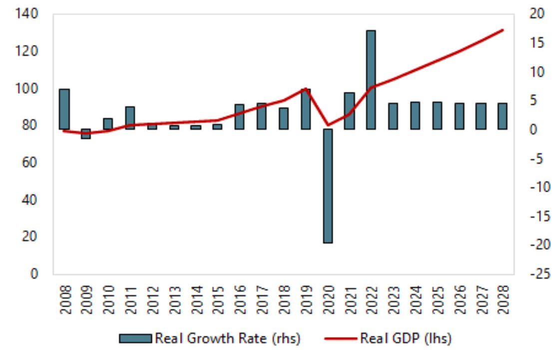
- **Real GDP grew at 5.8 percent year-on-year (y/y) in H1-2023 (Text Figure 1)**, reflecting a strong performance in the tourism sector (Text Figure 2). The services sector was the highest contributor to growth, accounting for 4.1 percentage points, while on the demand-side investment remains below pre-pandemic levels. Economic activity was supported by stable credit growth to the economy of 6.3. percent by end-June 2023 (y/y). Inflation decelerated faster than anticipated at the time of the second review to 2.9 percent (y/y) at end-August 2023 from 7.6 percent in December 2022, mostly driven by decreases in food and energy prices (Figure 1).

[1] The current Staff Report uses a revised version of the rebased GDP series, leading to some differences in growth rates and ratios relative to the last Staff Report.

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

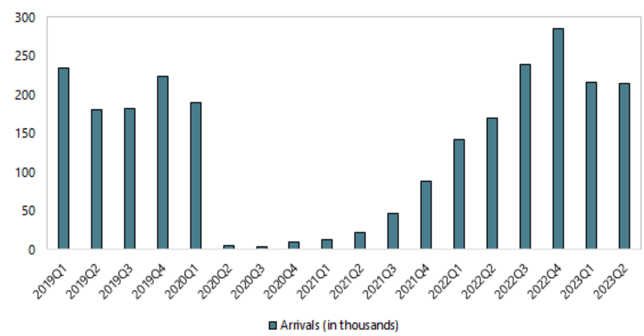


Text Figure 1b. Cabo Verde: Real Output and Growth Rates
(2019 Base = 100)

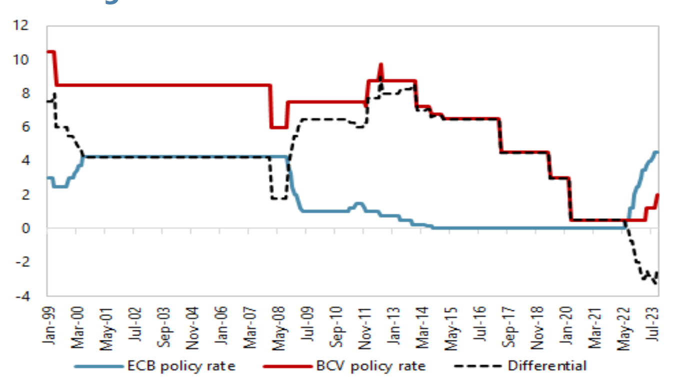


- **The fiscal position improved in the H1:2023**. Economic activity, and policy measures, supported an increase in tax revenues (22.6 percent 1H2023/1H2022). Primary expenditure grew by 6.1 percent 1H2023/1H2022. Subsidies, net acquisition of non-financial assets, and acquisition of goods and services were the main positive drivers, while slower growth in the wage bill and a fall in other current expenditures helped contain the overall primary expenditure growth rate. As a result, the primary balance over 1H2023 registered a surplus of CVE 2,759 million, compared with the CVE -4,141 million target under the program (1H2023).

Text Figure 2. Cabo Verde: Tourism Developments



Text Figure 3. Cabo Verde: Interest Rate Differential



- **The current account deficit narrowed in the first half of 2023**. This was due to the stronger-than-expected recovery in goods exports, tourism receipts, and remittances. Reserves were also boosted by the ECF disbursements of SDR15.76 million (66.5 percent of quota, about US$21.19 million). As a result, gross international reserves grew to around €639 million at end-September 2023.

- **Monetary policy remains focused on safeguarding the peg**. The Monetary Policy Committee (MPC) raised the policy rate from 0.25 to 1.0 percent in early May 2023, and to 1.25 percent in November 2023 to narrow the differential with the ECB policy rate and protect reserves. The monetary stance also considers the tightening impact of the reversal of the COVID-related credit moratorium and the Long-Term Financing Program. The reserve cover of 5.3 months of imports is adequate to protect the peg. At end-June 2023, M2 grew at 5.9 percent (y/y), total deposits by 6 percent (y/y) and credit to the economy by 6.3 percent (y/y).

- **The financial sector appears stable, adequately capitalized and liquid (Table 5)**. Data for end-June 2023 suggests that the financial system is liquid, profitable, and well capitalized. Regulatory capital to risk weighted assets (CAR) was 21.4 percent a slight decline relative to end-December 2022 (22.2 percent), but well-above the regulatory minimum of 12 percent. The return on equity and return on assets stood at 9.2 and 0.9 percent, respectively, a drop compared to end-December 2022 (16 and 1.5 percent, respectively). The relatively low return on assets is mainly a reflection of the legacy non-preforming loans (NPLs) portfolio related to the 2008 global financial crisis. NPLs increased from 7.8 percent at end 2022 to 8.7 percent of total loans at end-June 2023. The increase in the NPL ratio in 2023 is linked to customers in the real estate and construction sectors, who benefited from the public moratorium regime during Covid. Likewise, the credit at risk indicator shows an increasing trend, standing at 18.7 percent compared to 14.9 percent in June 2022. The banks continue the process of cleaning up their balance sheets by reinforcing impairments and writing off non-productive credits and, to a lesser extent, collecting collateral.

5. **Cabo Verde's near-term economic outlook remains favorable but has moderated from recent highs**. Real GDP growth is projected at 4.5 percent in 2023 as exports growth (especially services) normalizes following the return to the pre-pandemic levels of visitor arrivals. The economy is projected to grow at 4.7 percent next year before converging to potential growth of 4.5 percent after 2028, assuming structural reforms help lift potential growth. Inflation would moderate to 3 percent in 2023 and decline to 2 percent over the medium-term, broadly in line with Euro area inflation, as oil and food prices decline.

6. **The medium-term current account is driven by factors associated with the implementation of the climate reform agenda**. The current account deficit is expected to widen to about 5.9 percent of GDP in 2023 as the growth of exports of goods and services, tourism, and remittances slows down over Q2 and Q3 from levels recorded in 2022. In the medium term, the widening of the current account deficit is driven by the implementation of the RSF reform measures and imports of low carbon technologies. FDI is projected to improve in the medium term in line with the catalytic impact of the RSF, the EU Gateway program and growth in the tourism sector. The External Sector Assessment suggests that Cabo Verde's external position in 2022 was substantially stronger than implied by fundamentals and desirable policies, which points to an undervaluation of the real effective exchange rate.

7. **The outlook is uncertain and subject to downside risks (geopolitical and climate)**. Downside risks could emanate from weakened demand in major tourism markets and external price

shocks. Fiscal risks could also stem from the failure to advance State-Owned Enterprise (SOE) reforms or reduced fiscal consolidation efforts. The effects of climate change—a key medium-term risk—are evidenced in the recent years of drought. The country's high risk of overall debt distress is a source of vulnerability and thus concessional financing to limit debt servicing cost is important. On the upside, stronger tourism growth could lead to higher overall economic activity.

Box 1. Sensitivity of Potential GDP Growth and the Scarring Effect of the Pandemic

We explore the sensitivity of potential GDP growth using a production function approach. Potential growth is given by the Cobb Douglas production function, $Y_t = A_t K_t^{\alpha} L_t^{1-\alpha}$. We assume that capital evolves according to $K_t = (1-\delta)K_{t-1} + I_t$, where δ is depreciation rate and I_t is fixed investment. The growth rate of potential GDP, g_t, can then be recovered as:

$$1+ g_t = (1+ g_t^A)(1-\delta + (1+g_t)i_t/k_{t-1})^{\alpha}(1+ g_t^L)^{1-\alpha}$$

We calibrate the model using historical data and labor force projections. We set the capital share, α, to 37 percent, in line with the historical average between 2015-2019 to capture the pre-pandemic average before the COVID-19 shock. The capital-to-GDP ratio is calibrated at its 2018 level 4.66 according to the Penn World Table. Using demographic projections from INE, and assuming the labor force participation remains constant at its 2019 level, we estimate that the annual growth rate of the employed population will drop to about 0.8 percent over the next two decades, down from an average of 1.2 percent in the 2010s.

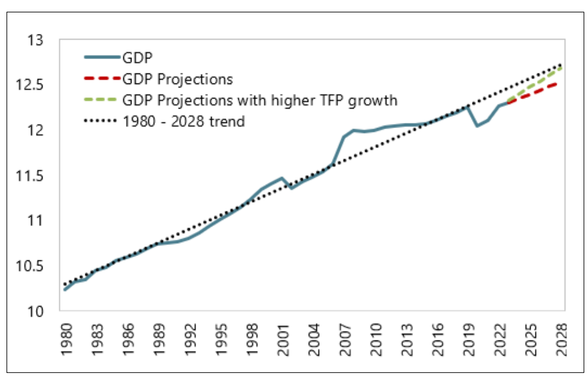
The results highlight that productivity growth needs to increase to boost potential growth, implying significant structural reforms. If productivity continues to grow at 1.6 percent and the investment share of GDP remains around 28 percent, in line with 2015-2019 averages, potential GDP is projected to be around 4.1 percent. To lift potential growth to about 7 percent, structural reforms are needed to raise productivity growth to at least 4.5 percent given that the investment rate is already high and unlikely to contribute more to higher growth (albeit temporarily) without catalytic reforms to boost private investments.

Investment to GDP ratio

Productivity growth	24	26	28	30	32
-1.5	-0.5	0.3	1.0	1.8	2.5
0.0	1.0	1.8	2.5	3.3	4.0
1.6	2.6	3.4	4.1	4.9	5.6
3.0	4.0	4.8	5.5	6.3	7.0
4.5	5.5	6.3	7.0	7.8	8.5

Source: staff's calculations
Notes: shaded areas corresponds to 2015-2019 average

If growth increases to around 7 percent, the scarring effect of the pandemic may vanish by 2028. In 2022, economic activity rebounded strongly to its pre-COVID level, mainly driven by the tourism sector. However, the baseline projection assumes a permanent gap between the forecasted GDP level and the pre-COVID trend level in line with other EMs and LICs. To close the gap, structural reforms are needed to enhance TFP and unlock private investments, especially considering the limited fiscal space of Cabo Verde due to its high level of debt.



POLICY DISCUSSIONS

ECF Arrangement

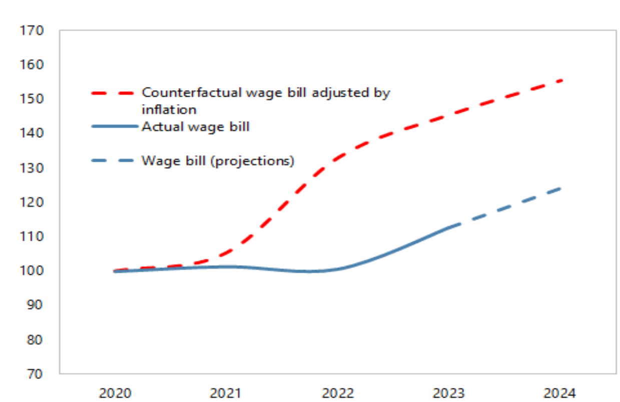
A. Strengthen Public Finances to Preserve Debt Sustainability

8. **Fiscal policy is anchored by the primary balance path consistent with putting debt on a downward path**. The primary deficit is projected at 1.1 percent of GDP in 2023, an improvement relative to the second review. This reflects strong revenues in 1H2023, which slow down in 2H2023 in line with economic activity, and under-execution of capital expenditures. The delayed airport concession fee (1.4 percent of GDP and already in the baseline) was received in 3Q2023, obviating the need for contingency measures. Current spending is projected at the level agreed in the program; however, there is a compositional shift from other current expenditures to subsidies of 0.2 percent of GDP to support: i) imports of a basic food staples, ii) the inter-island transportation company, and iii) energy/water SOEs to implement the social tariff for energy and water targeted to poor households. The spending-to-GDP ratio changes slightly, mainly reflecting updates to the revised nominal GDP series. The 2023 balance of risk for the estimated primary deficit is tilted to the upside given revenue performance in 1H2023.

9. **The 2023 fiscal deficit will be financed through a combination of external and domestic financing**. Gross financing needs are projected to be marginally lower than in 2022, with a shift in composition of financing sources to meet these GFNs towards external financing. Net external financing of 4 percent of GDP is projected for 2023, which is higher than the outturn for 2022 due in part to the completion of the first review in early 2023 instead of end-2022, and non-disbursement of project loans from the World Bank due to implementation delays. Net domestic financing is projected to continue trending downwards. Gross financing needs are higher than expected in the 2nd review, mainly explained by the postponement of the privatization of public enterprises in the banking and pharmaceutical sectors to 2024.

10. **The draft 2024 budget is in line with the program**. The draft budget is based on more optimistic growth forecasts than staff's and assumes higher tax collection of CVE 1.3 billion (Text Table 1). Grants increase in 2024 because of additional bilateral contracts and other revenues improve due to higher concessional, fee, and penalties incomes. Budgeted primary expenditures, however, are in line with staff projections. The budget will reverse the 2023 increase in subsidies by reducing the support to the water sector and ending the aid for basic food staples and include an additional CVE 1 billion capital spending relative to the

Text Figure 4. Cabo Verde: 2024 Wage Bill



second review. The wage bill is projected to grow above inflation to partially recover the purchasing power lost due to wage restraint over the last couple of years. As a result, while the primary deficit under the draft budget is 0.7 percent of GDP, the program includes a primary deficit of 1.1 percent of GDP. The higher investments (relative to the 2nd review) are related to the implementation of the RSF's RMs 5 and 6 and financed through a combination of higher grants, concession fees, and tax revenue implying a slight increase in the primary deficit compared to the 2nd review. The additional income allows higher investment over 2024 and 2025 before capital spending returns to the baseline path in 2026, which implies more adjustment in that year than under the 2nd review. The 2024 expansion of use of goods and services is driven by additional funding via grants and is projected to contract in 2025 due to a normalization of grants. The authorities agreed than improved execution of public investment plans is important for growth. SOE reforms are expected to reduce capitalization[2] and on-lending starting in 2025, helping improve the fiscal position.

Text Table 1. Cabo Verde: Revised 2023-24 Fiscal Framework[1]

	2023						2024					
	Budget		2nd Review-SR		Proj.		Draft Budget		2nd Review-SR		Proj.	
	Millions of CVE	Percent of GDP	Millions of CVE	Percent of GDP	Millions of CVE	Percent of GDP	Millions of CVE	Percent of GDP	Millions of CVE	Percent of GDP	Millions of CVE	Percent of GDP
Revenue	64,237	27.8	65,590.4	24.6	65,562	25.5	77,050	26.9	69,245.0	24.4	75,720	27.6
Taxes	44,349	19.2	48,205.9	18.1	48,537	18.9	55,337	19.3	53,006.0	18.7	53,974	19.6
Grants	5,225	2.3	5,162.9	1.9	4,798	1.9	6,409	2.2	3,504.0	1.2	6,409	2.3
Other revenue	14,663	6.3	12,221.6	4.6	12,227	4.8	15,303	5.3	12,735.0	4.5	15,337	5.6
Expenditure	77,220	33.4	77,359.1	29.0	74,388	28.9	85,227	29.8	78,684.0	27.7	85,001	30.9
Expense	66,022	28.6	66,028.9	24.8	66,055	25.7	74,439	26.0	69,305.0	24.4	74,231	27.0
Net acquisition of nonfinancial assets	11,198	4.8	11,330.1	4.2	8,333	3.2	10,788	3.8	9,380.0	3.3	10,770	3.9
Purchase of assets	11,945	5.2	12,077.1	4.5	9,080	3.5	11,510	4.0	10,085.0	3.6	11,475	4.2
Sale of assets	-747	-0.3	-747.0	-0.3	-747	-0.3	-722	-0.3	-705.0	-0.2	-705	-0.3
Primary balance	-7,106	-3.1	-5,890.6	-2.2	-2,948	-1.1	-1,939	-0.7	-2,804.0	-1.0	-3,064	-1.1
Overall balance	-12,983	-5.6	-11,768.6	-4.4	-8,826	-3.4	-8,177	-2.9	-9,439.0	-3.3	-9,281	-3.4
Net other liabilities	1,936	0.8	1,940.3	0.7	-1,368	-0.5	657	0.2	-557.9	-0.2	-558	-0.2
o/w Onlending to SOEs for investment purpose	-1,851	-0.8	-1,851.0	-0.7	-1,851	-0.7	-194	-0.1	-441.1	-0.2	-441	-0.2
o/w Other onlending (net)	194	0.1	197.3	0.1	198	0.1	-75	0.0	171.7	0.1	172	0.1
o/w Capitalization	-2,200	-1.0	-2,200.0	-0.8	-2,200	-0.9	-2,600	-0.9	-2,600.4	-0.9	-2,600	-0.9
Financing needs	11,047	4.8	9,828.3	3.7	10,194	4.0	7,520	2.6	11,713.0	4.1	9,839	3.6
Financing	11,047	4.8	9,828.3	3.7	10,194	4.0	7,520	2.6	11,713.0	4.1	9,839	3.6
Domestic (net)	6,631	2.9	3,771.7	1.4	-214	-0.1	3,835	1.3	8,277.0	2.9	-636	-0.2
External (net)	4,416	1.9	6,056.6	2.3	10,408	4.0	3,685	1.3	3,436.0	1.2	10,475	3.8
Public debt (percent of GDP)	…			112.6		119.9	…			109.3		116.2
Nominal GDP	231,002		266,599		257,068		286,355		283,791		274,688	

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.

11. The realization of the medium-term fiscal objectives is dependent on progress in implementing revenue mobilization measures (Box 2). Cabo Verde has a broad-based revenue mobilization plan that includes tax administration reforms through digitalization of revenue collection to help improve compliance, and already implemented policy measures (tobacco, alcohol, and international arrivals tax, import duty on previously exempted goods). To support fiscal and debt sustainability, the authorities are working on an action plan to reduce tax expenditures and undertake phased implementation of the ECOWAS tariff, that is expected to increase revenue by 1 percent of GDP (SBs, end-September 2024 and end-December 2024). The medium-term fiscal path could be impacted by the knock-on effects of climate related events on the macro economy.

[2] For example, capitalization expenditures to support the national airline (TACV) are projected to cease in 2025 reflecting the current company business plan which aims to increase routes.

12. The public debt-to-GDP ratio remains on a downward path. It is forecasted to decrease from 127.1 percent in 2022 to 119.9 percent at end-2023, mainly reflecting higher nominal growth. Even with higher public investment in 2024 the debt-to-GDP ratio improves to 116.5 percent, close to pre-pandemic levels. The authorities are committed to continued debt reduction over the medium-term to build buffers and fiscal space for investment and stressed that any revenue overperformance will be used to improve the primary deficit, as is planned in 2023.

Text Table 2. Cabo Verde: External Borrowing Program, 2023–24

	2023		2024	
PPG external debt contracted or guaranteed	**Volume of new debt, USD million 1/**	**Present value of new debt, USD million 1/**	**Volume of new debt, USD million 1/**	**Present value of new debt, USD million 1/**
Sources of debt financing	197.1	108.8	229.1	125.5
Concessional debt, of which 2/	197.1	108.8	229.1	125.5
Multilateral debt	119.0	62.8	153.7	81.1
Bilateral debt	78.2	46.1	75.3	44.4
Non-concessional debt, of which	0.0	0.0	0.0	0.0
Semi-concessional debt 3/				
Commercial terms 4/				
Uses of debt financing	197.1	108.8	229.1	125.5
Infrastructure	98.5	54.3	98.5	54.3
Budget financing	98.6	54.5	130.6	71.2

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 such established at a higher level.
Some of the loans are packaged with grants, 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.

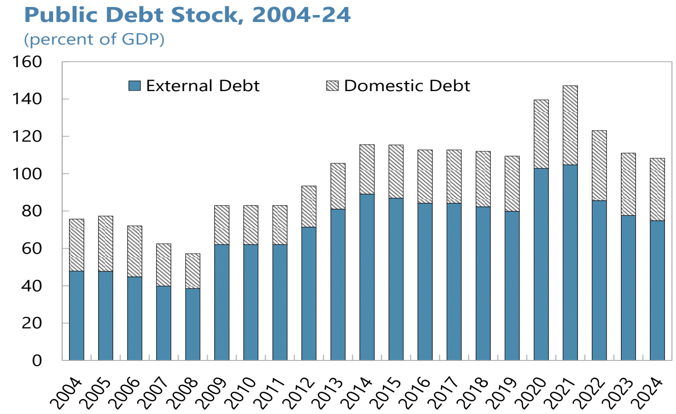
Text Table 3. Cabo Verde: Tax Revenue Projections 2023-25 (Percent of GDP)

Tax revenue to GDP ratio 2023 (second review)	**18.1**
Change in nominal GDP (rebasing)	**0.8**
Tax revenue to GDP ratio 2023 (third review)	**18.9**
Tax administration measues 2024	**0.5**
VAT arrears collection	0.2
Income tax arrears collection	0.1
Eletronic invoicing	0.1
Personal income tax arrears collection	0.1
Tax policy measures 2024	**0.3**
International arrivals tax	0.1
Increase of tabacco and alcohol lump-sum tax	0.2
Tax policy measures 2025	**0.9**
Reduction in tax expenditures and ECOWAS implementation	0.9
Tax revenue to GDP ratio 2025	**20.5**

Sources: Cabo Verdean authorities and IMF staff estimates.

13. Cabo Verde's risk external of debt distress remains moderate and public debt is assessed as sustainable. The current joint World Bank/IMF Debt Sustainability Analysis (DSA) shows that Cabo Verde's risk of external debt distress remains moderate under the ECF/RSF, but the overall risk of debt distress remained high. The analysis indicates that public debt is sustainable, due to manageable debt service from the favorable debt structure based largely on fixed interest rates, which provides protection from the ongoing global tightening cycle. Staff stressed that sustaining the gains in debt sustainability requires continued concessional funding from multilateral creditors.

Text Figure 5. Cabo Verde: Profile of Public Debt, 2004–24



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

Box 2. Tax Policy and Revenue Measures to Improve Fiscal Sustainability

Reducing tax incentives and tax expenditures is important to enhance the efficiency of tax policy. The already implemented tax policy measures are a step in the right direction. However, there is scope for tax policy changes to achieve additional revenue mobilization, and to improve the efficiency and simplicity of Cabo Verde's tax system. This can be achieved by repealing incentives in the financial sector, and abolishing duplicated tax incentives (for instance, those granted to Conventions of Establishment which are already granted in the tax code). Similarly, it is recommended to prioritize the rationalization of existing tax benefits whose objectives are not being achieved or that accentuate inequity and inefficiency in the tax system
(e.g., many VAT-exempt products and deductions to the personal income tax base). (Coelho, et al. 2023).[1]

Further investments in IT are needed to unlock digitalization gains. The digitization efforts of Direção Nacional das Receitas de Estado (DNRE), demonstrated in projects like electronic invoicing and a VAT audit system, are progressing yet face hurdles due to resource and staffing constraints. Despite an optimistic estimate that the VAT electronic auditing system could potentially contribute up to 1 percent of GDP, DNRE is confronted with challenges, particularly in hiring IT system developers to expedite key IT projects, such as those focused on tax crimes and a VAT audit system. Support from FAD in enhancing DNRE's administrative autonomy and discussions about the introduction of a revenue authority are positive strides towards bolstering the entity's capacity. Moreover, it is important to address tax arrears from SOEs, which comprise 24 percent of the total.

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[1] Coelho, Maria; Rafael Garcia, Fernando Peláez and Ricardo Varsano (2023). Racionalização de Benefícios Fiscais e Criação de Unidade de Política Tributária. FAD TA Report.

Text Table 4. Cabo Verde: Sources of Financing for 2023–25
(Millions of CVE)

	2023		2024		2025	
	Millions of Escudos	Percent of GDP	Millions of Escudos	Percent of GDP	Millions of Escudos	Percent of GDP
Total financing needs	10,194	4.0	9,839	3.6	6,653	2.3
Financing sources	10,194	4.0	9,839	3.6	6,653	2.3
Domestic Financing (Net)--Issuance of treasury securities[1]	(214)	(0.1)	(636)	(0.2)	(513)	(0.2)
External financing (Net)	10,408	4.0	10,475	3.8	7,165	2.4
Disbursements	21,014	8.2	20,193	7.4	17,026	5.8
Of which budget support	11,477	4.5	11,468	4.2	7,930	2.7
IMF	2,744	1.1	3,330	1.2	2,727	0.9
Of which RSF			2,121	0.8	1,062	0.4
World Bank	4,487	1.7	4,633	1.7	5,249	1.8
African Development Bank	2,205	0.9	1,653	0.6	2,205	0.8
Program and project loans	7,686	3.0	8,284	3.0	8,467	2.9
JICA	1,077	0.4	2,125		3,457	1.2
OFID	1,621	0.6	357	0.1		
World Bank	2,531	1.0	4,543	1.7	3,527	1.2
BADEA	897	0.3	706	0.3	510	0.2
Kuwait	356	0.1	2	0.0		
SDR						
Other	1,203	0.5	551	0.2	972	0.3
Onlending loans	1,851	0.7	441	0.2	628	0.2
African Development Bank						
Amortization	10,606	4.1	9,718	3.5	9,861	3.4

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.

B. Reduce Fiscal Risks from Public Enterprises and Improve Their Financial Management

14. Steady progress on SOE reforms remains critical for reducing fiscal risks and improving services. SOEs present a major risk for budget resources and financing needs (Box 3). Important recent reforms include quarterly publications on fiscal risk analysis ("health check") and SOE budget execution, and recently the launching of the SOE Manager platform where the financial data of the majority of SOEs are available in real time. The authorities improved the SOE report to include an evaluation of performance against medium-term plans and data on the financial flows between the government and SOEs on an individual and aggregate basis (SB, end-July 2023). Staff emphasized that reforms of the six major SOEs need to move forward steadily, as the SOEs "health-check" indicates continued risk.

15. The authorities continue to plan to restructure around nine SOEs in the period 2023–26. The restructuring process includes privatization, partial sale, concessions, and PPPs, covering water and electricity, naval services, ports, telecom, and air transportation (including the government's support strategy for Cabo Verde Airlines). Other reforms include: i) preparing to broaden public debt coverage to include domestically guaranteed SOE debt (see DSA); and ii) leveraging assistance from FAD to continue improving the framework for PPPs in the context of broader PIM reforms and the reform measures under the RSF. The coverage of fiscal risk reporting will be broadened to cover PPPs (**proposed new SB, end-September 2024)**. A forthcoming World Bank report on international and inter-island connectivity could provide strategic guidance to the authorities plans in the transport sector. The delayed privatization of public enterprises in the banking and pharmaceutical sectors is expected in 2024.

Box 3. Fiscal Support to SOEs

Recent improvements in data availability are a key step to enhance SOE's risk assessment and policy design. In October 2023, the MoF launched the SOE Manager, an IT platform developed with the support of the WB and IMF that will allow for the monitoring and evaluation of the SOE sector's performance by automating data collection, processing, and analysis. The new dashboard provides important data for properly designing further reforms to reduce the support of the central government to SOEs through explicit subsidies, new guarantees, on-lending, and capitalization (Table 1).

Explicit subsidies to SOEs have increased after the pandemic. At end-2022, these subsidies reached 0.2 percent of GDP and are budgeted to increase to 0.4 percent in 2023. This is due to compensation to: i) the inter-island transportation company, and ii) energy/water SOEs to implement the social tariff for energy and water targeted at poor households.

Fiscal risks from SOEs' domestically guaranteed debt have grown over time. Before the pandemic, the stock of SOEs' domestically guaranteed debt remained stable, but there were significant transactions below the line to SOEs via on-lending and capitalization. After the pandemic, the stock of SOEs' domestically guaranteed debt jumped to about 8 percent of GDP, while quasi-fiscal flows decreased. The DSA for Cabo Verde captures the flows stemming from quasi-fiscal operations, while the stock of SOEs' domestically guaranteed debt is captured only through the contingent liability shock.

The combined fiscal support via on-lending and capitalization was an average of about 2.4 percent of GDP during 2015-2022. On-lending loans to SOEs totaled on average of around 1.4 percent of GDP that were mainly channeled to Electra and TACV. Capitalization flows, in turn, were on average about 1 percent of GDP mainly directed to back TACV.

Further improvements in the strategy to reduce the fiscal support to SOEs are welcome. Currently, authorities are focusing on a bottom-up approach by revising the business plan of key SOEs to increase their profitability. For example, capitalization expenditures to support TACV are projected to cease in 2025 reflecting the current company business plan which aims to increase routes. However, additional efforts to speed up the privatization agenda and improve the financial performance of loss-making enterprises are needed to reduce the fiscal support to SOEs.

Table 1. Cabo Verde: Fiscal Support to SOEs

Stock of SOE Guaranteed Debt (Percent of GDP)	2015	2016	2017	2018	2019	2020	2021	2022
Domestic Debt (A)	5.4	5.5	5.7	5.5	6.3	8.5	9.8	8.5
External Debt (B)	0.4	0.3	0.9	0.8	0.2	0.9	1.2	0.9
Total SOE-Guaranteed Debt (A+B)	**5.8**	**5.8**	**6.6**	**6.3**	**6.4**	**9.4**	**11.0**	**9.4**
Flow of fiscal support for SOEs (Pecent of GDP)	2015	2016	2017	2018	2019	2020	2021	2022
Explicit subsidies (C)	0.1	0.1	0.0	0.1	0.0	0.1	0.1	0.2
Total flow above the line (C)	**0.1**	**0.1**	**0.0**	**0.1**	**0.0**	**0.1**	**0.1**	**0.2**
Net increase in domestic guarantees (D)		0.1	0.2	-0.2	0.7	2.2	1.3	-1.3
Net increase in external guarantees (E)		0.0	0.6	-0.1	-0.6	0.8	0.3	-0.3
On-lending loans (F)	2.3	2.5	2.1	0.7	1.7	0.9	0.7	0.5
Capitalization (G)	0.8	0.8	0.6	1.9	2.0	0.4	0.4	1.2
Total flow below the line (D+E+F+G)	**3.1**	**3.3**	**3.5**	**2.4**	**3.8**	**4.3**	**2.7**	**0.0**
Total Flow of fiscal support for SOEs (C+D+E+F+G)	**3.2**	**3.4**	**3.5**	**2.4**	**3.9**	**4.4**	**2.7**	**0.2**

Source: Cabo Verdien authorities and IMF staff calculations.

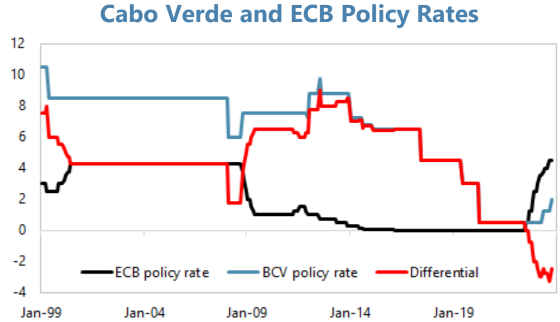
C. Modernize the Monetary Policy Framework and Improve Resilience of the Financial System

16. Monetary policy is focused on safeguarding the peg and improving the policy framework. The conventional fixed peg exchange regime continues to provide a stable anchor for monetary policy and has helped maintain external buffers. The recent hikes in the policy rate were appropriate given the interest rate differential with the Euro area and the need to mitigate the risks associated with a potential outflow of currency (Box 4). The BCV noted that it carefully monitors the ECB stance and inflation in the Euro zone. It is targeting greater convergence of policy rates over the medium-term, while also considering the moderation of real growth rates in Cabo Verde, slowing inflation and the impact of macro prudential policy tightening from the end of the moratorium. The BCV agreed it should be vigilant to signs of inflation and pressures on reserves, and stands ready to tighten as required to support the peg.

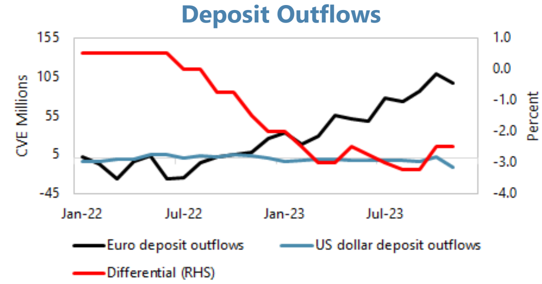
Box 4. The Negative Interest Rate Differential and Exchange Rate Peg

Cabo Verde adopted a fixed exchange rate regime with the euro in 1999. The Banco de Cabo Verde (BCV) is tasked to ensure convertibility of the Cabo Verde Escudo (CVE) and to create conditions for price and financial stability. The BCV protects the credibility of the exchange rate regime by targeting a level of international reserves in the range of 5 to 5½ months of prospective imports that is sufficient to ensure the short-term coverage of external liabilities.

Cabo Verde and ECB Policy Rates



Interest Rate Differential and Foreign Currency Deposit Outflows



The BCV policy rate differential with the ECB has been negative since October 2022 and this coincided with foreign exchange outflows in search for yield/returns, especially in euro denominated assets, as shown above.

The foreign currency outflows reduced international reserves, although they remain adequate and are projected to remain at 5.5 months in the medium term. Excess reserves and the liquidity ratios in the banking sector remain high and the financial system is sound and resilient. Emigrant deposits which are an important source of foreign currency remain on an upward trend although a persistent wide negative interest rate differential poses a risk to further inflows.

17. Structural reforms are focused on strengthening the monetary policy transmission mechanism and enhancing analytical capacity to monitor the economy. BCV has benefited from Fund CD support in developing instruments to better manage the money market and improve the communication process. Other reforms in progress include strengthening the payment systems, introduction of composite indicators of economic activity (end-June 2023 SB), establishing monthly High Frequency Indicators and other reform to strengthen near-term forecasting, implementation of central bank digital currency, and developing a framework for the provision of emergency liquidity assistance. The authorities continue to improve the supervisory oversight. Staff emphasized that the BCV standards for prudential provisioning should be tightened in line with a recent AFW2 CD report. SOE lending presents risks in the financial sector.

18. The authorities agreed with staff to continue working with banks to facilitate resolution of NPLs. Following the unwinding of COVID-19 related credit and liquidity measures, the BCV conducted a study of loan loss provisions covering the majority of the banking sector and based on this instructed some banks to strengthen provisioning. In this context, staff urged the BCV to continue developing detailed reporting templates for restructured/rescheduled loans and NPL monitoring, the implementation of foreclosure regulations, and working with banks on legacy NPLs resolution mechanisms.

19. The authorities continue to advance reforms on financial inclusion and the digitalization agenda. The pandemic triggered the use of mobile payments and internet banking services with the potential to broaden the use of financial services all over the country. Other activities in the authorities' strategy that can lead to scaling up digital financial services include the upgrade of the payment systems, interoperability of instant payments, and strengthened security regulations.

20. The authorities are working to address weaknesses in the AML/CFT framework and address the FSSR recommendations. Staff encouraged the BCV to continue to improve the AML/CFT framework, in line with the recommendations of the 2019 Inter-Governmental Action Group against Money Laundering in West Africa (GIABA) mutual evaluation report (MER). The discussions also followed up on Cabo Verde's 2023 National Strategy for Preventing and Combating ML/TF/PF (ENCAVE), which contains plans relating to updating the AML/CFT framework to include virtual assets and customer due diligence obligations for DNFBPs. Regarding the responsibility of the BCV AML/CFT framework to include virtual assets, and in line with the recommendations of the FATF, in particular Recommendation 15, a bill was approved by parliament in June. This law regulates the provision of services with virtual assets and gives BCV the responsibility for regulation and supervision in matters of AML/CFT to entities that carry out activities with virtual assets. Furthermore, the law stipulates that the creation of digital banks depends on the authorization of BCV and that they are subject to compliance with the same duties applicable to conventional banks. As for the DNFBP's, the authorities continue to work with partners to build capacity for sectoral risk assessment.

21. The government should submit to parliament amendments to the Organic Law of the BCV in line with the 2022 safeguards recommendations. Draft amendments, developed with support from Fund staff, were submitted to the Ministry of Finance, in December 2022, that, inter alia, strengthen the BCV's decision-making structure, autonomy, accountability and transparency. Discussions on the Law's submission to parliament are ongoing and the authorities agreed to continue to engage with Fund staff on the outstanding safeguards recommendations prior to submitting amendments to parliament **(proposed new SB, end-July 2024**). Separately, while the BCV has implemented some key safeguards recommendations, including the adoption of International Financial Reporting Standards as its accounting framework and approval of a revised internal audit charter that strengthens the functions independence, progress on other recommendations (e.g., on strengthening IFRS capacity, fully operationalizing the risk management function, and finalizing the ELA framework in line with IMF TA) has been slower.

D. Raise the Growth Potential and Increase Climate Resilience

22. The authorities shared the view that structural reforms and policies should mitigate the scarring effects of the pandemic while building resilience to different protracted shocks, including climate change. To this end, key priority areas in the new five-year development strategy include: (i) completing SOE reforms; (ii) facilitating access to finance; and (iii) improving the business environment. In the last few years, the authorities have advanced a set of reforms to improve the business environment, mainly directed to the SMEs. Discussions focused on plans to promote private sector-led economic diversification with the aim of supporting quality investments, employment and enhanced productivity. Efforts to reduce the high costs of finance, electricity (including through RSF supported reforms), and transport which are major impediments to private sector growth, should continue.

23. The government will continue providing financial support to vulnerable households. Social spending will be aided by funding from the social protection fund financed by the tourism tax. In addition, steps are being taken to enhance the targeting regime to improve the effectiveness and reach of the social support framework, when dealing with policies related to climate-related reforms.

RSF Arrangement

24. Climate change poses risks to Cabo Verde’s macroeconomic, fiscal, and social development. Cabo Verde faces development challenges from multiple structural factors, including insularity, territorial discontinuity, fragility of ecosystems, and scarcity of natural resources, namely water and arable land. The resulting reliance on external provision of key resources, including food and energy, exposes the country to global market fluctuations, which affect especially the vulnerable and poor. Climate change implications are amplifying these development challenges, placing an energy-water-climate nexus at the center of policy and development considerations. For example, Cabo Verde recently experienced a multi-year drought that severely weakened the agriculture sector and created challenges in maintaining a reliable supply of water, which impacted livelihoods and the tourism sector, the main pillar of the economy and driver of economic growth. The tourism sector, which is mainly concentrated in the coastal areas is also particularly sensitive to slow-onset climate change, i.e., by sea level rise. To address these issues, Cabo Verde has put climate change adaptation and mitigation at the center of its sustainable development strategy with comprehensive and coordinated energy and water sector reforms playing a critical role for mitigation and adaptation and long-term sustainability (see Annex III).

25. The RSF will support the government's effort to implement macro-critical climate reforms and catalyze private finance for climate adaptation, and transition. While recognizing the uncertainty that comes with attempting to quantify long-term costs of uncertain events and, even more, the long-term benefits of proposed reform measures (RMs), the RSF will focus on: (i) strengthening climate change policy governance; (ii) improving physical and fiscal resilience; (iii) strengthening mitigation and resilience through energy efficiency and transition; (iv) promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts; and (v) financial sector resilience to climate change (Table 11).

Reform Area 1. Strengthen Governance of Climate Change Policy

26. The coordination of climate change related policies and disaster risk management could be improved. The Climate Policy Diagnostic (CPD) noted that these functions require strong leadership and cross-government coordination, which is best provided by a coordination function at the level of the Council of Ministers[3] (**RM1**). This function could promote awareness of the implications of climate change, ensure cross sectoral consistency of climate change related policies, and provide for the strategic coordination of disaster risk management (DRM) to build resilience and to manage climate change related challenges effectively. Staff stressed that strategic communication with the population will be an important task to ensure social buy-in. The government has taken important steps towards sectoral planning, however more is needed to ensure the cross sectoral consistency of climate change related policy measures and the effective mitigation of, and response to, climate-related hazards.

Reform Area 2. Improve Fiscal and Physical Resilience to Climate Change

27. The RSF will aim to resolve gaps in fiscal risk analysis and in the climate resilience of the public investment management system. The C-PIMA identified that climate change considerations are not adequately integrated into the public investment planning process. There is a need to improve awareness of climate-related risks in fiscal planning (**RM2**). The latest WB DPF loan (1st in a series of three) of USD 25 million is focused on creating fiscal space and enabling sustainable growth towards the green and blue economy. The loan has conditions that support improved PIM and the RSF will complement to ensure that better risk analysis and investment planning are also applied to PPPs, thus playing a catalytic role in attracting climate finance **(RM3**). The RSF will also strengthen the financing framework for achieving climate mitigation and adaptation objectives including by developing the pipeline of public projects that result in climate-resilient structural change (**RM4**).

Reform Area 3. Strengthen Mitigation and Resilience Through Energy Efficiency and Transition

28. Energy efficiency and transition will support mitigation goals, resilience and, through

[3] In Cabo Verde at the Cabinet level there is a body called "Chefia do Governo" (in Portuguese). This is a body composed by the Prime Minister, the Vice-Prime Minister and two Ministers.

the link to water, adaptation. More than 80 percent of electricity generation relies on imported fossil fuels products, and the majority of the GHG emissions come from the energy sector. This also represents a fiscal risk as the government shields households from the effect of pass-through costs. However, Cabo Verde has potential from renewable energy sources (RES). The energy transition will: (i) contribute to emission reduction and the attainment of Cabo Verde's NDC objectives; (ii) allow for a cost-efficient response to growing energy demand from the desalination reliant water sector; and (iii) yield favorable long-term impacts in its balance of payments as fossil fuel imports decline. In turn, the energy transition will require: (i) substantial public investment in electricity grid infrastructure to build the capacity for higher RES in the electricity mix; and (ii) market conditions that encourage private investment in energy production. The RSF will support energy efficiency, facilitate the upgrading of network infrastructure, and promote the development of appropriate market conditions. The RSF will ensure resources for infrastructure investment, which together with reforms will prepare the electricity system for the onboarding of more RES, a precondition for private investment in RE capacity (**RM5**). The authorities, with support from the WB, are taking important steps to unbundle the energy sector. FAD CD can support the design of tariff reforms including distributional impact analysis of policy measures in this field.

Reform Area 4. Promote Adaptation by Ensuring Ecological and Economic Sustainability of Water Resources and Planning for Long-run Climate Impacts

29. Cabo Verde faces water shortages and climate related threats amplify water scarcity and pose a challenge for, and risk to, water availability and quality. The RSF will support efforts to address these challenges by improving the efficiency of water use and provision and by expanding water sourcing. Cabo Verde has a long history of using desalination for freshwater production and uses this technology to address the increasing demand for water in light of declining freshwater resources. Inefficiencies in water distribution and management cause significant technical and commercial losses, which amount on average to about 50 percent of the total fresh water entering the system. Several of the publicly owned water operators are running operational losses and/or have negative equity. The RSF aims at promoting the efficient use of water resources and improved adaptation to climate change, ensuring resources for implementing investments that enhance resilience to climate change impacts, including droughts, by reducing technical losses and increasing water supply through desalination. It also aims to improve the financial sustainability of the public utilities (**RM6**). While part of the infrastructure related cost of water service provision might be funded transparently from the budget, to mitigate the potential adverse implications of water sector reforms and energy transition, as well as the impact of climate hazard events on the poor and vulnerable, the social safety net (SSN) will be strengthened (**RM7**). The WB has been assisting the authorities with strengthening the SSN.[4]

30. Effective preparation for climate change implications also requires good information regarding what to expect. The RSF will enable investment decisions based on reliable information on climate change related risks, such as sea level rise, through the definition

[4] The tariff reforms can be equity-enhancing by themselves, and a distributional impact assessment will be done using current household budget survey (the CPAT assessment undertook an illustrative distributional assessment using the 2001 HBS, as the latest HBS was not made available and is incomplete).

and sharing of climate scenarios relevant to Cabo Verde and hazard vulnerability maps that include potential climate related hazards consistent with the climate scenarios (**RM8**).[5] Understanding climate related risks will reduce information uncertainty, lowering the risk premium required by investors and helping to avoid underinvestment in sectors such as tourism. Considering climate related risks in the context of land planning and building design will reduce the physical damage of climate hazards and thereby contain the economic cost of adverse climate events.

Reform Area 5. Financial Sector Resilience to Climate Change

31. The RSF aims to support steering private finance towards a low-carbon climate-resilient economy, while strengthening financial sector resilience to climate-related risks. Given the strong role of the banking sector in Cabo Verde, this will include the adoption by the BCV of guidelines to monitor banks' assessment and disclosure of climate-related risks and opportunities (**RM9**). Enhancing the financial sector's capacity to manage climate change risks is crucial for Cabo Verde, given that it is a tourism-dependent small island state where climate events could easily escalate. Proposed reforms include the design of a climate information architecture for banks (taxonomy and climate disclosures) and promote climate resilience among financial institutions. These could be the foundation to unlock private sector climate financing and laying out robust foundations for scaling up private climate finance, in line with the messages in the Global Financial Stability Report (October 2023). The recent debt-for-financing swap agreement with Portugal could provide seed money for a Climate and Nature Fund. It will be important to ensure that Fund is a subaccount in the Treasury and develop the financial regulations for the transparent governance and use of those resources.

32. The proposed RMs reflect the recommendations of analytical and diagnostic work from both the IMF and the WB. Discussions with the authorities regarding the formulation of RSF reform measures were guided by recent diagnostics, including the C-PIMA and the 2017 Climate Change Policy Assessment (CCPA), and the 2021 NDC also provided key inputs (see Table 12).

PROGRAM ISSUES AND RISKS

33. Performance under the current ECF program has been strong. All quantitative performance criteria (QPCs) for end-June 2023 were met (Text Table 5). The indicative targets (ITs) for end-March and end-June 2023 were met. Regarding structural benchmarks (SBs) (Text Table 6), the authorities met the ones for end-June, end-July, and end-September 2023. The ECF will expire in June 2025. A new set for end-December 2024 PCs and end-September 2024 ITs is proposed. The authorities request the modification of the PC on the PV of new external debt for end-December 2023 reflecting the latest World Bank disbursement schedule.

[5] The work on climate scenarios and maps is ongoing and once the council is in place, it will officially cover the matter.

They also requested a clarification of the definition of government deposits under *other net liabilities* in the TMU (from a stock to a flow), and a modification of the PC on *other net liabilities* in December 2023 and June 2024 to reflect the delay in privatization receipts from 2023 to 2024. The privatization proceeds, which are uncertain, entered net other liabilities as a positive flow. Staff are supportive of these changes.

Text Table 5. Cabo Verde: Performance Criteria and Indicative Targets for end-June 2023[1]

(Billions of CVE; cumulative from the beginning of the year, except where otherwise indicated)

	End-June 2023			
	PC/IT	PC/IT with adjuster	Actual	Status
Quantitative performance criteria				
Primary balance, floor [2]	-4141		2759	met
Tax revenue, floor	19095		24670	met
Net other liabilities, floor [3]	-625		593	met
Net domestic financing, ceiling	5886		1728	met
Nonaccumulation of domestic arrears [4]	0		0	met
Non-accumulation of external payment arrears [4]	0		0	met
PV of new external debt, ceiling (in millions of US Dollars)	60		24	met
Nominal level of new nonconcessional external debt of central government, ceiling [4]	0		0	met
Gross international reserves (in millions of euros), floor [2]	572		626	met
Indicative Targets				
Social spending, floor	6180		6982	met
Non-quantitative continuous PCs				
Non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions				met
Non-introduction or modification of multiple currency practices				met
Non-imposition or intensification of import restrictions for balance of payments reasons				met
Non-conclusion of bilateral payments agreements that are inconsistent with Article VIII				met
Memorandum items:				
Net onlending	827		47	
Capitalization	765		1366	
Program assumptions				
Project and budget support grants	623		1206	
External debt service	6445		3420	
Sales of assets	517		97	
Project and budget support loans	5888		5591	

Sources: Cabo Verdean auhtorities; and IMF Staff

[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.

34. Additional conditionality is proposed (Table 7). New SBs aimed at keeping the medium-term fiscal path on track and advancing governance at the BCV are proposed. These are: i) a SB for end-September 2024 aimed at broadening the coverage of fiscal risk analysis and reporting to include PPPs; and ii) a safeguards linked SB with the submission of the BCV organic law to parliament for end-July 2024.

35. Proposed access. Cabo Verde is eligible for the RSF and belongs to Group A. The access level is proposed at 100 percent of quota (SDR 23.7 million or about $31.7 million), for an 18-month duration, based on the package of RMs in Table 11. The RSF arrangement will help the authorities implement macro-critical climate reforms and catalyze private finance for climate adaptation, and transition. This access is based on staff's assessment that: i) the reforms proposed under the RSF are strong; and ii) Cabo Verde's debt is sustainable, with adequate capacity to repay (see below), and the concurrent ECF is underpinned by high-quality policies. The reform measures are closely related with policy reforms and investment plans under the country's NDC. The authorities have strong ownership of reforms in the ECF, which is a positive institutional foundation to support a successful RSF.

Text Table 6. Cabo Verde: Structural Benchmarks Up to September 2023

Actions	Target date	Objective	Status
Fiscal reforms			
Publish annual budget execution reports for the general government.	End-September 2023	Improve fiscal transparency	Met
SOE Reforms			
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 reduce fiscal risks	Met
Monetary policy reforms			
Introduce a composite indicators of economic activity.	End-June 2023	Support monetary policy analysis	Met

36. Use of RSF resources. RSF disbursements increase external financing by about CVE 2.1 billion in 2024 and 1 CVE billion in 2025 (Text Table 7). The RSF substitutes more expensive domestic financing with cumulative estimated savings in debt service of 0.7 percent of GDP until 2028. These savings will help build buffers and make Cabo Verde more resilient to climate-related shocks.[6] They will also create fiscal space, including to support critical climate-related public investment. From the balance of payment standpoint, RSF disbursements increase international reserves by the disbursement amounts in 2024 and 2025, respectively (Text Table 8).

Text Table 7. Cabo Verde: RSF Fiscal Table
(Millions of CVE and Euros)

	2024		2025	
	CVE	Euros	CVE	Euros
Total revenue and grants	**75,720**	**687**	**76,414**	**693**
Total expenditure	85,001	771	82,665	750
Net Purchase of Non-financial assets for Investments:	10,770	98	11,806	107
Other expenditures	74,231	673	70,859	643
Fiscal Balance	**-9,281**	**-84**	**-6,251**	**-57**
Other liabilities (including onlending, capitalization, and use of deposits)	**-558**	**-5**	**-401**	**-4**
Financing needs	**9,839**	**89**	**6,653**	**60**
Net External Financing	**10,475**	**95**	**7,165**	**65**
Disbursement	20,193	183	17,026	154
Prospective Financing from multilaterals	11,468	104	7,930	72
IMF ECF	1,208	11	606	5
Budget support loans (Multilateral exc. IMF)	8,139	74	6,262	57
RSF financing	2,121	19	1,062	10
Loans for onlend	441	4	628	6
Project loans	8,284	75	8,467	77
Amortization	9,718	88	9,861	89
Net Domestic Financing (after refinancing)	**-636**	**-6**	**-513**	**-5**
Total Financing	**9,839**	**89**	**6,653**	**60**
Change in government assets	**0**	**0**	**0**	**0**
of which RSF	0	0	0	0

[6] An MoU between the MoF and BCV will detail the institutional arrangements.

37. The Fund-supported program continues to be fully financed (i.e., there are firm commitments for the next 12 months, and good prospects the financing will be adequate for the remainder of the program). In addition to Fund support, financing in the second and third year of the ECF is being provided through budget support from development partners and multinational development institutions, including the World Bank and the African Development Bank. Through the Global Gateway, the EU and European Investment Bank (EIB) recently announced significant support for Cabo Verde, although the phasing is still not finalized.

Text Table 8. Cabo Verde: RSF BoP Implications Table

(Millions of CVE and Euros)

	2024		2025	
	CVE	Euros	CVE	Euros
Current account	**-16760**	**-152**	**-18350**	**-166**
Goods and services	-65064	-590	-67262	-610
Primary and secondary income	48304	438	48912	444
Capital and Financial Account 1/	**-5462**	**-50**	**-4334**	**-39**
Overall balance 2/	-2353	-21	-4996	-45
Financing	-2353	10	4287	39
Change in reserves (-: increase, excl. RSF)	-5120	-46	-1693	-15
Loans (Multilaterals excl. IMF)	6262	57	5980	54
Financing Gap	-1210	-11	-616	-6
Use of ECF	1232	11	616	6
Residual Gap	0	0	0	0
Use of Fund credit: RSF	2121	19	1062	10
Change in reserves (-:= increase, incl. RSF)	-8473	-77	-3371	-31
Memorandum items				
Gross reserves (incl. RSF)	87568	794	90323	819
Gross reserves (excl. RSF)	85447	775	89261	810

1/ Not considering financing from multilaterals
2/ Considering the net impact of RSF above and below the line items

38. Cabo Verde's capacity to repay the Fund is assessed as adequate (Table 8). Fund credit outstanding will peak at 380 percent of quota by 2025. Credit outstanding would peak at about 4.1 percent of GDP, 13.4 percent of gross international reserves, and 11.8 percent of exports by 2025. At the same time, annual repayments to the Fund would peak at 1.3 percent of exports, 1.8 percent of reserves, and almost 10.9 percent of PPG external debt service, all in 2029.

Text Table 9. Cabo Verde: External Financing Gap 2020-25

(Millions of Euros, unless otherwise specified)

	2020	2021	2022	2023	2024	2025
Current account balance	**-246**	**-206**	**-79**	**-138**	**-152**	**-166**
Balance of goods and services	-513	-547	-433	-530	-590	-610
Exports of goods	113	151	269	261	283	324
Imports of goods	692	753	1013	1082	1167	1241
Exports of services	258	193	490	522	568	609
Imports of services	192	139	178	230	274	301
Balance on primary income	-36	-24	-27	14	26	11
Balance on secondary income	303	365	381	378	412	433
Financing						
Capital account	22	23	21	51	41	41
Financial account, net[1]	-23	-37	-25	-88	-90	-81
Direct investment, net	-55	-78	-105	-100	-102	-104
Portfolio investment, net	0	1	1	1	1	1
Other investment, net	-100	-85	-5	-90	-77	-47
Net acquisition of financial assets	-18	54	32	4	4	5
Net incurrance of liabilities	-49	14	-46	-7	-23	-20
Monetary Authority	-1	0	0	0	0	0
Central Government	101	93	44	108	95	65
Disbursements 1/	141	133	82	191	183	154
Amortization	-41	-39	-38	-83	-88	-89
Exceptional financing	0	0	0	0	0	0
Commercial Banks	4	49	15	7	7	8
Non-bank flows	-21	-4	-21	-21	-21	-21
Errors and ommisions/2	-5	31	-28	0	0	0
Overall balance	-206	-115	-60	1	-21	-45
Financing	206	115	45	-26	10	39
Change in reserves (-:=increase, excl. RSF)	75	-10	-25	-102	-46	-15
Loans (Multilaterals excl. IMF)	131	124	70	76	57	54
Financing gap	0	0	-14	-25	-11	-6
Use of ECF	0	0	14	25	11	6
Residual Gap	0	0	0	0	0	0
Use of Fund credit: RSF	0	0	0	0	19	10
Change in reserves (-:= increase, incl. RSF)	75	-10	-39	-127	-77	-31
Memorandum Items:						
Targeted reserves path as months of prospective imports	7.8	6.0	5.7	6.1	6.2	6.0

Source: Authorities and IMF staff estimates.
1/Includes reserves and exceptional financing.
2/ Including banks' delays on trade credits reporting.

39. Risks to the program are assessed as moderate. The worsened global outlook and ongoing effects of the spillovers from the war in Ukraine increase risks to the program. Also, the high risk of overall debt distress remains a concern. Policy responses to materialization of risk are set out in the RAM (Annex 1). Mitigating factors to the worsened outlook are the authorities' strong track record under the previous Fund-supported programs and the current ECF, which shows strong program ownership.

STAFF APPRAISAL

40. Cabo Verde continues its strong macroeconomic performance in 2023 and the near-term outlook is favorable despite some downside risks. Tourism arrivals have surpassed pre-pandemic levels with positive impacts in tourism-related sectors. Real growth is expected to be 4.7 percent in 2024. The level of gross international reserves is projected to reach 6.1 months of prospective imports in 2023 and to remain stable around 5.5 months in the medium term. However, the economy remains vulnerable to external shocks that impact tourism activity, as well as climate risks.

41. Inflation is decreasing but requires close monitoring. Inflation is expected to decline in 2023 and continue decelerating next year. Global food and fuel prices transfer rapidly to the economy given the heavy share of imports in consumption, thus calling for vigilance. The authorities are committed to continue supporting vulnerable groups as required.

42. Staff support the authorities' commitment to the program's fiscal consolidation path. Staff welcome the improvement in the primary balance in 2023. The 2024 budget is in line with the program. Achievement of the program's medium-term target is dependent on the authorities adhering to tax and other revenues measures. Fiscal risks from SOEs and PPPs need to be closely monitored and mitigating measures adopted. Delays in SOE reforms could undermine the credibility of the authorities' reform agenda and fiscal sustainability. Staff encourages efforts towards the continued reduction in the debt-to-GDP ratio to about 94 percent by 2028.

43. The monetary tightening was appropriate and the policy stance should remain data dependent to safeguard the peg. Staff supports the recent cautious step-wise increase in the policy rate, given the current interest differential with the ECB, while recognizing that inflation is decreasing. The BCV should remain vigilant and stand ready to tighten the policy stance as required to support the peg. Staff commends the authorities' implementation of CD recommendations to strengthen monetary policy transmission mechanisms and build analytical capacity to monitor the economy. It would be important to submit the amendments to the BCV law to parliament.

44. Staff welcomes the improvement in financial stability indicators. The financial sector remains stable from a medium-term perspective, banks' profitability has been positive, and NPLs maintained the downward trend since 2016, due to the credit recovery processes and the write-off of NPLs and prudence from the banking system. Staff urged the authorities to continue working with banks to facilitate resolution of NPLs.

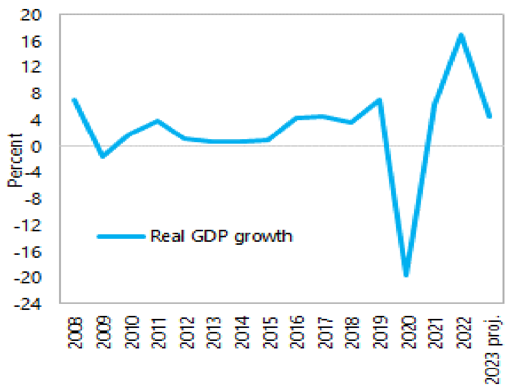
45. Decisive reforms are needed to sustain high, inclusive, and resilient growth. Moving to a post-pandemic phase, it is critical to implement reforms that will create the conditions to support the goals under the PEDS II. In this context, a clear reform agenda for the major SOEs is of the utmost importance, while creating the basis for improved connectivity among the islands, employment and social development, and a strong domestic and dynamic private sector. In this context, capital spending to accelerate investments in climate action and seeking support from partners (including the Fund) to access financing are critical at this juncture. The RSF supports a transformative reform agenda closely linked to the authorities climate change and developmental reform objectives.

46. Program performance under the ECF has been strong. All quantitative performance criteria (QPCs) for end-June 2023 were met. The indicative targets (ITs) for end-March and end-June 2023 were met. Regarding structural benchmarks (SBs), the authorities met the ones for end-June, end-July, and end-September 2023. A new set for end-December 2024 QPCs and end-September 2024 ITs is proposed. Staff support the modification of the PC on the PV of new external debt for end-December 2023. Staff also support definition of deposits under other net liabilities in the TMU as a flow variable. Under the new definition it is the use/creation of government deposits to reduce/increase borrowing needs that enters net other liabilities in line with authorities' fiscal accounts. Staff agree that privatization proceeds are uncertain with elements beyond the authorities control and support a modification of the PC on other net liabilities in December 2023 and June 2024 to reflect the delay in 2023 privatization receipts and the definitional change.

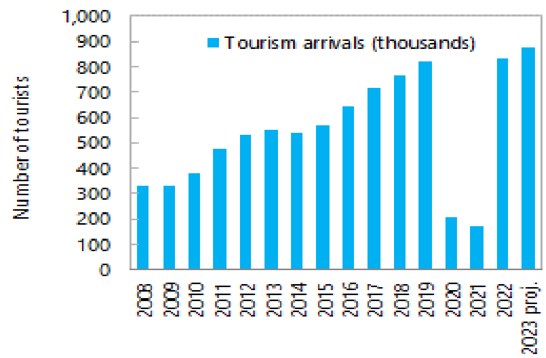
47. Staff supports the completion of the third review under the ECF arrangement and the authorities' request for an 18-month RSF. This reflects the commendable performance to tackle medium-term economic challenges and address climate risks. In view of Cabo Verde's external financing needs and the authorities' strong policy commitments, staff supports the completion of the review. In addition, Cabo Verde has presented a strong and comprehensive package of reforms to address its climate-related challenges. Staff encourages the authorities to leverage the RSF to exploit synergies with other official financing and catalyze further private financing for climate mitigation and adaptation efforts.

Figure 1. Cabo Verde: Recent Economic Developments

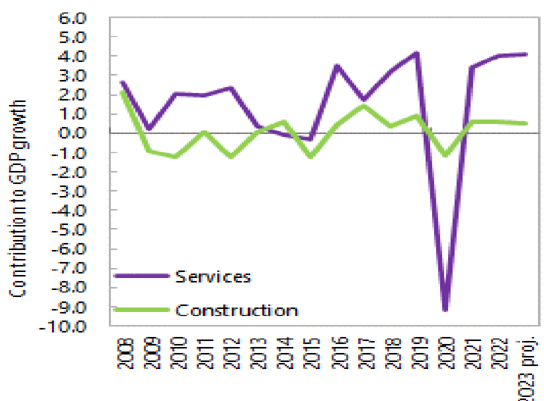
Economic growth is projected to moderate in 2023…



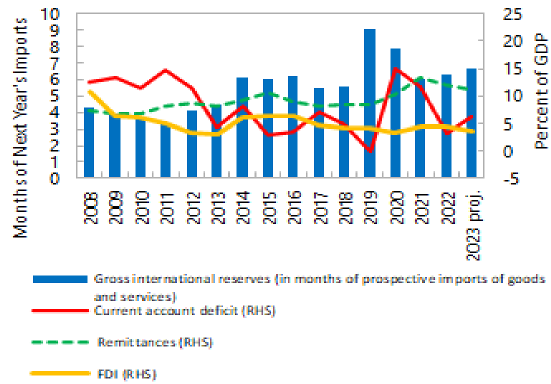
…after significant improvements in the tourism sector in 2022…



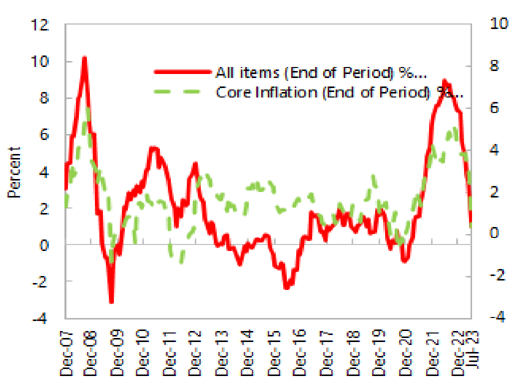
… that is expected to support activity in the services sector.



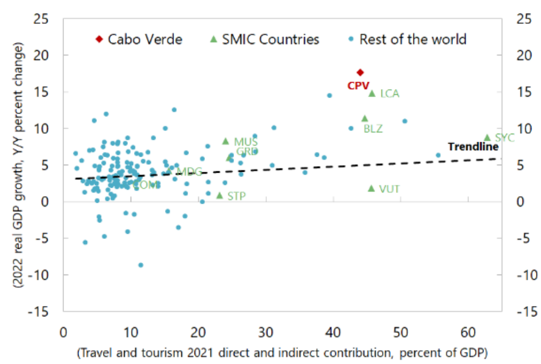
International reserves are projected to remain adequate reflecting steady FDI and higher remittances.



Headline inflation decreased due to lower food and fuel prices.



Tourism Dependency and GDP Growth – 2022.

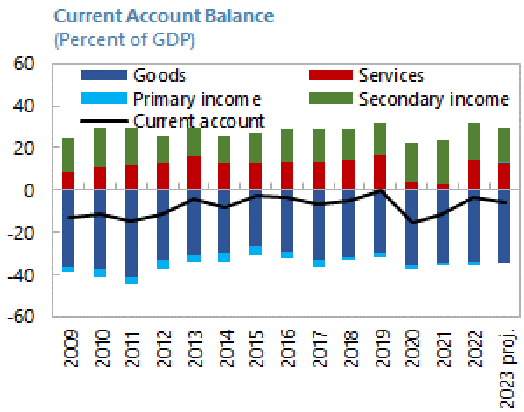


Sources: World Travel and Tourism Council and Fund staff calculations.

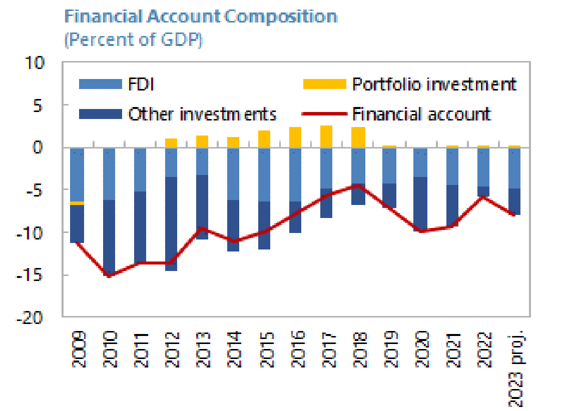
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 2. Cabo Verde: External Sector Developments

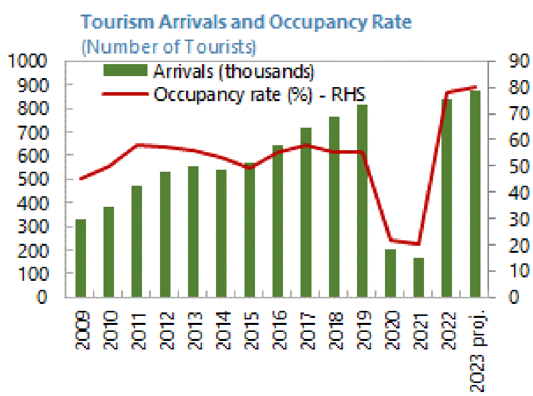
The current account deficit widens slightly in 2023 as exports slow from 2022 highs.



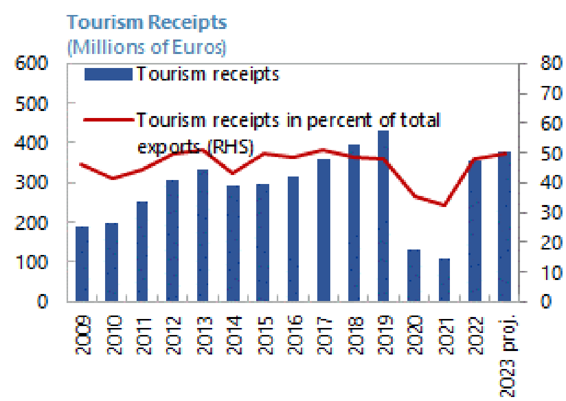
The financial account is projected to deteriorate, financed by an increase in other investments.



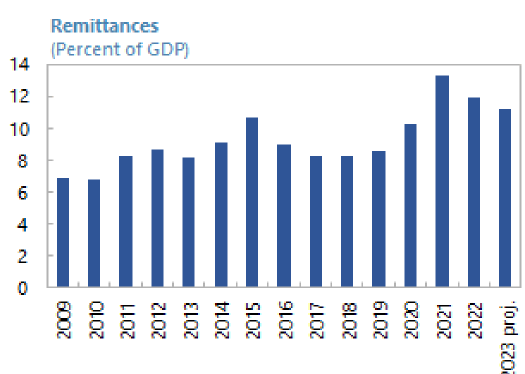
Tourism arrivals are projected to increase and remain slightly above pre pandemic levels.



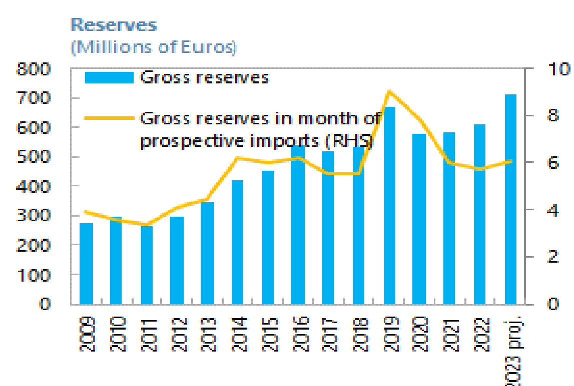
Resulting in a steady increase in tourism receipts.



Remittances are projected to decelerate in 2023 but remain an important source of foreign currency…



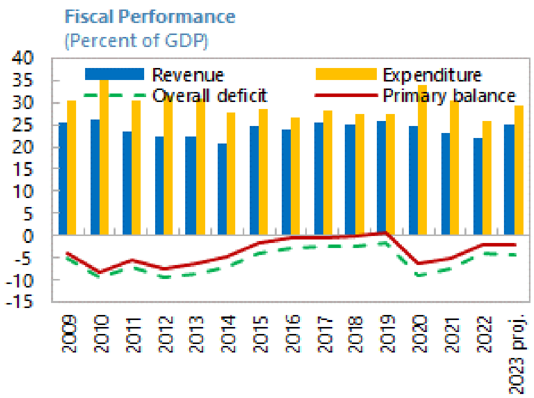
… supporting the country's strong reserve position.



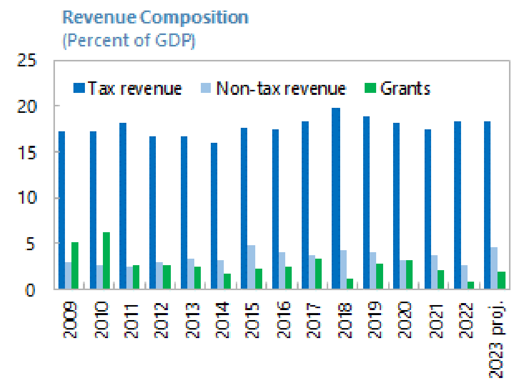
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 3. Cabo Verde: Fiscal Sector Developments

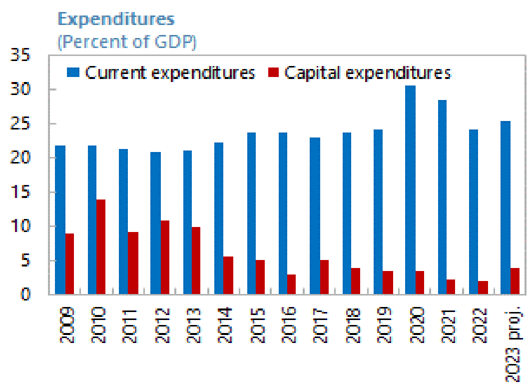
Fiscal performance is projected to stay stable in 2023 ...



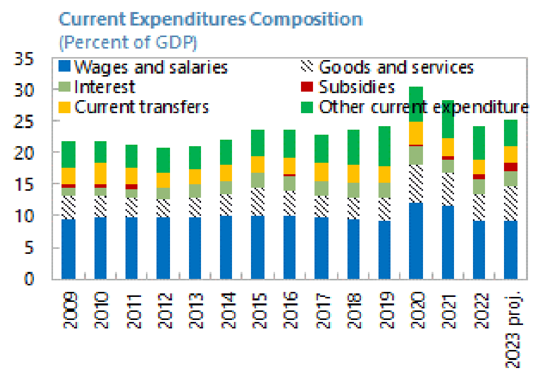
...with tax revenues expected to remain robust supported by positive economic growth.



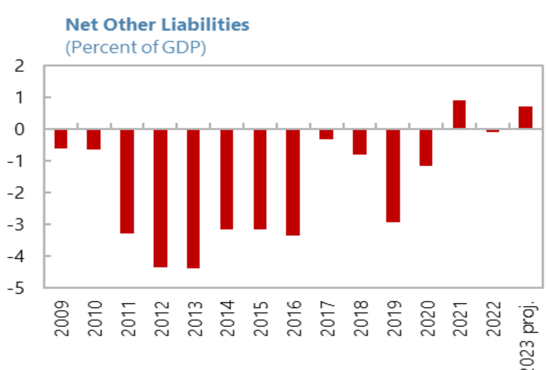
Expenditures are projected to increase on account of higher current and capital spending.



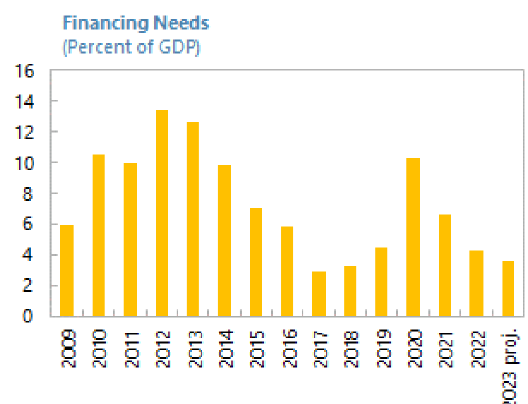
...current expenditure increases due to the expansion of good and services.



Net other liabilities are projected to improve in 2023 reflecting lower government support to SOEs.



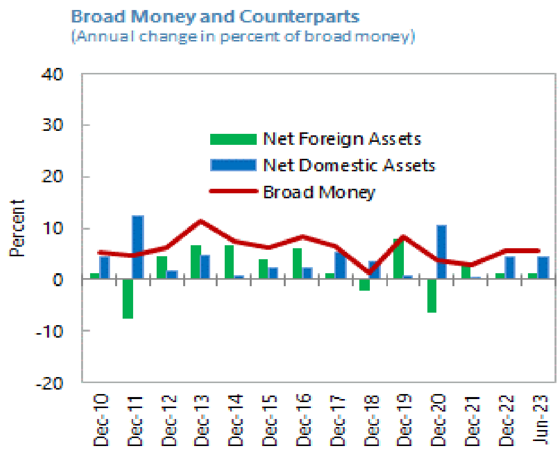
... as a result, financing needs are projected to decline.



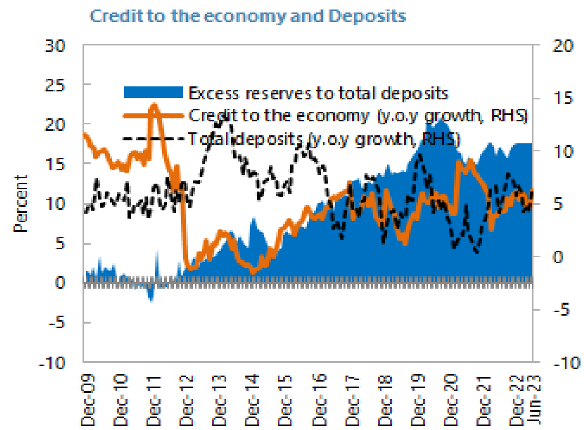
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 4. Cabo Verde: Monetary and Financial Sector Developments

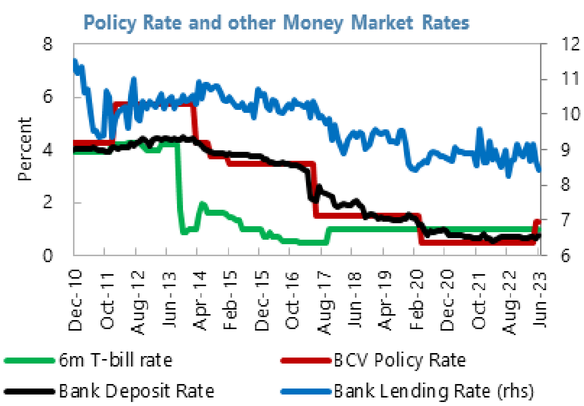
At end June 2023 broad money increased slightly due to the increase of domestic assets...



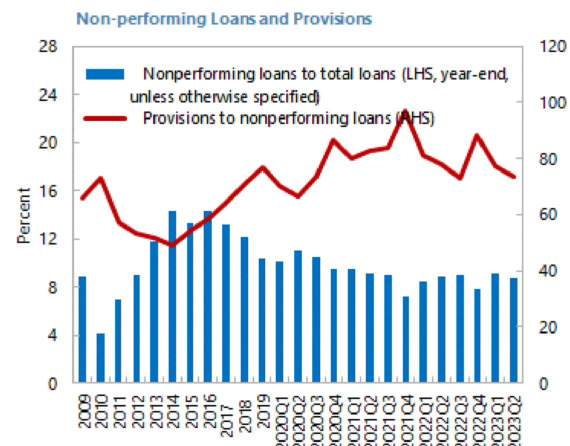
...credit to the economy increased even with the gradual phasing out of the COVID-19 relief measures.



The central bank started to adjust its policy rate, narrowing the interest differential with the ECB rates.



Nonperforming loans increased in Q2 2023, in part reflecting the gradual phasing out of the credit moratorium.



Sources: Cabo Verdean authorities; and IMF staff estimates.

Table 1. Cabo Verde: Selected Economic Indicators, 2020–28

	2020	2021	2022		2023		2024	2025	2026	2027	2028
			SR ECF 2nd review	Act.	SR ECF 2nd review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Annual percent change)										
National accounts and prices 1/											
Real GDP	-20.8	5.6	17.7	17.1	4.4	4.5	4.7	4.7	4.6	4.6	4.5
GDP deflator	0.7	-0.3	6.4	7.7	4.5	4.7	2.0	2.0	2.0	2.0	2.0
Consumer price index (annual average)	0.6	1.9	7.9	7.9	5.2	4.0	2.0	2.0	2.0	2.0	2.0
Consumer price index (end of period)	-0.9	5.4	7.6	7.6	5.2	3.0	2.0	2.0	2.0	2.0	2.0
External sector											
Exports of goods and services	-58.7	-7.5	120.6	120.6	3.7	3.2	8.7	9.5	9.4	8.7	8.1
Of which: tourism	-69.1	-16.4	225.4	225.4	7.7	6.5	10.1	8.8	9.4	8.7	8.7
Imports of goods and services	-23.2	0.8	33.7	33.7	7.8	10.2	9.8	7.0	5.4	6.0	4.9
	(Change in percent of broad money, 12 months earlier)										
Money and credit											
Net foreign assets	-6.6	2.9	1.2	1.2	3.4	4.8	2.8	0.9	0.0	0.0	1.6
Net domestic assets	10.3	0.1	4.6	4.6	4.9	4.6	4.3	4.5	4.8	4.9	3.6
Net claims on the central government	-1.3	2.4	3.1	3.1	0.8	0.0	-0.1	-0.1	0.2	-0.4	-0.6
Credit to the economy	2.9	4.2	3.9	3.9	3.9	4.5	4.4	4.5	4.5	5.2	4.2
Broad money (M2)	3.8	3.0	5.8	5.8	8.3	9.4	7.2	5.4	4.8	4.9	5.3
	(Percent of GDP, unless otherwise indicated)										
Savings and investment											
Domestic savings	8.8	28.3	41.7	34.7	18.7	21.4	18.1	17.5	13.7	10.3	12.4
Government	-7.6	-5.3	-0.4	0.8	0.5	0.2	1.1	2.4	2.5	3.1	3.1
Private	16.4	33.6	42.1	33.9	18.2	21.2	17.0	15.1	11.2	7.2	9.3
National investment	24.1	40.5	45.3	38.4	24.3	27.3	24.2	23.8	19.5	15.7	17.0
Government	3.4	2.3	1.9	1.9	4.2	3.2	3.9	4.0	3.2	3.5	3.6
Private	20.7	38.2	43.4	36.4	20.0	24.1	20.2	19.8	16.3	12.2	13.4
Savings-investment balance	-15.3	-12.2	-3.6	-3.7	-5.6	-5.9	-6.1	-6.3	-5.8	-5.4	-4.6
Government	-11.0	-7.6	-2.2	-1.1	-3.8	-3.1	-2.8	-1.6	-0.7	-0.4	-0.5
Private	-4.4	-4.6	-1.3	-2.6	-1.8	-2.9	-3.3	-4.6	-5.1	-5.0	-4.1
External sector											
External current account (including official transfers)	-15.3	-12.2	-3.6	-3.7	-5.6	-5.9	-6.1	-6.3	-5.8	-5.4	-4.6
External current account (excluding official transfers)	-18.0	-14.7	-4.9	-5.1	-5.9	-6.2	-6.9	-6.9	-6.4	-6.0	-5.1
Overall balance of payments	-4.7	0.6	1.1	1.1	3.0	4.4	2.7	0.9	0.1	0.1	1.5
Gross international reserves (months of prospective imports of goods and services)	7.8	6.0	5.9	5.7	6.1	6.1	6.2	6.0	5.7	5.5	5.5
Government finance											
Revenue	25.2	23.9	21.6	22.4	24.6	25.5	27.6	26.0	25.3	25.9	25.8
Tax and nontax revenue	21.9	21.8	20.7	21.5	22.7	23.6	25.2	24.6	24.5	24.7	24.7
Grants	3.3	2.1	0.9	0.9	1.9	1.9	2.3	1.5	0.7	1.2	1.1
Expenditure	34.5	31.6	25.7	26.7	29.0	28.9	30.9	28.2	26.4	26.3	26.4
Primary balance	-6.6	-5.4	-1.9	-2.0	-2.2	-1.1	-1.1	0.0	1.0	1.0	1.0
Overall balance (incl. grants)	-9.3	-7.7	-4.1	-4.3	-4.4	-3.4	-3.4	-2.1	-1.2	-0.4	-0.5
Net other liabilities (incl. onlending)	-1.2	0.9	-0.1	-0.1	0.7	-0.5	-0.2	-0.1	-0.1	0.0	0.0
Total financing (incl. onlending and capitalization)	9.8	6.8	4.2	4.3	3.7	4.0	3.6	2.3	1.3	0.4	0.5
Net domestic credit	3.1	1.7	2.3	2.4	1.4	-0.1	-0.2	-0.2	0.3	-0.7	-1.0
Net external financing	6.7	5.1	1.9	2.0	2.3	4.0	3.8	2.4	0.9	1.0	1.5
Public debt stock and service											
Total nominal government debt	142.6	152.0	121.2	127.1	112.6	119.9	116.2	111.2	105.4	99.4	93.9
External government debt	105.1	108.2	84.0	88.0	79.8	82.7	81.9	79.4	75.1	71.3	68.8
Domestic government debt	37.5	43.8	37.1	39.1	32.8	37.2	34.3	31.8	30.3	28.1	25.1
External debt service (percent of exports of goods and	14.8	20.2	11.5	15.2	12.4	12.3	11.9	10.9	10.5	9.8	9.1
Present value of PPG external debt											
Percent of GDP (risk threshold: 55%)	70.3	57.2	53.5	53.5	50.9	54.2	53.3	52.0	49.5	47.4	46.1
Percent of exports (risk threshold: 240%)	335.9	197.4	159.1	163.8	156.6	161.4	156.1	148.6	137.8	129.5	124.1
Present value of total debt											
Percent of GDP (benchmark: 70%)	92.4	104.3	91.3	97.1	84.0	90.8	87.5	83.7	79.9	75.6	71.2
Memorandum items:											
Nominal GDP (billions of Cabo Verde escudos)	176.8	186.2	244.3	235.0	266.6	257.1	274.7	293.4	313.1	333.9	356.0
Gross international reserves (€ millions, end of period)	582	595	626	626	699	728	794	819	823	827	875

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, 2020–28

(Millions of Euros; unless otherwise indicated)

	2020	2021	2022	2023		2024	2025	2026	2027	2028
			Act.	SR ECF 2nd review	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account	-246	-206	-79	-136	-138	-152	-166	-164	-164	-148
Trade balance	-579	-602	-744	-806	-822	-883	-918	-955	-999	-1035
Exports, f.o.b.	113	151	269	260	261	283	324	363	402	436
Imports, f.o.b.	692	753	1013	1066	1082	1167	1241	1318	1401	1471
Consumer goods	256	232	297	329	329	357	382	408	449	492
Intermediate goods	159	128	166	169	164	179	188	186	167	182
Capital goods	93	70	83	93	91	104	113	139	161	159
Others (including fuel)	185	322	468	476	498	527	558	586	623	639
Fuel	62	74	123	124	128	127	133	134	144	135
Services (net)	66	55	311	308	292	293	308	350	385	427
Receipt	258	193	490	526	522	568	609	657	706	761
Of which: tourism	133	112	363	391	387	425	463	506	550	598
Payment	192	139	178	218	230	274	301	307	321	334
Primary Income (net)	-36	-24	-27	-16	14	26	11	-4	-16	-28
Of which: interest on public debt	-15	-30	-77	-20	-14	-13	-12	-13	-14	-15
Secondary Income (net)	303	365	381	378	378	412	433	446	466	488
General Government	43	42	29	7	7	20	17	18	18	18
Other Sectors	260	324	352	371	371	392	416	428	448	470
Of which: remittances	178	232	263	270	270	279	287	299	316	336
Capital account	22	23	21	54	51	41	41	40	24	25
Of which: Grants	10	7	9	42	39	28	29	27	12	13
Financial account 1/	-23	-37	-25	-84	-88	-90	-81	-73	-90	-118
Foreign direct investment	-55	-78	-105	-100	-100	-102	-104	-107	-112	-121
Portfolio investment	0	1	1	1	1	1	1	1	1	1
Other investment	-100	-85	-5	-55	-90	-77	-47	-22	-32	-50
Net acquisition of financial assets	-18	54	32	4	4	4	5	5	5	5
Net incurrence of liabilities	-49	14	-46	60	-7	-23	-20	-28	-17	0
Monetary authority	-1	0	0	0	0	0	0	0	0	0
Central government	101	93	44	73	108	95	65	21	32	50
Disbursements	141	133	82	152	191	183	154	116	126	143
of which RCF	29	0	0	0	0	0	0	0	0	0
Amortization	-41	-39	-38	-78	-83	-88	-89	-94	-94	-94
Exceptional financing 2/	0	0	0	0	0	0	0	0	0	0
Commercial banks	4	49	15	7	7	7	8	8	8	8
Non-bank flows	-21	-4	-21	-21	-21	-21	-21	-3	-3	-3
Errors and omissions 3/	-5	31	-28	0	0	0	0	0	0	0
Overall balance	-206	-115	-60	3	1	-21	-45	-51	-50	-5
Financing	206	115	45	-28	-26	10	39	51	50	5
Reserve assets excl RSF (-:=accumulation)	75	-10	-25	-104	-102	-46	-15	-4	-4	-48
Loans (Multilaterals excl. IMF)	131	124	70	76	76	57	54	54	53	54
Financing gap	0	0	-14	-25	-25	-11	-6	0	0	0
Use of ECF	0	0	14	25	25	11	6	0	0	0
Residual gap	0	0	0	0	0	0	0	0	0	0
Use of Fund credit: RSF	0	0	0	0	0	19	10	0	0	0
Change in reserves incl. RSF (-:=accumulation)	75	-10	-39	-129	-127	-77	-31	-4	-4	-48
Memorandum items:										
Current account (incl. official transfers, percent of GDP)	-15.3	-12.2	-3.7	-5.6	-5.9	-6.1	-6.3	-5.8	-5.4	-4.6
Current account (excl. official transfers, percent of GDP)	-18.0	-14.7	-5.1	-5.9	-6.2	-6.9	-6.9	-6.4	-6.0	-5.1
Overall balance (percent of GDP)	-4.7	0.6	1.1	3.0	4.4	2.7	0.9	0.1	0.1	1.5
Gross international reserves	582	595	626	699	728	794	819	823	827	875
Months of current year's imports of goods and services	7.9	8.0	6.3	6.5	6.7	6.6	6.4	6.1	5.8	5.8
Months of next year's imports of goods and services	7.8	6.0	5.7	6.1	6.1	6.2	6.0	5.7	5.5	5.5
Gross international reserves excl. RSF	582	595	626	699	728	775	810	823	827	875
Months of current year's imports of goods and services	7.5	6.2	6.3	6.5	6.7	6.5	6.3	6.1	5.8	5.8
Months of next year's imports of goods and services	7.8	6.0	5.7	6.1	6.1	6.0	6.0	5.7	5.5	5.5
External public debt	1,998	2,192	2,260	2,338	2,335	2,472	2,568	2,593	2,625	2,693
External aid (grants and loans, percent of GDP)	12.1	10.7	5.6	8.3	10.1	9.3	7.6	5.7	5.2	5.4
Nominal GDP	1,604	1,689	2,131	2,418	2,331	2,491	2,661	2,839	3,028	3,228

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, 2022–2028[1]

(Millions of CVE)

	2022		2023		2024			2025	2026	2027	2028
	SR 2nd review	Act.	SR 2nd review	Proj.	SR 2nd review	Draft Budget	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	52,661	52,660	65,590	65,562	69,245	76,994	75,720	76,414	79,078	86,513	91,968
Tax	44,146	44,146	48,206	48,537	53,006	55,282	53,974	60,200	65,228	70,166	74,808
Taxes on income and profit	10,174	10,174	12,317	12,346	12,635	12,834	12,693	13,966	15,794	18,022	19,215
Taxes on goods and services	23,136	23,136	24,084	24,140	27,685	28,592	27,818	30,601	32,894	35,080	37,602
Taxes on international trade	10,025	10,025	10,955	11,199	11,780	12,914	12,353	14,647	15,436	15,886	16,736
Other taxes	811	811	850	852	906	941	1,110	986	1,104	1,178	1,256
Grants	2,131	2,131	5,163	4,798	3,504	6,409	6,409	4,308	2,330	4,061	4,061
Other revenue	6,384	6,383	12,222	12,227	12,735	15,303	15,337	11,905	11,520	12,285	13,099
Expenditure	62,676	62,676	77,359	74,388	78,684	85,227	85,001	82,665	82,679	87,823	93,828
Expense	58,141	58,141	66,029	66,055	69,305	74,439	74,231	70,859	72,662	76,138	81,014
Compensation of employees 2/	21,984	21,984	24,431	24,581	26,141	27,099	27,099	27,244	27,612	29,447	30,768
Use of goods and services	10,420	10,420	14,692	14,727	13,359	17,050	16,850	13,792	14,314	15,291	16,330
Interest	5,376	5,376	5,878	5,878	6,635	6,238	6,217	6,275	6,755	4,746	5,406
Subsidies	1,964	1,964	2,016	2,364	2,057	1,885	1,885	1,865	1,845	1,825	1,806
Current transfers	5,646	5,646	6,659	6,674	7,099	7,587	7,400	7,219	7,551	8,053	8,586
Social benefits	9,010	9,010	9,146	9,167	9,750	10,740	10,740	10,780	11,055	12,195	13,226
Other expense (incl. capital transfer)	3,742	3,742	3,207	2,665	4,263	3,840	4,040	3,686	3,530	4,580	4,892
Net acquisition of nonfinancial assets	4,535	4,535	11,330	8,333	9,380	10,788	10,770	11,806	10,018	11,685	12,814
Primary balance	-4,639	-4,641	-5,891	-2,948	-2,804	-1,994	-3,064	23	3,154	3,436	3,546
Overall balance	-10,015	-10,016	-11,769	-8,826	-9,439	-8,233	-9,281	-6,251	-3,601	-1,310	-1,860
Net other liabilities	-173	-173	1,940	-1,368	-2,274	657	-558	-401	-376	0	0
Onlending to SOEs for investment purpose 3/	-1,075	-1,075	-1,851	-1,851	-543	-441	-441	-628	-590	0	0
Other onlending (net)	197	197	197	198	144	-441	172	227	215	0	0
Capitalization	-2,716	-2,716	-2,200	-2,200	-2,200	-2,600	-2,600	0	0	0	0
Other	3,059	3,059	5,794	2,485	325	3,527	2,312	0	0	0	0
Financing needs	10,188	10,189	9,828	10,194	11,713	7,576	9,839	6,653	3,977	1,310	1,860
Total financing	10,188	10,189	9,828	10,194	11,713	7,576	9,839	6,653	3,977	1,310	1,860
Net domestic financing	5,592	5,593	3,772	-214	8,277	3,864	-636	-513	1,020	-2,187	-3,605
Net external financing	4,596	4,596	6,057	10,408	3,436	3,712	10,475	7,165	2,957	3,497	5,465
Net errors and omissions (+ overfinancing)	0	0	0	0	0	0	0	0	0	0	0
Memorandum items:											
Counter factual overall balance without RSF 4/	0	0	0	0	0	0	-9,669	-6,819	-4,149	-1,837	-2,366
Cumulative estimated RSF savings from substituting more expensive domestic financing 4/	0	0	0	0	0	…	388	956	1,504	2,031	2,537
Social Spending	15,800	15,800	17,304	17,304	18,448	…	18,490	19,752	21,073	22,473	23,960
Total Public Investment	6,970	6,970	13,928	10,931	10,627	…	11,916	12,905	11,079	11,685	12,814
of which: public investment done by SOEs	2,339	2,339	1,851	1,851	543	…	441	628	590	0	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.

4/ Assuming a nominal interest rate differential of 4 percent and average term to maturity differential of 13 years between RSF and domestic financing.

Table 3b. Cabo Verde: Statement of Operations of the Central Government, 2022–2028[1]

(Percent of GDP)

	2022		2023		2024			2025	2026	2027	2028
	SR 2nd review	Act.	SR 2nd review	Proj.	SR 2nd review	Draft Budget	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	21.6	22.4	24.6	25.5	24.4	26.9	27.6	26.0	25.3	25.9	25.8
Taxes	18.1	18.8	18.1	18.9	18.6	19.3	19.6	20.5	20.8	21.0	21.0
Taxes on income and profit	4.2	4.3	4.6	4.8	4.4	4.5	4.6	4.8	5.0	5.4	5.4
Taxes on goods and services	9.5	9.8	9.0	9.4	9.7	10.0	10.1	10.4	10.5	10.5	10.6
Taxes on international trade	4.1	4.3	4.1	4.4	4.1	4.5	4.5	5.0	4.9	4.8	4.7
Other taxes	0.3	0.3	0.3	0.3	0.3	0.3	0.4	0.3	0.4	0.4	0.4
Grants	0.9	0.9	1.9	1.9	1.0	2.2	2.3	1.5	0.7	1.2	1.1
Other revenue	2.6	2.7	4.6	4.8	4.5	5.3	5.6	4.1	3.7	3.7	3.7
Expenditure	25.7	26.7	29.0	28.9	27.7	29.8	30.9	28.2	26.4	26.3	26.4
Expense	23.8	24.7	24.8	25.7	24.4	26.0	27.0	24.1	23.2	22.8	22.8
Compensation of employees 2/	9.0	9.4	9.2	9.6	9.2	9.5	9.9	9.3	8.8	8.8	8.6
Use of goods and services	4.3	4.4	5.5	5.7	4.7	6.0	6.1	4.7	4.6	4.6	4.6
Interest	2.2	2.3	2.2	2.3	2.3	2.2	2.3	2.1	2.2	1.4	1.5
Subsidies	0.8	0.8	0.8	0.9	0.7	0.7	0.7	0.6	0.6	0.5	0.5
Current transfers	2.3	2.4	2.5	2.6	2.5	2.6	2.7	2.5	2.4	2.4	2.4
Social benefits	3.7	3.8	3.4	3.6	3.4	3.8	3.9	3.7	3.5	3.7	3.7
Other expense (incl. capital transfer)	1.5	1.6	1.2	1.0	1.5	1.3	1.5	1.3	1.1	1.4	1.4
Net acquisition of nonfinancial assets	1.9	1.9	4.2	3.2	3.3	3.8	3.9	4.0	3.2	3.5	3.6
Primary balance	-1.9	-2.0	-2.2	-1.1	-1.0	-0.4	-1.1	0.0	1.0	1.0	1.0
Overall balance	-4.1	-4.3	-4.4	-3.4	-3.3	-2.9	-3.4	-2.1	-1.2	-0.4	-0.5
Net other liabilities	-0.1	-0.1	0.7	-0.5	-0.8	0.2	-0.2	-0.1	-0.1	0.0	0.0
Onlending to SOEs for investment purpose 3/	-0.4	-0.5	-0.7	-0.7	-0.2	-0.2	-0.2	-0.2	-0.2	0.0	0.0
Other onlending (net)	0.1	0.1	0.1	0.1	0.1	-0.2	0.1	0.1	0.1	0.0	0.0
Capitalization	-1.1	-1.2	-0.8	-0.9	-0.8	-0.9	-0.9	0.0	0.0	0.0	0.0
Other	1.3	1.3	2.2	1.0	0.1	1.2	0.8	0.0	0.0	0.0	0.0
Financing Needs	4.2	4.3	3.7	4.0	4.1	2.6	3.6	2.3	1.3	0.4	0.5
Total financing	4.2	4.3	3.7	4.0	4.1	2.6	3.6	2.3	1.3	0.4	0.5
Net domestic financing	2.3	2.4	1.4	-0.1	2.9	1.3	-0.2	-0.2	0.3	-0.7	-1.0
Net external financing	1.9	2.0	2.3	4.0	1.5	1.3	3.8	2.4	0.9	1.0	1.5
Net errors and omissions (+ overfinancing)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Counter factual overall balance without RSF 4/	0	0	0	0	0	0	-3.5	-2.3	-1.3	-0.6	-0.7
Cumulative estimated RSF savings from substituting more expensive domestic financing 4/	0	0	0	0	0	0	0.1	0.3	0.5	0.6	0.7
Debt-to-GDP (Third review)	…	127.1	…	119.9	…	…	116.2	111.2	105.4	99.4	93.9
Change in debt-to-GDP (Third review)	…	…	…	-7.3	…	…	-3.6	-5.1	-5.8	-6.0	-5.6
of which: contribution from primary deficit	…	…	…	1.1	…	…	1.1	0.0	-1.0	-1.0	-1.0
of which: contribution from real GDP growth	…	…	…	-5.5	…	…	-5.4	-4.9	-4.3	-4.0	-3.8
of which: contribution from average real interest rate	…	…	…	-3.2	…	…	-0.8	0.0	-0.3	-0.3	-0.2
of which: contribution from other debt creation flows 1/	…	…	…	0.3	…	…	1.5	-0.2	-0.1	-0.7	-0.5
Social Spending	6.5	6.7	6.5	6.7	…	…	6.7	6.7	6.7	6.7	6.7
Total Public Investment	2.9	3.0	5.2	4.3	…	…	4.3	4.4	3.5	3.5	3.6
Of which: public investment done by SOEs	1.0	1.0	0.7	0.7			0.2	0.2	0.2	0.0	0.0
GDP at current market prices (billions of CVEsc)	244.3	235.0	266.6	257.1	284.2	286.4	274.7	293.4	313.1	333.9	356.0

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

1/ Includes net other liabilities and other debt-creating flows

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.

4/ Assuming a nominal interest rate differential of 4 percent and average term to maturity differential of 13 years between RSF and domestic financing.

Table 4. Cabo Verde: Deposit Corporations Survey, 2020–28

(Millions of CVE, unless otherwise indicated)

	2020	2021	2022	2023	2024	2025	2026	2027	2028
			Act.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Net foreign assets	57,716	63,718	66,329	77,232	84,240	86,665	86,729	86,779	91,724
Foreign assets	91,373	99,880	106,860	118,557	126,377	129,634	130,549	131,471	137,309
Of which: gross international reserves	64,213	65,636	69,036	80,243	87,568	90,323	90,730	91,136	96,452
Foreign liabilities	-33,658	-36,162	-40,531	-41,325	-42,137	-42,969	-43,821	-44,692	-45,585
Net domestic assets	148,917	149,183	158,957	169,250	179,922	191,839	205,094	219,299	230,465
Net domestic credit	146,433	170,936	185,609	195,902	206,574	218,491	231,746	245,951	257,117
Net claims on general government (net)	20,036	35,916	42,273	42,430	42,323	42,291	43,035	42,191	40,653
Investment in TCMFs 1/	6,433	6,433	6,433	6,433	6,433	6,433	6,433	6,433	6,433
Net claims on the central government	21,380	26,322	33,029	32,922	32,604	32,348	32,858	31,764	29,962
Credit to central government	44,681	52,916	63,182	63,075	62,757	62,501	63,011	61,918	60,115
Deposits of central government	-23,300	-26,593	-30,153	-30,153	-30,153	-30,153	-30,153	-30,153	-30,153
Of which: project deposits	-80	-92	-104	-104	-104	-104	-104	-104	-104
Net claims on local government and other agencies 2/	-7,777	3,161	2,811	3,075	3,286	3,510	3,744	3,993	4,258
Credit to the economy	126,396	135,019	143,336	153,472	164,251	176,200	188,711	203,760	216,464
o/w Credit to Private Sector	120,703	129,224	136,470	148,351	156,532	167,903	179,809	194,130	206,220
o/w Credit to Public Non-financial Corporations	5,681	5,783	6,857	5,112	7,710	8,288	8,893	9,621	10,235
Other items (net)	2,484	-21,752	-26,652	-26,652	-26,652	-26,652	-26,652	-26,652	-26,652
Broad money (M2)	206,632	212,902	225,286	246,482	264,162	278,504	291,823	306,077	322,188
Narrow money (M1)	108,321	105,352	120,585	131,930	141,393	149,070	156,199	163,829	172,452
Currency outside banks	11,115	11,416	12,236	13,388	14,348	15,127	15,850	16,624	17,500
Demand deposits	97,207	93,936	108,349	118,542	127,045	133,943	140,349	147,204	154,953
Quasi-money	97,565	99,673	98,824	108,122	115,877	122,169	128,011	134,264	141,331
Foreign currency deposits	4,599	4,606	5,877	6,430	6,891	7,266	7,613	7,985	8,405
(Change in percent of broad money, 12 months earlier)									
Net foreign assets	-6.6	2.9	1.2	4.8	2.8	0.9	0.0	0.0	1.6
Net domestic assets	10.3	0.1	4.6	4.6	4.3	4.5	4.8	4.9	3.6
Net domestic credit	-3.1	11.9	6.9	4.6	4.3	4.5	4.8	4.9	3.6
Net claims on the central government	-1.3	2.4	3.1	0.0	-0.1	-0.1	0.2	-0.4	-0.6
Credit to the economy	2.9	4.2	3.9	4.5	4.4	4.5	4.5	5.2	4.2
o/w Credit to Private Sector	3.1	4.1	3.4	5.3	3.3	4.3	4.3	4.9	3.9
o/w Credit to Public Non-financial Corporations	-0.2	0.0	0.5	-0.8	1.1	0.2	0.2	0.2	0.2
Other items (net)	13.4	-11.7	-2.3	0.0	0.0	0.0	0.0	0.0	0.0
Broad money (M2)	3.8	3.0	5.8	9.4	7.2	5.4	4.8	4.9	5.3
Memorandum items:									
Emigrant deposits	66,422	67,592	69,143	75,550	80,969	85,365	89,448	93,817	98,755
Emigrant deposits/total deposits (percent)	34.0	33.5	32.5	32.4	32.4	32.4	32.4	32.4	32.4
Excess reserves/total deposits (percent)	19.7	15.6	13.9	20.6	14.1	14.2	14.0	15.0	15.6
Money multiplier (M2/M0)	2.9	3.2	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Money velocity (Nominal GDP/M2)	0.9	0.9	1.0	1.0	1.0	1.1	1.1	1.1	1.1
Credit to the economy (percent change) 3/	4.8	6.8	6.2	7.1	7.0	7.3	7.1	8.0	6.2
o/w Credit to Private Sector	5.4	7.1	5.6	8.7	5.5	7.3	7.1	8.0	6.2
o/w Credit to Public Non-financial Corporations	-5.5	1.8	18.6	-25.4	50.8	7.5	7.3	8.2	6.4
Broad money (M2 in percent of GDP)	116.9	114.3	95.9	95.9	96.2	94.9	93.2	91.7	90.5

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, 2018–23Q2

(End-year; percent unless otherwise indicated)

	2018	2019	2020Q1	2020Q2	2020Q3	2020Q4	2021Q1	2021Q2	2021Q3	2021Q4	2022Q1	2022Q2	2022Q3	2022Q4	2023Q1	2023Q2
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	21.4	22.0	21.4	21.9	22.2	22.7	21.4
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	21.1	21.6	21.1	21.5	22.6	23.2	22.1
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	8.1	8.2	8.8	8.9	7.8	9.1	8.7
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	1.6	7.4	9.4	11.6	3.9	8.6	10.8
Provisions to nonperforming loans	71.0	77.0	70.1	66.5	73.3	86.4	80.0	83.0	84.1	95.5	81.3	77.9	73.2	88.4	77.1	73.5
Earnings and profitability																
Return on assets	0.3	1.3	0.4	0.6	1.0	1.3	0.4	0.8	1.2	1.4	0.4	0.8	1.3	1.5	0.4	0.9
Return on equity	4.8	17.8	5.3	7.9	12.7	15.4	4.9	9.1	12.7	14.9	4.4	8.7	13.6	16.0	4.4	9.2
Interest margin to gross income	79.6	81.1	78.2	85.8	86.7	85.7	84.8	83.1	83.5	80.8	83.9	82.0	78.6	80.0	83.6	82.7
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	46.5	45.6	44.2	46.2	45.7	45.4
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	24.1	22.8	23.2	24.6	24.8	25.2
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	30.1	28.5	29.1	31.5	31.6	32.3
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	15.7	15.8	17.1	17.0	17.3	17.6
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	52.6	51.8	52.9	53.3	53.8	54.3
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	55.5	56.3	56.1	57.4	56.7	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	58.0	57.4	56.5	55.6	58.1	57.5

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: Quantitative Performance Criteria and Indicative Targets Under the ECF, March 2023-December 2024[1]

(Millions of CVE, unless otherwise indicated)

	2023									2024					
	end-March			end-June			end-September	end-December		end-March		end-June		end-September	end-December
	Indicative Targets (IT)	Actual	Status	Performance Criteria (PC)	Actual	Status	Indicative Targets (IT)	Performance Criteria (PC)	Revised Performance Criteria (PC)	Indicative Targets (IT)	Revised Indicative Target	Performance Criteria (PC)	Revised Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)
	Cumulative from the beginning of the calendar year														
Quantitative performance criteria															
Primary balance, floor [2]	-2,612.0	608.1	met	-4,141.0	2,759.2	met	-5,564.2	-6,298.0		-1,849		-2417		-2740.6	-3,063.9
Tax revenue, floor	9,550.1	13,228.8	met	19,095.0	24,669.9	met	31,483.0	45,849.0		8,088		21029		37501.4	53,973.7
Net other liabilities, floor [3]	-501.5	2,327.7	met	-625.3	593.2	met	-1,150.2	1,940.3	-1,368.2	-1,099	-418	-1259	-446.3	-502.12	-557.9
Net domestic financing, ceiling	5,651	820	met	5,886	1,728	met	4,920.5	4,179		3,093		4021		2241.25	462
Nonaccumulation of domestic arrears [4]	0	0	met	0	0	met	0	0		0		0		0	0
Non-accumulation of external payment arrears [4]	0	0	met	0	0	met	0	0		0		0		0	0
PV of new external debt, ceiling (in millions of US Dollars)	46	11.93	met	60	24	met	75	98.7	108.8	24		37		95.4	125.5
Nominal level of new nonconcessional external debt of central government, ceiling	0	0	met	0	0	met	0	0		0		0		0	0
Gross international reserves (in millions of euros), floor [2]	554	653.9	met	572	626.0	met	592	622		671		693		743.58	794
Indicative Targets															
Social spending, floor	2,923	3,135	met	6,180	6,982	met	10,009.0	17,304.0		3,690		7379		12934.5	18,490.1
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	413.3	15.6		827	47		1,286	1,653		116.6		136		165.209	194
Capitalization	300.0	1,955.1		765.3	1,366.4		880.1	2,200.4		1,100		1600		2100.2	2,600
Program assumptions															
Project and budget support grants	522.5	479.0		623.3	1,206.1		2,090.0	5,225.0		526		1121		3765.34	6,409.3
External debt service	3,664.8	2,557.5		6,445.4	3,420.2		10,664.6	12,921.0		2,409		4818		8424.69	12,031.9
Sales of assets	142.2	12.2		516.6	97.0		612.0	747.0		106		226		465.3	705.0
Project and budget support loans	913.9	2,758.1		5,887.7	5,590.6		13,523.5	16,663.0		1,816		4238		11995.3	19,752.2

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

[1] 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 7. Cabo Verde: Structural Benchmarks Under the ECF for 2022-24

Actions	Target date	Objective	Status
Fiscal reforms			
1) Invoice electronically at least 50 percent of tax payers for VAT	End-December 2022	Improve revenue collection	Met
2) Submit to parliament the budget for 2023 that is in line with commitments under the program.	End December 2022	Support fiscal and debt sustainability	Met
3) Compile and publish historical series of government financial statistics for general government.	End-March 2023	Improve fiscal transparency	Met
4) Publish annual budget execution reports for the general government.	End-September 2023	Improve fiscal transparency	Met
5) Construct a Compliance Risk Management system to allow for the optimization of tax revenue collection by end-December 2023.	End-December 2023	Support fiscal and debt sustainability	
6) Submit to parliament the budget for 2024 that is in line with the primary balance commitment under the program.	End-December 2023	Support fiscal and debt sustainability	
7) Develop and publish an action plan to reduce tax expenditures by 1 percent of GDP and include published estimates of annual tax expenditures in the budget to improve transparency	End-September 2024	Support fiscal and debt sustainability	
8) Implement the action plan to reduce expenditures during in the 2025 budget	End-December 2024	Support fiscal and debt sustainability	
9) Broadening the coverage of fiscal risk analysis and reporting to include PPPs **(Proposed new SB)**	End-September 2024	Improve fiscal transparency and risk analysis	
SOEs reforms			
10) Conduct quarterly analysis of fiscal risk assessment using the IMF SOEs health check tool.	End-September 2022	Improve fiscal reporting and reduce fiscal risks	Met
11) Introduce a quarterly monitoring report on SOEs budget execution.	End-September 2022	Improve fiscal reporting and reduce fiscal risks	Met
12) 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 reduce fiscal risks	Met
13) Based on the July 2023 structural benchmark, publish in the annual report on public companies the targets agreed between the Ministry of Finance and Business Development and the six largest public companies , on improving financial performance and reducing the need for central government support.	End-June 2024	Improve fiscal reporting and reduce fiscal risks	
Monetary policy reforms			
14) Preannounce a schedule for TIM and TRM auctions.	End-June 2022	Support the development of the money market	Met
15) Introduce composite indicators of economic activity.	End-June 2023	Support monetary policy analysis	Met
Financial sector reforms			
16) 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	Met
17) Carry out a comprenhensive study of loan losses and provisions at the expiration of the credit moratorium.	End-December 2022	Strengthen financial stability	Met
18) Develop a common framework for the resolution of crisis related NPLs.	End-December 2022	Strengthen financial stability	Met
19) Increase the frequency of stress testing to twice per year (June 2023 and December 2023) to ensure the effectiveness of the supervisory process and revamp the stress testing methodology to include detailed banking data and cyber security risk assessment.	End-December 2023	Strengthen financial stability	
20) Submit the draft amendments to the BCV Law, in line with IMF recommendations, to parliament with a view to (i) establish an independent oversight process that is separate from executive management, (ii) strengthen the BCV's personal and financial autonomy, and (iii) enhance transparency and accountability mechanisms **(Proposed new SB)**	End-July 2024	Strengthen BCV institutional framework	

Table 8. Cabo Verde: Indicators of Capacity to Repay the Fund, 2023-43

	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	2038	2039	2040	2041	2042	2043
Fund obligations based on existing credit (millions of SDRs)																					
Principal	0.00	0.00	2.37	4.74	5.87	8.57	10.14	7.77	5.40	4.28	1.58	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Charges and interest	0.00	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33
Total	0.00	1.33	3.70	6.07	7.20	9.90	11.47	9.10	6.73	5.61	2.91	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33
Fund obligations based on existing and prospective credit (millions of SDRs)																					
Principal	0.00	0.00	2.37	4.74	5.87	8.57	11.49	10.93	9.01	7.88	5.18	2.65	2.43	2.37	2.37	2.37	2.37	2.37	2.37	2.37	2.37
o/w PRGT	0.00	0.00	2.37	4.74	5.87	8.57	11.49	10.93	9.01	7.88	5.18	2.25	0.45	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
o/w RST	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.40	1.98	2.37	2.37	2.37	2.37	2.37	2.37	2.37	2.37
Charges and interest	0.00	1.42	1.80	1.86	1.86	1.87	1.86	1.86	1.86	1.87	1.86	1.86	1.85	1.80	1.74	1.69	1.64	1.58	1.53	1.48	1.42
o/w PRGT	0.00	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33
o/w RST	0.00	0.09	0.47	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.51	0.46	0.41	0.36	0.30	0.25	0.20	0.14	0.09
Total	0.00	1.42	6.54	11.34	13.60	19.01	24.84	23.72	19.88	17.63	12.22	7.16	6.71	6.54	6.48	6.43	6.38	6.32	6.27	6.22	6.16
Total obligations based on existing and prospective credit																					
Millions of SDRs	0.00	1.42	4.17	6.60	7.73	10.44	13.35	12.79	10.87	9.75	7.04	4.51	4.28	4.17	4.11	4.06	4.01	3.95	3.90	3.85	3.79
o/w PRGT	0.00	1.33	3.70	6.07	7.20	9.90	12.82	12.26	10.34	9.21	6.51	3.58	1.78	1.33	1.33	1.33	1.33	1.33	1.33	1.33	1.33
o/w RST	0.00	0.09	0.47	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.53	0.93	2.49	2.83	2.78	2.73	2.67	2.62	2.57	2.51	2.46
Millions of U.S. dollars	0.00	1.91	5.65	8.98	10.53	14.27	18.24	17.48	14.86	13.32	9.62	6.16	5.85	5.70	5.62	5.55	5.48	5.40	5.33	5.26	5.18
o/w PRGT	0.00	1.79	5.01	8.26	9.81	13.53	17.52	16.76	14.13	12.59	8.90	4.89	2.43	1.82	1.82	1.82	1.82	1.82	1.82	1.82	1.82
o/w RST	0.00	0.12	0.64	0.72	0.72	0.72	0.72	0.72	0.72	0.72	0.72	1.27	3.40	3.87	3.80	3.73	3.65	3.58	3.51	3.43	3.36
Percent of exports of goods and services	0.00	0.20	0.55	0.79	0.86	1.08	1.26	1.11	0.87	0.72	0.48	0.28	0.24	0.22	0.20	0.18	0.16	0.14	0.12	0.11	0.10
Percent of debt service	0.00	1.20	3.47	5.19	6.91	9.05	10.72	10.04	8.30	6.83	4.57	2.79	2.51	2.30	2.14	2.03	1.95	1.84	1.79	1.77	1.78
Percent of quota	0.00	5.99	17.59	27.85	32.62	44.05	56.33	53.97	45.86	41.14	29.70	19.03	18.06	17.59	17.34	17.13	16.92	16.67	16.46	16.24	15.99
Percent of gross international reserves	0.00	0.22	0.62	0.98	1.15	1.48	1.78	1.58	1.21	1.00	0.67	0.39	0.33	0.30	0.27	0.24	0.21	0.19	0.17	0.15	0.13
Percent of GDP	0.00	0.07	0.19	0.28	0.31	0.40	0.48	0.43	0.34	0.29	0.20	0.12	0.11	0.10	0.09	0.08	0.08	0.07	0.07	0.06	0.06
Outstanding Fund credit																					
Millions of SDRs	55.2	80.0	90.1	85.3	79.5	70.9	59.4	48.5	39.5	31.6	26.4	23.9	21.5	19.1	16.7	14.4	12.0	9.6	7.2	4.9	2.5
Millions of U.S. dollars	74.2	107.8	122.0	116.1	108.2	96.9	81.2	66.2	53.9	43.2	36.1	32.6	29.3	26.1	22.9	19.6	16.4	13.1	9.9	6.7	3.4
Percent of exports of goods and services	8.7	11.448	11.778	10.2	8.8	7.3	5.6	4.2	3.2	2.3	1.8	1.5	1.2	1.0	0.8	0.6	0.5	0.3	0.2	0.1	0.1
Percent of debt service	45.4	67.4	75.0	67.0	71.0	61.4	47.7	38.0	30.1	22.1	17.1	14.8	12.6	10.5	8.7	7.2	5.8	4.5	3.3	2.2	1.2
Percent of quota	233	338	380	360	335	299	251	205	166	133	111	101	91	81	71	61	51	41	31	21	11
Percent of gross international reserves	9.3	12.3	13.4	12.7	11.8	10.0	7.9	6.0	4.4	3.3	2.5	2.1	1.7	1.4	1.1	0.9	0.6	0.5	0.3	0.2	0.1
Percent of GDP	2.9	3.9	4.1	3.7	3.2	2.7	2.1	1.6	1.2	0.9	0.7	0.6	0.5	0.4	0.4	0.3	0.2	0.2	0.1	0.1	0.0
Net Use of Fund Credit (millions of SDRs)	20.3	24.8	10.1	-4.7	-5.9	-8.6	-11.5	-10.9	-9.0	-7.9	-5.2	-2.5	-2.4	-2.4	-2.4	-2.4	-2.4	-12.0	-2.4	-2.4	-2.4
Disbursements	20.3	24.8	12.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments	0.0	0.0	2.4	4.7	5.9	8.6	11.5	10.9	9.0	7.9	5.2	2.5	2.4	2.4	2.4	2.4	2.4	12.0	2.4	2.4	2.4
Memorandum items:																					
Exports of goods and services (millions of U.S. dollars)	856.1	941.9	1036.0	1135.9	1229.9	1324.2	1445.1	1580.1	1706.0	1840.3	2006.7	2197.0	2420.7	2600.2	2844.0	3142.3	3510.0	3874.2	4300.1	4722.4	5240.3
Debt service (millions of U.S. dollars)	163.5	160.0	162.7	173.1	152.4	157.7	170.2	174.2	178.9	195.1	210.6	220.8	233.4	247.3	262.0	273.2	281.0	294.2	298.0	297.2	291.4
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	23.7	23.7	23.7	23.7	23.7
Gross international reserves	795.9	879.0	910.5	916.8	917.4	967.0	1024.1	1107.3	1230.1	1327.4	1429.4	1587.4	1746.7	1878.5	2077.8	2295.2	2553.5	2840.9	3138.6	3443.9	4123.8
GDP (millions of U.S. dollars)	2549.7	2757.4	2958.0	3163.3	3360.6	3568.9	3801.3	4051.2	4317.3	4601.0	4903.2	5224.7	5566.8	5931.4	6319.3	6732.0	7171.9	7639.3	8133.5	8657.9	9219.1

Sources: IMF staff estimates and projections.

Table 9. Cabo Verde: Schedule of Reviews Under the ECF, 2022-25

Date Available	Amount (SDR millions)	% of Quota	Conditions Necessary for Purchase
15-Jun-22	11.26	47.5	Executive Board approval of ECF
15-Oct-22	11.26	47.5	Observance of end-June 2022 performance criteria and completion of the first review under the arrangement
15-Mar-23	4.50	19.0	Observance of end-Dec 2022 performance criteria and completion of the second review under the arrangement
15-Oct-23	4.50	19.0	Observance of end-June 2023 performance criteria and completion of the third review under the arrangement
15-Mar-24	4.50	19.0	Observance of end-December 2023 performance criteria and completion of the fourth review under the arrangement
15-Oct-24	4.50	19.0	Observance of end-June 2024 performance criteria and completion of the fifth review under the arrangement
15-Mar-25	4.51	19.0	Observance of end-December 2024 performance criteria and completion of the sixth review under the arrangement
Total	45.03	190.0	

Source: IMF staff estimates.
Note: Quota is SDR 23.70 million.

Table 10. Cabo Verde: Access and Phasing Under the RSF Arrangement

Available date	SDR million	Percent of Quota	Total Disbursements	Conditions for disbursement
15-Mar-24	2.632	11.11	5.264	Reform measure 1 implementation review
15-Mar-24	2.632	11.11		Reform measure 3 implementation review
15-Oct-24	2.632	11.11	10.528	Reform measure 2 implementation review
15-Oct-24	2.632	11.11		Reform measure 7 implementation review
15-Oct-24	2.632	11.11		Reform measure 8 implementation review
15-Oct-24	2.632	11.11		Reform measure 9 implementation review
15-Mar-25	2.632	11.11	7.908	Reform measure 4 implementation review
15-Mar-25	2.632	11.11		Reform measure 5 implementation review
15-Mar-25	2.644	11.16		Reform measure 6 implementation review
Total access	**23.7**	**100.0**		

Source: IMF staff estimates.

Note: Quota is SDR 23.7 million.

Table 11. Cabo Verde: RSF Reform Measures Matrix						
KEY CHALLENGE	**REFORM MEASURE**	**DIAGNOSTIC REFERENCE**	**IMF CD INPUT**	**RM EXPECTED OUTCOME**	**DEVELOPMENT PARTNER ROLE**	**TIMING**
National coordination and management of climate change is under the MAE that is not able to ensure cross sector coordination	**RM1.** Government will establish a council/body for coordinating climate change policy planning and strategy, and DRM under the Heads of Government, with a clear tasks, responsibilities and procedures, including mechanisms for (i) holding entities accountable for consistency across sectoral plans in line with the national development strategy (PEDS II) and international commitments (NDC), and (ii) providing strategic oversight of DRM defined in the TORs, with implementation reflected in the protocols of regular meetings. The MAE serves as secretariate.	Climate Policy Diagnostic (CPD)		Integrated and effective coordination of climate change activities in the public administration, ensuring cross sectoral consistency of key reform plans, including for electricity and water (for human consumption and for irrigation), and in DRM	LuxDev is providing support to MAE for the climate management function	End-April 2024; 4th ECF Review
Natural disaster and climate related risk not adequately featured in fiscal planning	**RM2**. To improve fiscal risk management, the Ministry of Finance will conduct and publish in the annual Fiscal Risk Statement quantitative analysis of the fiscal risks generated by climate change.	C-PIMA; CPD	Follow up support from FADM2 on fiscal risk reporting	Improve awareness of climate -related matters in fiscal planning and budgeting	World Bank has prior actions and triggers in the latest DPF supporting a stronger PIM framework and aligned with the C-PIMA recommendations	End-September 2024; 5th ECF Review

Table 11. Cabo Verde: RSF Reform Measures Matrix (continued)

KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TIMING
Investments don't reflect needed physical resilience to Climate Change	**RM3**. The Ministry of Finance will enact amendments to the PPP legal framework to ensure climate requirements are reflected in PPP agreements and the Ministry of Finance will publish a manual integrating these requirements throughout the PPP capital project lifecycle, from project identification to contract management stages.	C-PIMA	FAD Support	Stronger PPP framework; reduced fiscal risks from PPPs; enhanced climate sensitive public investment planning and budgeting		End-April. 2024; 4th ECF Review
	RM4. To scale up and systematize climate finance the Ministry of Finance will (i) adopt a national climate finance mobilization strategy that comprehensively identifies the financing instruments to unlock climate finance sources; and (ii) develop and publish, a pipeline of appraised public capital projects, including climate-related projects, as part of the budget process.	C-PIMA	Luxembourg and follow up support from FADM2	Generate a robust pipeline of projects and scale up climate investments		End-April 2025; 6th ECF Review

Table 11. Cabo Verde: RSF Reform Measures Matrix (continued)

KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TIMING
Mitigation, adaptation and resilience in the energy sector are held up by energy inefficiency and obstacles to transition	**RM5**. To support energy transition plans, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of electricity (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting electricity tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments. (Ministry of Industry, Trade and Energy and MoF)	CPD	FADEP support on the analytical study and distributional impact – TBC	Energy efficiency and facilitation of more renewable energy through development of appropriate market conditions and by ensuring funding for necessary infrastructure investment. Ensuring the financial soundness of electricity sector operator to create an environment conducive to private sector investment in RES production	WB energy projects are providing support on unbundling the energy SOE	End-April 2025; 6th ECF Review

Table 11. Cabo Verde: RSF Reform Measures Matrix (continued)

KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TIMING
Access to water resources and fiscal sustainability are vulnerable to long-run climate impacts due to lack of investment and non-ecological use	**RM6** To support reform initiatives, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of water (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting water tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments, and/or by financing infrastructure investment transparently from the budget, with a view to ensure sustainability of the water sector. (National Water and sanitation Agency (ANAS) and MoF)	CPD	FAD support for tariff review and the distributional impact – TBC	Sustainable use of water resources to improve adaptation to climate change effects, clarifying the source of funding for necessary infrastructure investment, ensuring the financial soundness of water sector operators to create an environment conducive to private sector investment in water and sanitation service provision	LuxDev is providing support in the water sector. TBC.	End-April 2025; 6th ECF Review
	RM7. The Unique Social Registry (USR) will be expanded to provide the basis for a social support system that can efficiently mitigate the implications of climate transition and climate hazard events. To this end, the Ministry of Family and Social Inclusion and the MoF will expand coverage of the USR to 100 percent of poor and vulnerable households (including from rural areas) as identified based on the latest household budget survey, and offer inclusion in the USR to 100 percent of the households in climate vulnerable areas.	CPD		Strengthen the social safety net to prepare for efficiently supporting the vulnerable and poor as needed (i) in case of adverse climate change related events, and (ii) through the climate transition.	WB	End-Nov. 2024; 5th ECF Review

Table 11. Cabo Verde: RSF Reform Measures Matrix (concluded)						
KEY CHALLENGE	**REFORM MEASURE**	**DIAGNOSTIC REFERENCE**	**IMF CD INPUT**	**RM EXPECTED OUTCOME**	**DEVELOPMENT PARTNER ROLE**	**TIMING**
	RM8 INGT or new unit/council for CC management and DRM will develop and disseminate natural disaster risk and vulnerability maps, including information on how and where climate hazards might affect the areas and regions, to assess risks and vulnerabilities of the population, infrastructure assets, sectors, and the economy/businesses. The land use planning regulation and construction code requirements will be amended to consider disaster risks and vulnerabilities for urban and rural development planning and for designing and constructing infrastructure and buildings.			Investment decisions that are resilient to climate change impacts such as sea level rise, flooding, and landslides.		End-Nov. 2024; 5th ECF Review
Green financing/Climate Finance	**RM9**. The BCV will develop a climate information architecture for banks, consisting of 1) the adoption of a climate change adaptation and mitigation taxonomy, and 2) the publication of climate risk and opportunities and disclosure guidelines, so that banks are expected to submit their internal roadmaps within six months from the effective date of application of the guideline, followed by progress reports every six months.		MCM CD TBC	Transparency on impact of climate change and disaster risks in the financial sector	TBC	End-Nov. 2024; 6th ECF Review

Table 12. Cabo Verde: RSF Reform Areas/Priorities and Reform Measures

3rd Review ECF Dec-23 RSF approval	4th Review ECF Jun-24 1st RSF Review	5th Review ECF Dec-24 2nd RSF Review	6th Review ECF Jun-25 3rd RSF Review
Reform Area 1: Strengthen governance of climate change policy	**RM1.** Government will establish a council/body for coordinating climate change policy planning and strategy, and DRM under the Heads of Government, with a clear tasks, responsibilities and procedures, including mechanisms for (i) holding entities accountable for consistency across sectoral plans in line with the national development strategy (PEDS II) and international commitments (NDC), and (ii) providing strategic oversight of DRM defined in the TORs, with implementation reflected in the protocols of regular meetings. The MAE serves as secretariate.		
Reform Area 2: Improve Fiscal and Physical Resilience to Climate Change	**RM3**. The Ministry of Finance will enact amendments to the PPP legal framework to ensure climate requirements are reflected in PPP agreements and the Ministry of Finance will publish a manual integrating these requirements throughout the PPP capital project lifecycle, from project identification to contract management stages.	**RM2**. To improve fiscal risk management, the Ministry of Finance will conduct and publish in the annual Fiscal Risk Statement quantitative analysis of the fiscal risks generated by climate change.	**RM4**. To scale up and systematize climate finance the Ministry of Finance will (i) adopt a national climate finance mobilization strategy that comprehensively identifies the financing instruments to unlock climate finance sources; and (ii) develop and publish, a pipeline of appraised public capital projects, including climate-related projects, as part of the budget process.
Reform Area 3: Strengthening mitigation and resilience through energy efficiency and transition			**RM5**. To support energy transition plans, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of electricity (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting electricity tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments. (Ministry of Industry, Trade and Energy and MoF)
Reform Area 4: Promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts		**RM8** INGT or new unit/council for CC management and DRM will develop and disseminate natural disaster risk and vulnerability maps, including information on how and where climate hazards might affect the areas and regions, to assess risks and vulnerabilities of the population, infrastructure assets, sectors, and the economy/businesses. The land use planning regulation and construction code requirements will be amended to consider disaster risks and vulnerabilities for urban and rural development planning and for designing and constructing infrastructure and buildings.	**RM6** To support reform initiatives, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of water (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting water tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments, and/or by financing infrastructure investment transparently from the budget, with a view to ensure sustainability of the water sector. (National Water and sanitation Agency (ANAS) and MoF)
		RM7. The Unique Social Registry (USR) will be expanded to provide the basis for a social support system that can efficiently mitigate the implications of climate transition and climate hazard events. To this end, the Ministry of Family and Social Inclusion and the MoF will expand coverage of the USR to 100 percent of poor and vulnerable households (including from rural areas) as identified based on the latest household budget survey, and offer inclusion in the USR to 100 percent of the households in climate vulnerable areas.	
Reform Area 5: Financial sector resilience to climate change		**RM9**. The BCV will develop a climate information architecture for banks, consisting of 1) the adoption of a climate change adaptation and mitigation taxonomy, and 2) the publication of climate risk and opportunities and disclosure guidelines, so that banks are expected to submit their internal roadmaps within six months from the effective date of application of the guideline, followed by progress reports every six months.	

Annex I. Risk Assessment Matrix[1]

(Scale—high, medium, or low)

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Conjunctural risks			
Intensification of regional conflict(s)	**High** Escalation of Russia's war in Ukraine or other regional conflicts and resulting economic sanctions disrupt trade (e.g., energy, food, tourism, and/or critical supply chain components), remittances, FDI and financial flows, and payment systems, and lead to refugee flows. ,.	**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 lower FDI, increase inflation leading to food insecurity and poverty.	• Slow down planned unwinding of policy support while ensuring that recovery is well entrenched. • Create fiscal space through spending review and tax mobilization for new policies to mitigate supply shocks in the economy.
Abrupt global slowdown or recession	**Medium** Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and markets fragmentation. A new bout of global financial tightening, possibly combined with volatile commodity prices, leads to spiking risk premia, debt distress, widening of external imbalances, fiscal pressures, and sudden stops.	**Medium** Recession in key tourist markets would lower tourist arrivals and slow down economic recovery and revenues. Rising core yields and risk premia will increase the cost of new debt and add pressure to foreign reserves and financial account due to a "Fly-to-quality" effect. Rising yields could also reduce the flow of migrant deposits.	• Maintain adequate reserves and fiscal consolidation and reliance on concessional financing from bilateral and/or multilateral creditors. • Develop contingency plans to lower the impact of delayed recovery. • 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. The conjunctural shocks and scenarios highlight risks that may materialize over a shorter horizon (between 12 to 18 months) given the current baseline. Structural risks are those that are likely to remain salient over a longer horizon.

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Commodity price volatility	**High** A succession of supply disruptions (e.g., due to conflicts, uncertainty, and export restrictions) and demand fluctuations causes recurrent commodity price volatility, external and fiscal pressures, contagion effects, and social and economic instability	**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, and impacts vulnerable consumers.	• Build external buffers and resilience to shocks. • Diversification of energy usage (renewable energies transition), to mitigate oil price shocks. • Improve effectiveness of government's targeted supports to vulnerable groups.
Structural Risks			
Deepening geoeconomic fragmentation	**High** Broader and deeper conflict(s) and weakened international cooperation result in a more rapid reconfiguration of trade and FDI, supply disruptions, protectionism, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial systems, and lower potential growth.	**High** Cabo Verde is an open economy, highly dependent on trade (food, intermediates, and fuel), remittances and tourism. Hence any disruption on each of these areas is bound to deeply affect economic activity. The impact however could be mitigated by country's strong international trade ties.	• The limited fiscal resources should be prioritized and allocated to investments that increase diversification across tourism source markets. • Contingency planning should be undertaken in anticipation of operational or financial disruptions. • Accelerate the implementation of structural reforms to support international competitiveness and productivity.
Cyberthreats	**Medium** Cyberattacks on physical or digital infrastructure (including digital currency and crypto assets ecosystems) or misuse of AI technologies trigger financial and economic instability	**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.
Extreme climate events	**Medium** Extreme climate events driven by rising temperatures cause loss of human lives, severe damage to infrastructure, supply disruptions, lower growth, and financial instability	**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. • Prioritize public investments projects resilient to climate change, improve risk management and building codes.

Source of Risks	Relative Likelihood	Impact if Realized	Policy Response
Domestic			
Faltering fiscal consolidation efforts	**Medium/High** Less ambitious and slower fiscal consolidation efforts and delayed SOEs reforms as the economy recovers.	**High** Delayed fiscal consolidation efforts and SOEs reforms would undermine macroeconomic stability and hinder the return to pre-COVID medium-term fiscal and debt sustainability trajectory.	Unwind temporary measures, 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.

Annex II. Capacity Development Strategy

1. The IMF Technical Assistance (TA) will support the ECF and the RSF arrangement's objectives. Capacity Development (CD) priority areas are aligned with the authorities' reform agenda under their medium-term development strategy (PEDS II). Consequently, the core of the Fund CD activities will focus on strengthening revenue mobilization, improving public investment management, reducing fiscal risks, strengthening the monetary policy transmission mechanism, and improving collection and dissemination of macroeconomic and financial statistics. With respect with RSF program objectives, Fund TA will be provided to establish climate-related issues in fiscal planning and budgeting and on public investment, distributional impact assessments, and on climate finance.

2. The authorities' commitment to the implementation of CD recommendations is good, though hampered by limited administrative capacity and staffing. Cabo Verde is a high-intensity CD user and with relatively appropriate institutional capacity and good track record of implementing TA recommendations. The CD strategy aims to ensure adequate integration of CD recommendations with policy advice in the context of surveillance and program design. CD will also be used, where appropriate, to help support climate related reform measures. It also seeks to support effectiveness, understand the political economy of reforms and to avoid overlap of CD activities through enhanced coordination with IMF CD departments, AFRITAC West 2, and other CD providers. An intensification of hands-on training and peer learning could be ways to increase traction and advance with reforms. The main CD priorities and objectives are summarized in the table below.

Priorities	Objectives	Challenges
Revenue administration	Improve customs administration core functions; strengthen management and governance arrangements; enhance compliance with tax obligations; improve the quality of tax audits and inspections in the tax administration, keep the digitalization modernization agenda at DNRE, enhance compliance risk management strategies, and revamping the existing tax exemptions regime.	Staffing; lack of structured coordination between tax and customs areas.
Tax Policy	Rationalization of tax incentives; identification of new potential sources of revenue; ensure the effectiveness, efficiency, and equity of the incentives in practice for the socio-economic development of the country; institutional reform supported by the creation of a Tax Policy Unit within the Ministry of Finance.	Institutional and staffing constraints.

Priorities	Objectives	Challenges
Public Financial Management	Improve the integration of the assets and liabilities management framework; improve coverage, quality of and access to fiscal reporting; improve budget execution and control; strengthen identification, monitoring and management of fiscal risks; increase efficiency in public investment management (PIM) and follow up CD to implement the recommendations of the C-PIMA; enhance public expenditure management (PFM); assist to improve the introduction of climate dimension in budgeting and public investment; distributional impact assessments.	Staffing constraints.
Real Sector Statistics	Strengthen the compilation and dissemination of macroeconomic and financial data by further improving and extending the national accounts indicators, updating the CPI and increasing staff capacity. Monthly High Frequency Indicators.	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, and central bank's governance structures.	Staffing constraints.
Banking supervision and financial stability	Strengthen the bank and non-bank supervision processes and implement risk-based supervision, follow up of the 2022 FSSR road map and recommendations, and implementation of IFRS, climate finance	Staffing constraints.

Annex III. Cabo Verde's Energy-Water Climate Nexus

Cabo Verde's Exposure to Climate Change

1. Cabo Verde faces significant development challenges from structural factors. Cabo Verde is a small economy which comprises of a group of islands, with fragile ecosystems, that are prone to floods and droughts. The World Bank estimates that the average economic damage from natural disasters, particularly floods, costs just under 1 percent of GDP per year, causing damage to the capital stock and disrupting economic activity. The economy suffers from a poor natural resource base, including serious water shortages exacerbated by cycles of long-term drought which has adverse implications for agriculture and tourism, two key activities in Cabo Verde. The resulting reliance on external provision of vital resources, including food and energy, exposes the country to global market fluctuations, which affect especially the vulnerable and poor.

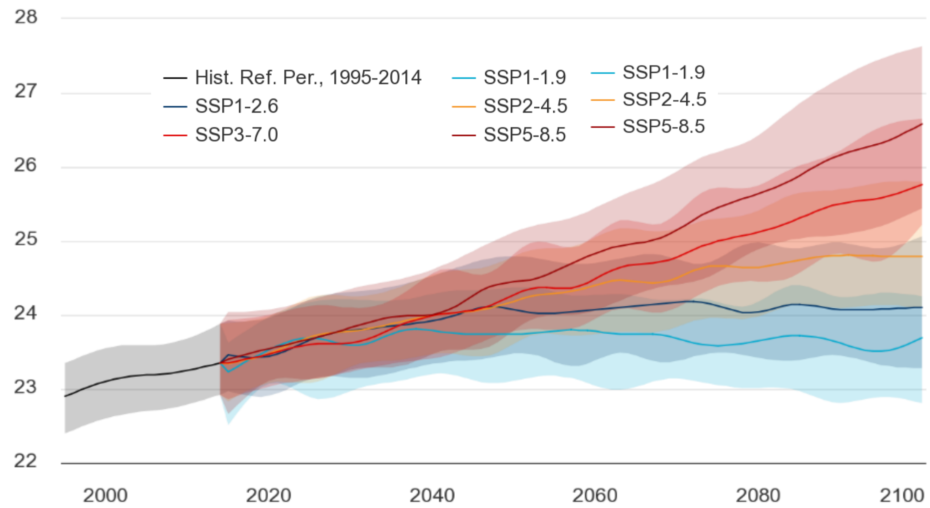
2. In addition, Cabo Verde is vulnerable to range of climate change risks. Climate projections indicate that the temperature in Cabo Verde could increase by 0.5°C to 4°C, by the end of the century (Figure 1a), impacting the ecosystems. Downward trends in annual precipitation, with potentially higher seasonal volatility (Figure 1b), further exacerbate the cycles of long-term drought and risks for floods (Figure 1c), both of which have adverse implications for agriculture and tourism, i.e., livelihoods and the economy. As an island nation, it is vulnerable to sea level rise (SLR); coastal communities (where 80 percent of the population resides), economic operations (especially tourism), and infrastructure are particularly exposed to this type of climate related risk.

3. Climate change vulnerabilities are amplifying the development challenges, building a climate-energy-water nexus.

- Changing precipitation patterns are aggravating water scarcity, increasing the need for provision of water for human consumption and irrigation.
- Water scarcity is being addressed through energy intensive desalination efforts.
- Cabo Verde heavily relies on imported petroleum for 80 percent of its energy, resulting in high energy costs and making freshwater a costly good.
- Heavy reliance on imported food and energy makes Cabo Verde vulnerable to global market fluctuations, disproportionately impacting vulnerable populations.
- Tourism, a key GDP contributor, relies on water and imports; in addition, global price fluctuations worsen income inequality and food insecurity.

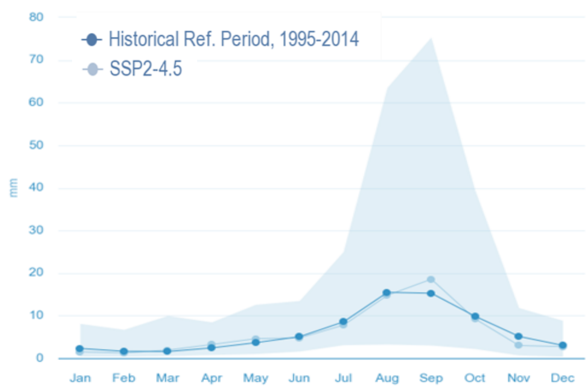
Figure 1. Cabo Verde: Climate Change Vulnerabilities in Cabo Verde

a. Projected Mean Temperature Multi-Model Ensemble (Reference Period 1995-2014)

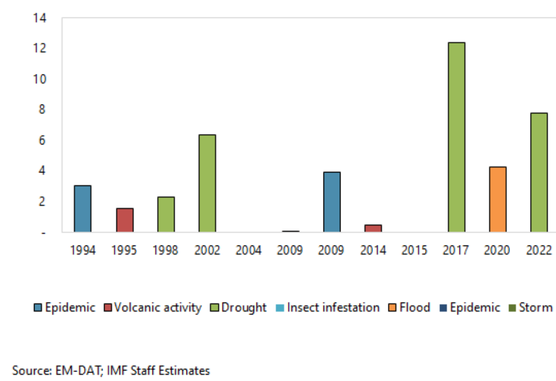


Source: World Bank, Climate Change Knowledge Portal.

b. Projected Precipitation, SSP2-4.5



c. Disaster by Type
(percent of population affected)[1]



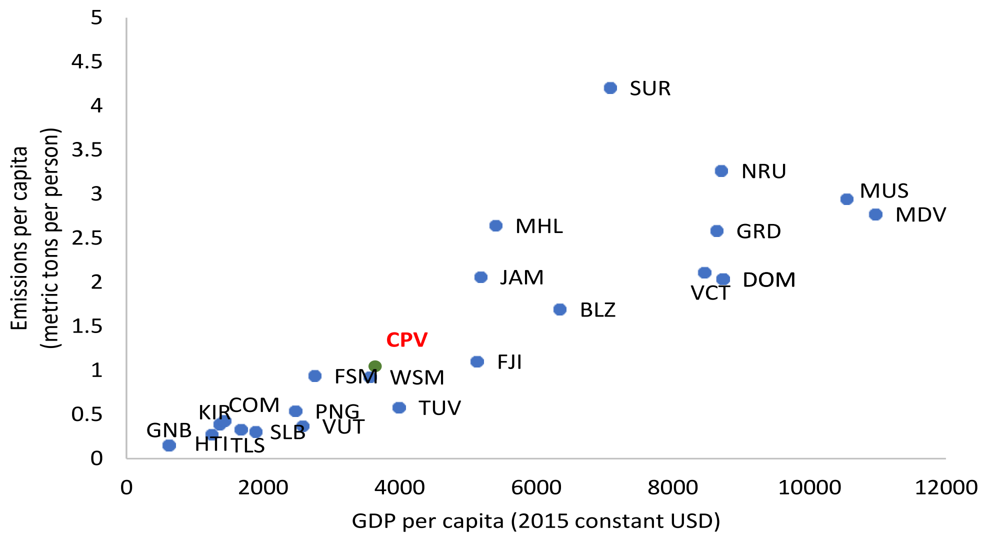
Source: EM-DAT; IMF Staff Estimates

[1]Staff acknowledge that the EM-DAT does not report the actual economic impact of an event but only provides estimates. A better indication of economic impact of a disaster would be the cost of insurance or reinsurance, if available.

4. **Cabo Verde's contribution to global emissions is very small with most emissions coming from the energy sector**. Globally, Cabo Verde ranks as the 189th largest emitter, contributing 0.0018 percent to total global emissions. Per capita emissions are at par with other Small Island Developing States (SIDS) of similar income level (Figure 2). Cabo Verde's performance aligns with several SIDS peers. The energy sector accounts for most emissions and contributed most of the historical emission growth, with emissions almost tripling since 1995 with the expansion of thermal generation capacity to meet the growing electricity demand and the rise in fuel demand for road transportation (Figure 3). In the same period, emissions from agriculture and waste rose by about 120 and 60 percent, respectively. Given

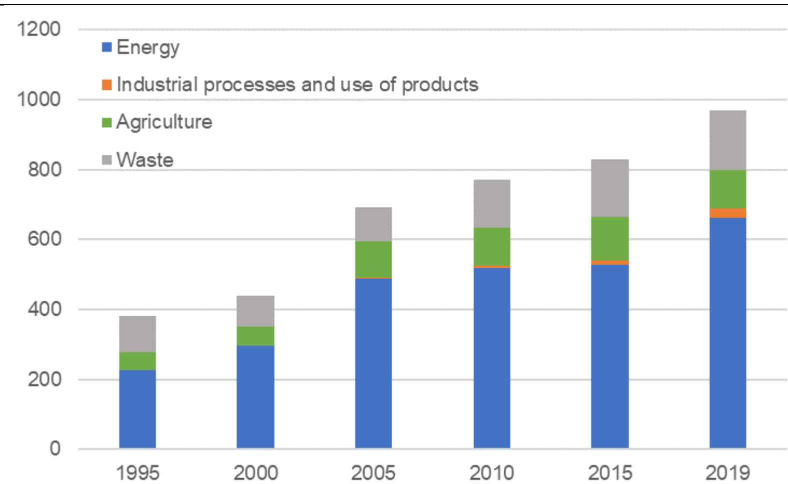
the structure of Cabo Verde's service-oriented economy, the industrial sector constitutes a relatively small proportion of overall emissions.

Figure 2. Cabo Verde: Emissions Per Capita in Small Island Developing States
(metric tons)



Source: IMF staff using World Development Indicators.

Figure 3. Cabo Verde: Historical GHG Emissions in Cabo Verde (in CO2e, Excluding Land Use, Land Use Change, and Forestry (LULUCF))



Source: Preliminary National Emission Inventory, 2023.

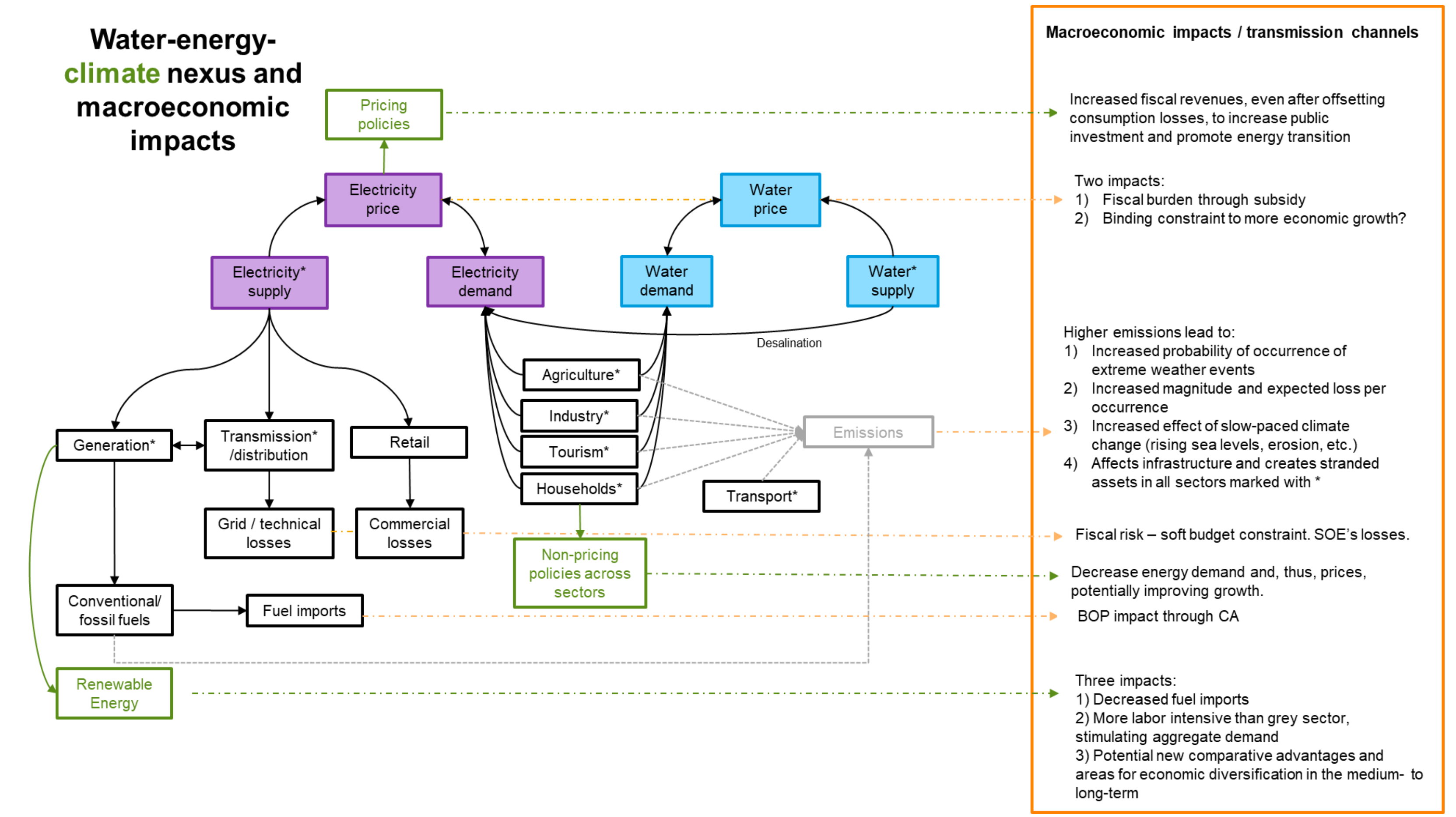
Policies to Improve Adaptation and Mitigation

5. The expansion of the water supply is expected to continue relying on desalination, which will increase energy demand, requiring close coordination between the two sectors. The 2015 National Strategic Plan for Water and Sanitation (PLENAS) suggests that demand for water, for human consumption and for irrigation, could be five times higher in 2030 than in 2022. Irrespective of the exact numbers, the expected demand increase linked to growing tourist numbers, as well as from the ambitious irrigation program, is considerable. Desalination plants may be built with their own solar-based energy supply but will need to rely partly or in full on the electricity grid for energy provision unless storage is also built. To ensure continued stability of the electricity network, the electricity grid must be fit for the highly volatile energy supply pattern from renewable energy (RE) sources, so that it matches the constant demand from the continuous operation of desalination plants.

6. The inseparability of energy and water, i.e., of mitigation and adaptation comes with significant challenges but, if well managed, also offers important opportunities. The complexity of energy and water sector challenges, the reform needs and the interconnection between these services and other key sectors, including agriculture and tourism, requires strong leadership and coordination from and within the government (Figure 4). Energy transition, replacing costly and emission intensive thermal energy with lower cost RE sources, will improve the availability and affordability of energy and water while reducing emissions.

7. Cabo Verde has an ambitious plan for RE in electricity generation (2021 NDC). The goal is to increase RE from below 20 percent in 2021 to 30 percent in 2025, 54 percent in 2030, and ultimately reach 100 percent by 2050. This involves doubling the current RE capacity by 2030. Cabo Verde has substantial untapped RE potential identified in the Electricity Master Plan 2018–2023. Solar energy represents 80 percent of this potential, with 12 percent from wind sources and 5 percent from marine energy resources (Figure 5). This abundant RE potential positions Cabo Verde favorably to achieve its sustainability and climate objectives.

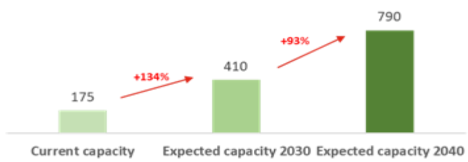
Figure 4. Cabo Verde: Climate-Energy-Water Nexus



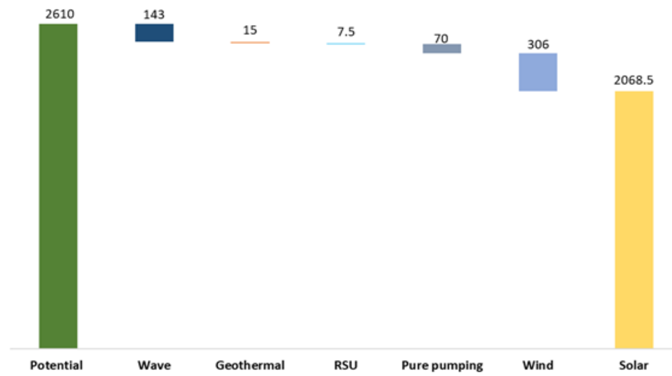
Source: IMF Staff.

Figure 5. Cabo Verde: Current and Potential Renewable Energy Capacity

a. Renewable energy current capacity and expected capacity according to NDC (MW).



b. Potential renewable energy capacity by source (MW).



Source: IMF staff using EMP 2018-2040 and NDC.

8. Electricity and water sector operators face important financial challenges. While the energy sector is managed at the national level and the water sector at the municipal level, both sector face similar structural challenges. Energy and water tariffs have not covered the cost-of-service provision and the publicly owned utilities have accumulated losses. This has resulted in a financially unsustainable situation for several entities, including the national electricity company and several municipal water companies, resulting in a low-quality, low-tariff cycle. Important reforms are ongoing in both sectors to address these challenges:

- **Electricity**. To enhance the viability and performance of the energy sector, ELECTRA (*Empresa de Electricidade e Água*), the national electricity and water company separated the electricity and water businesses and started the unbundling of electricity services. The latter, supported by the World Bank, will be an important step towards creating a transparent and competitive environment conducive for private sector investment in energy production. To this end, it will be important to improve the management and financial performance of the publicly owned transmission and distribution companies to make them a reliable partner for private sector investors, who will have to rely on the public sector entity as the single buyer and off taker. Without further investment, Cabo Verde will only be able to move to about 35 percent RE, far below the 2030 objective of 54 percent. Important public infrastructure investment, including in storage, will be required to move beyond 35 percent renewable target in the energy mix. The coordination required to synchronize the strengthening of grid infrastructure and the expansion of RE capacity is exacerbated by the segregation of the grids, which need to be managed on an island-by-island basis.

- **Water**. Operations of the water sector have been consolidated, moving from a municipality-by-municipality approach to a multi-municipality island-by-island setup. Operators are appointed for each island and are responsible for the operation of the distribution system. Several important operators, including the largest one on Santiago Island, are running considerable technical and commercial losses, losing up to 60 percent of generated water in the distribution. In combination with a tariff structure that does not cover the full cost of service provision, these losses are leaving the operators in a financially unsustainable situation. Addressing the technical losses will require substantial investment in distribution infrastructure. To motivate these investments and potential increases in water tariffs, the cost of the losses and their sources need to be identified and made transparent.

9. **Adaptation will require ecological and sustainable use of water resources, as well as greater energy efficiency**. And this depends on a conducive environment to catalyze private investment in climate change resilience. To facilitate this, operators in both sectors need to be compensated for the cost-of-service provision either through the tariff, which might require increasing electricity and/or water tariffs, or through a combination of the tariff and a government transfer from the budget in case the government regulates the tariff, e.g., by providing a social tariff. Putting the sector on a sound economic footing and allowing the operators to run their organizations under commercial-like terms, can enhance efficiency and creates transparency and competition.

10. **The adverse implications of any adaptation and mitigation reforms on the vulnerable or poor should be compensated through targeted transfers from the social safety net**. The reliability of the social safety net could be enhanced by expanding the social registry towards universal coverage. The cost to the government of introducing higher tariffs and compensating the vulnerable and poor could be neutral, while improving the situation of the households that receive compensation. Compensation measures can also be designed to compensate the vulnerable and poor from the impact of the tariff increase while providing extra revenues to the government. A careful design of such a reform and the implementation of a well-designed communication strategy is critical for ensuring the full benefit while avoiding social and political opposition to the reform.

11. **Energy-related initiatives, with an emphasis on the power and transport sectors, are of pivotal importance in the pursuit of Cabo Verde's mitigation objectives**. To this end, the government is currently focusing on the unbundling of the state-owned enterprise ELECTRA. Additionally, efforts are concentrated on diminishing energy intensity and fostering energy efficiency, increasing renewable energy deployment, and lowering the carbon intensity of mobility. The government is also working to shift towards responsible tourism and circular economy and fostering the natural sink function of ecosystems.

12. **Building climate change resilience will require substantial investment in energy and water infrastructure**. Infrastructure poses a binding constraint for the efficient operation of the electricity and water sectors and the acceleration of the energy transition. The current electricity infrastructure has only limited capacity to incorporate RE. Cabo Verde's ability to benefit from the transition to a clean and less expensive generation matrix is limited, since it must maintain significant thermal capacity to cover demand when RE is not available. For the energy sector investment should focus on wind and solar capacity, energy storage solutions and grid reinforcement, e-mobility, and energy efficiency measures. The water sector infrastructure is partly outdated and worn down, causing substantial technical losses and making the service provision

costly and inefficient. For the water and sanitation sector, priority investments include sustainable energy for desalination and distribution of water intended for human consumption and for irrigation, network infrastructure, desalination capacity, and capacity for the treatment and recovery of wastewater.

13. **Adaptation and mitigation, including for energy and water, are estimated to require about USD 2 billion of public and private investment over the next decade**. This amounts to almost 6.1 percent of GDP a year, compared to a projected annual public investment budget of about 3.8 percent of GDP. To implement these actions, while maintaining debt sustainability, additional concessional resources would be needed for public investment, as well as increased private investment. The RSF aims to help these efforts by providing funding and setting the groundwork for additional, climate sensitive, investment.

Governance and Coordination of Climate Change Policy

14. **Cabo Verde has made tackling climate change a key part of its national strategy, but the critical issue is the actual implementation road map and monitoring**. Climate action is a key part of the PEDS II priorities/pillars. The NDC and the NAP present high-level mitigation and adaptation ambitions for key sectors and policy areas, emphasizing resilient infrastructure in the following six areas: i) water; ii) agriculture; iii) oceans and coastal zones; iv) transport; v) disaster risk reduction; and vi) health. The authorities are focused on climate mitigation goals geared to reduce energy intensity; improve energy efficiency; shift towards low carbon economy; and increase forest area. In this context, Cabo Verde aims to reduce domestic GHG emissions by 18 percent unconditional (24 percent conditional) compared to the 2019 Business-as-Usual (BAU) scenario by 2030 and achieve net-zero emissions by 2050.

15. **The overall coordination of climate change related policies and disaster risk management should be improved**. The government has taken important steps towards sector-by-sector planning; however, more is needed to ensure that climate change implications are fully incorporated and to foster cross-sector consistency of policy measures. For example, while the 2020 update to the first Nationally Determined Contribution (NDC) and National Climate Change Adaptation Plan (NAP) outline general policy objectives, specific sectors, such as energy and water, are responsible for defining detailed objectives and policy measures in their respective plans. Both sectors are undertaking reforms to address challenges, aiming to improve their financial sustainability and service quality, while also addressing the climate challenges. However, improving coordination between these interdependent sectors remains a significant challenge. Disaster risk management practices should be strengthened. The economic impact of disasters and climate change on infrastructure needs to be better understood, including the fiscal risks associated with public assets. While some ex-ante financing mechanisms for natural disaster risk to infrastructure have been established, it is important to ensure that the current disaster financing instruments are adequate.

16. **Similarly, in public investment management work remains to be done to enhance climate-awareness and climate resilience**. Progress has been made in developing a

comprehensive climate change policy framework, spatial planning, coordination with municipalities, and in planning for disaster risk financing. However, central government coordination is weak, lacking a strategic leader for adaptation or mitigation investments.

17. A high-level public institution should provide strong leadership, cross-government coordination and promote awareness of the implications of climate change. This would better support resilience building and the management of climate-change related challenges. The awareness of climate change implications across government entities and the capacity for assessing its potential consequences is limited. While the government has started working on closing important information gaps, for example related to climate scenarios and hazard vulnerability mapping, these efforts are still at an early stage. Sectors which rely largely on private investment, such as tourism, are not being guided on the long-run impact of climate change scenarios nor being regulated to mitigate those risks. Generation and dissemination of consistent information regarding the expected implications of climate change will be an important step towards creating awareness and guiding climate-sensitive policy making.

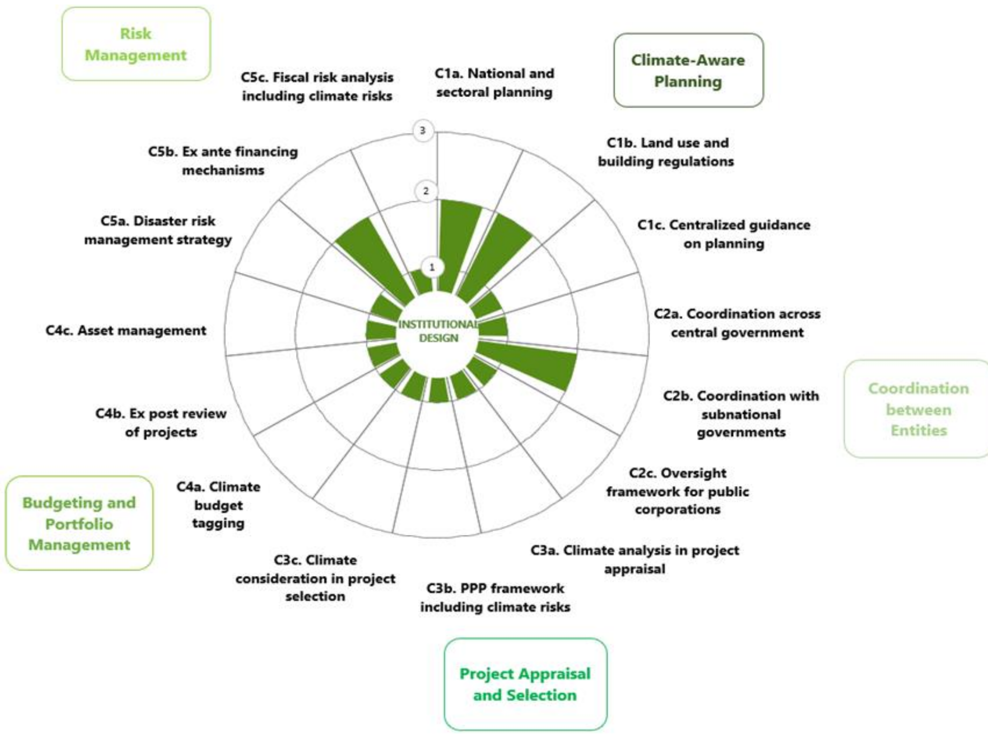
Policies to Improve Fiscal and Physical Resilience to Climate Change

18. The C-PIMA identified that climate change considerations are not adequately integrated into the public investment planning process. There is a need to improve awareness of climate-related risks in fiscal planning. The World Bank's Developing Policy Financing (DPF) loan has conditions that support improved Public Investment Management (PIM), and the RSF will complement them to ensure that better risk analysis and investment planning are also applied to Public-Private Partnerships (PPPs), thus playing a catalytic role in attracting climate finance.

19. Cabo Verde's public investments are particularly vulnerable to the impacts of climate change due to the country's socio-economic and geographical specificities. Climate change is expected to affect Cabo Verde's population and assets which are mainly located in coastal cities through a projected sea level rise, which would increase coastal submergence, erosion, flooded lands and salinity of small estuaries, streams, and coastal waters. There is also increased exposure of assets and people to adverse natural events due to urban development into risk-prone areas.

20. Key investment drivers outside central governments are not adequately incorporating climate change considerations. The regulatory framework for public enterprises (PEs) does not align with national climate policies, even though PEs drive public investments. PPPs lack clear climate risk allocation guidelines, despite the increasing use of this investment modality. Investment project appraisal and selection practices do not exist. Climate-responsive spending in infrastructure is at a concept development stage. Ex-post reviews or external audits of projects on climate outcomes are not conducted, and climate impact is not integrated into public asset management.

Figure 6. Cabo Verde: Institutional Strength of C-PIMA Institutions in Cabo Verde



Source: Cabo Verde C-PIMA.

21. Key C-PIMA recommendations have been included in the World Bank's DPF loan to foster climate sensitive and efficient public investment management. The DPF foresees the development and approval of a PIM legal framework regulating the whole capital project cycle (planning, appraisal, selection, capital portfolio management, etc.) and including climate considerations. Another World Bank's DPF condition relates to the inclusion of climate and disaster risks assessment in the preparation of public investment projects. The World Bank's DPF loan also foresees climate budget tagging to improve visibility and tracking of climate investments.

22. The authorities plan to increase the resilience of the country 's macro-fiscal stance to climate change, by integrating climate risks into fiscal planning. This is in line with the C-PIMA assessment and complements the World Bank's engagement. An institutional framework for fiscal risks assessment and analysis has been put in place.[1] The 2023 Fiscal Risks Statement (*Declaração dos Riscos Orçamentais*) identifies disaster risks such as rainfall, flooding, and drought, and the authorities plan to improve this analysis by further conducting quantitative assessments of risks by assessing long-term fiscal sustainability under different climate change scenarios.

[1] In July 2018, a Risk Management Service was created within the Treasury Department of the Ministry of Finance (MOF) to manage operational fiscal risks. In 2022, the government created a high-level Fiscal Risk Coordination Committee, explicitly tasked with managing fiscal risks associated with climate and disaster risks.

23. Cabo Verde plans to add climate change requirements into the PPP legal framework, as PPPs could be a good source of climate-related financial flows and can promote sustainable practices and technological innovation. Compared to other African countries, Cabo Verde has been dynamic in developing PPPs. The PPP capital stock in Cabo Verde stood at 3 percent of GDP in 2019, close to Mauritius (3.3 percent of GDP) and South Africa (4.6 percent of GDP). However, the private sector does not support mobilization of resources for climate action, and its involvement in climate considerations has been weak. Among other obstacles, the private sector has been constrained by weaknesses in the national PPP framework. The legal framework for PPPs has been in place for almost a decade, but it does not include climate-related aspects. The authorities aim to amend the existing policy and regulatory framework to include climate requirements in PPP project agreements from project identification to contract management, including comprehensive insurance policies to distribute among the PPP partners the burden of contingent liabilities related to natural disasters. The PPP reform complements the WB DPF loan's conditionalities, which address different and distinct aspects of the PIM such as general PIM legal and regulatory framework (not applicable to PPPs), climate budget tagging, and climate considerations in project appraisal.

24. In line with the Cabo Verde's 2021 NDC, the authorities plan to adopt a national climate finance mobilization strategy. This will include different financing instruments and aim to develop a robust pipeline of climate investment projects. Financing adaptation and mitigation actions will require substantial financial resources—estimated at around USD 2 billion over the next decade, half for mitigation and half for adaptation. Cabo Verde has a range of financing mechanisms to drawn on to meet the climate costs: (i) a dedicated environmental fund which generates about USD 7 million per year, mainly from taxes on plastics: (ii) a Sovereign Emergency Fund (Fundo Soberano de Emergência or FSE) established with the purpose of funding, among other things, the restoration and reconstruction of public infrastructure following disasters; and (iii) Cabo Verde launched its first blue bond on the Blu-X sustainable finance platform in January 2023.[2] The authorities are also exploring the establishment of a new Climate and Nature Fund with technical assistance from the World Bank. However, the climate financing gap remains large and is contributing to the slow implementation of some climate initiatives. In addition, the choice of financial tools in Cabo Verde appears to be based more on opportunities than on a robust assessment of the most cost-effective instruments. The government also does not dispose of a pipeline of appraised capital projects. As, underlined by the C-PIMA, most projects included the capital investment plan (Programa de Investimento Público, (PIP)) are externally funded and its inclusion in PIP results from negotiations with development partners. No projects are included in PIP based on the explicit appraisal and selection criteria. The distinction between a capital and a development project is also not clearly mainstreamed in the PIP.

[2] This is the first Initial Public Offering (IPO) listed on Blu-X, and the bond could generate $3.5 million in private finance. The bond aims to raise investment in Cabo Verde's Ocean economy while divesting from polluting industries. The proceeds will support microentrepreneurs, startups, and small and medium-sized enterprises in coastal communities.

25. The envisaged climate change reforms will also help catalyze private funding. The tourism sector has shown the ability of Cabo Verde to attract international investment. Improving the management and financial performance of operators in the energy and water sector, as well as developing a list of bankable projects, have the potential to catalyze additional financing in new sectors. More clarity on climate change risks, using climate scenarios and vulnerability mapping, will allow private investors to better understand and manage these risks, thus it may lower risk premiums and facilitate investment.

Collaboration with Other Partners

26. Cabo Verde has worked closely with bilateral and multilateral partners in supporting its climate change agenda. In terms of bilateral support, Portugal, and Luxembourg, two of Cabo Verde's main bilateral partners in terms of the amount of aid and financing provided, have large climate components in their programs:

a. In the case of Portugal, the recent debt-for-financing swap agreement will provide seed money for the Climate and Nature Fund and allow financing of climate change projects, although the procurement will be restricted to Portuguese firms. This is being presented as a model that could be emulated by other bilateral creditors.

b. In the case of Luxembourg, one of the priority topics is access to water and sanitation and to electricity, with emphasis on the quality of access to these basic services. It also has a focus on RE. The advantage of this support is that it is large, multiannual, all grant-based, and unrestricted in terms of its use (it can be used for budget support).

c. Another bilateral partner working on climate change issues is Saudi Arabia, who are financing a project on water management through BADEA and the Saudi Development Fund.

27. Multilaterals are also supporting the climate change agenda through financing and CD. The World Bank is preparing a DPF with a major focus on strengthening PIM capacity and is providing technical assistance to the government in the unbundling of the electricity utility. It has started its Country Climate and Development Report (CCDR) for Cabo Verde. The RSF work is coordinated with the WB team. The AfDB has worked on electrification along with JICA in the past and could reengage if the overall risk of debt distress is lowered to moderate. The latest technology employed in electrification in Cabo Verde has allowed for significant reductions in technical losses.

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Annex IV. Debt Decomposition and Capacity to Repay

Table 1. Cabo Verde: Decomposition of Public Debt and Debt Service by Creditor, 2022-24[1]

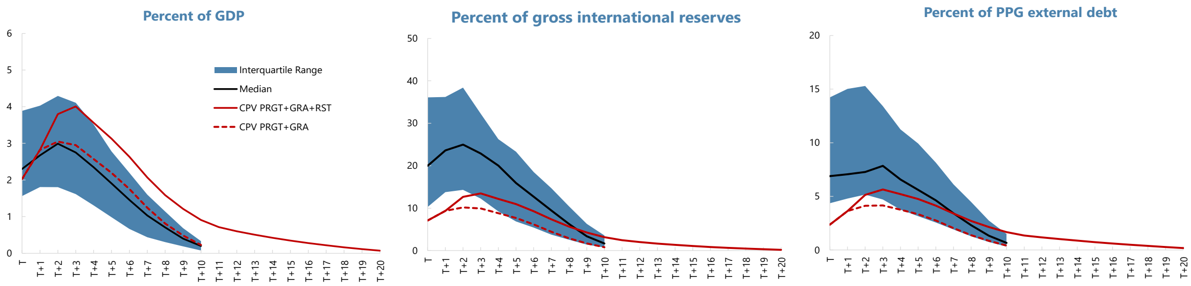
	Debt Stock (end of period)			Debt Service					
	2022			2022	2023	2024	2022	2023	2024
	(In US$)	*(Percent total debt)*	*(Percent GDP)*		*(In US$)*			*(Percent GDP)*	
Total	2855.4	100.0	127.1	195.0	250.9	254.7	8.7	9.7	9.2
External	2048.0	71.7	91.2	98.3	102.3	108.3	4.4	4.0	3.9
Multilateral creditors[2]	1115.6	39.1	49.7	44.0	44.5	48.5	2.0	1.7	1.8
IMF	65.4	2.3	2.9	0.0	0.0	0.0	0.0	0.0	0.0
World Bank	541.3	19.0	24.1	14.3	11.6	12.5	0.6	0.5	0.5
African Development Bank Fund	279.0	9.8	12.4	16.6	18.9	21.9	0.7	0.7	0.8
European Investment Bank(incl.EEC)	32.1	1.1	1.4	3.8	3.9	3.9	0.2	0.2	0.1
Other Multilaterals	202.8	7.1	9.0	8.8	10.2	10.2	0.4	0.4	0.4
BADEA	39.9	1.4	1.8	0.4	0.4	0.6	0.0	0.0	0.0
CEDEAO	7.9	0.3	0.4	0.9	0.7	0.8	0.0	0.0	0.0
FAD	102.7	3.6	4.6	4.1	4.9	5.2	0.2	0.2	0.2
Bilateral Creditors	399.5	14.0	17.8	24.0	26.7	29.0	1.1	1.0	1.0
Paris Club	202.5	7.1	9.0	13.8	18.2	18.4	0.6	0.7	0.7
France	52.0	1.8	2.3	5.0	5.5	5.9	0.2	0.2	0.2
Japan	73.2	2.6	3.3	1.8	3.2	3.3	0.1	0.1	0.1
Other (Spa, Belg, Aus, Swed)	72.6	2.5	3.2	7.0	9.6	9.1	0.3	0.4	0.3
Non-Paris Club	197.0	6.9	8.8	10.2	8.4	10.6	0.5	0.3	0.4
Portugal	154.5	5.4	6.9	5.1	3.3	5.6	0.2	0.1	0.2
China	29.1	1.0	1.3	3.3	3.6	3.6	0.1	0.1	0.1
Kuwait	13.4	0.5	0.6	1.7	1.4	1.4	0.1	0.1	0.1
Bonds	0.0	0.0	0.0	-1.0	0.0	0.0	0.0	0.0	0.0
Commercial creditors	411.4	14.4	18.3	40.4	38.6	38.4	1.8	1.5	1.4
BPI	0.0	0.0	0.0	10.6	6.0	5.9	0.5	0.2	0.2
Caixa Geral Déposito (CGD)	407.7	14.3	18.1	29.7	32.7	32.4	1.3	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	870.7	30.5	38.8	131.9	148.6	146.4	5.9	5.8	5.3
T-Bills	26.2	0.9	1.2	0.0	0.0	0.0	0.0	0.0	0.0
Bonds	838.0	29.3	37.3	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memo items:	202.0	7.1	9.0						
Collateralized debt[3]	0.0	0.0	0.0						
Contingent liabilities[4]	202.0	7.1	8.6						
o/w: Public guarantees	202.0	7.1	9.0						

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 Arrears).
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 stream to 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. Collateral is "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).

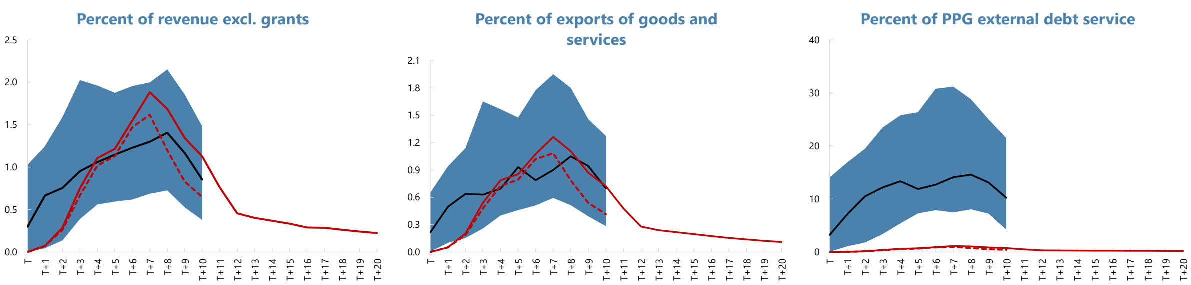
Figure 1. Cabo Verde: Capacity to Repay Indicators Compared to UCT Arrangements for PRGT Countries

(Percent of the indicated variable)

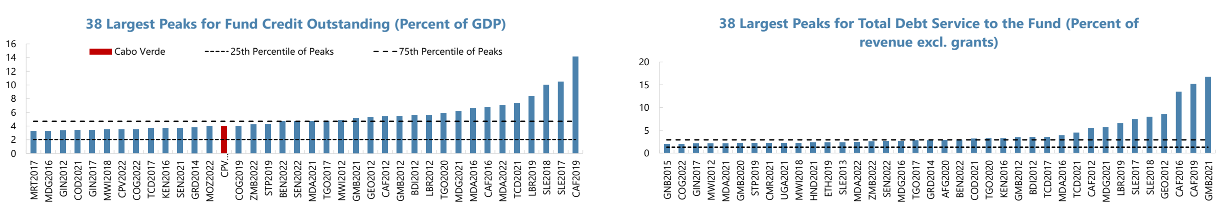
A. Total Fund Credit Outstanding



B. Total Debt Service to the Fund



C. Largest Peaks



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 2012 and 2022.
4) PRGT countries in the control group with multiple arrangements are entered as separate events in the database.
5) Comparator series is for PRGT arrangements only and runs up to T+10.
6) Debt service obligations to the Fund reflect prospective payments, including for the current year.
7) In the case of blenders, the red lines/ bars refer to PRGT+GRA. In the case of RST, the red lines/ bars refer to PRGT+GRA+RST.

Appendix I. Letter of Intent

Praia

November 22, 2023

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 the continuous support provided to the Republic of Cabo Verde under the current Extended Credit Facility (ECF) program. Our efforts to meet balance of payments needs, sustain foreign exchange reserves, and restore conditions for more resilient growth have played a vital role in the current strong recovery, despite the challenging global environment. The Government of Cabo Verde with the IMF's support under the three-year ECF continues to implement its economic and financial program that is aligned to the new Sustainable Development Strategy 2022-2026 (PEDS II), sustaining the economic recovery, building buffers, and dealing with climate challenge.

Our country's macroeconomic performance under the three-year ECF arrangement has been strong. All quantitative performance criteria (QPCs) for end-June 2023 were met. The indicative targets (ITs) for end-March and end-June 2023 were met. Regarding structural benchmarks (SBs), those for end-June, end-July, and end-September 2023 were met. Bearing in mind the program achievements to date, we are requesting a disbursement equivalent to SDR 4.5 million (or 19 percent of our quota). We request the modification of the PC on the PV of new external debt for end-December 2023. We also requested a clarification of the definition of deposits under *other net liabilities* in the TMU (from a stock to a flow), and a modification of the PC on *other net liabilities* in December 2023 and June 2024 to reflect the delay in 2023 privatization receipts from public enterprises in the pharmaceutical and banking sectors.

Risks related to climate change pose an increasing threat to our country's favorable growth and development prospects. Our country is indeed one of the world's most vulnerable to the effects of climate change, because of the preponderance of rainfed agriculture and the increased frequency and severity of droughts and floods, resulting in marked volatility in economic activity. Efforts to combat climate change are therefore a top priority on the government's agenda, and national and sectoral strategies have been developed accordingly to address the country's vulnerabilities. However, given the challenges we face, we will need the support of external financial partners to implement the reforms and investments planned in the context of our climate change adaptation and risk mitigation policies.

The government is committed to strengthen the resilience to climate change. To this end, the Government requests access to the Resilience and Sustainability Facility for an amount of SDR 23.7 million (100 percent of quota) to implement reform measures (RMs), as presented in the Table 3 attached to the Memorandum of Economic and Financial Policies (MEFP), with an articulated five pillars: (i) strengthening climate change policy governance; (ii) improving physical and fiscal resilience; (iii) strengthening mitigation and resilience through energy efficiency and transition; (iv) promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts; and (v) financial sector resilience to climate change. The RSF resources will help support the government's ongoing efforts to respond to the pressing challenges of climate change and strengthen the resilience of the economy and populations. In particular, it will support the implementation of new reforms aimed at equipping the government with modern tools for coordination, monitoring, assessing, and managing climate risks.

The attached MEFP, which supplements the memorandum signed on June 6, 2023, describes the recent economic and financial developments, presents the economic and financial policies that the government intends to implement during 2023–25 and defines the quantitative criteria, indicative targets, and structural benchmarks through end-December 2024. Disbursements under the arrangement will be subject to observance of the performance criteria and structural benchmarks shown in Tables 1 and 2 of the attached MEFP. The economic and financial policies described in the MEFP continue to provide a robust macroeconomic framework that promotes the mobilization of financing from development partners, strengthens public institutions and good governance, and increases the resources allocated to protection of the most vulnerable segments of the population, including to better tackle the food and energy crisis. Finally, we will provide Fund staff with all data and information necessary to assess the policies and measures presented in the Technical Memorandum of Understanding (TMU).

During the implementation of the RSF arrangement, we will maintain a close policy dialogue with the IMF and will consult it in advance of any revisions to the RMs contained in the MEFP, in accordance with the Fund’s policies on such consultations. Moreover, we will provide the IMF with information in connection with our progress in implementing these measures and achieving their objectives, which is linked to the disbursement schedule under the RSF.

The government commits to providing the IMF with information on implementation of the agreed measures and execution of the program, as provided in the attached Technical Memorandum of Understanding (TMU). In addition, the government authorizes the IMF to publish this letter and its attachments, as well as the staff report, once the review has been approved by the IMF Executive Board. 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 2023–25

This memorandum describes recent economic developments, the outlook for the medium term, and the program objectives, policies and measures to achieve them. The main objectives of the program include: (i) strengthening public finances to increase fiscal space for investment in catalytic sectors, as well as promoting social inclusion; (ii) reducing *fiscal risks from public enterprises; (iii) modernization of the monetary policy framework and strengthening the financial system; and (iv) raising growth potential and building resilience to shocks from climate related change.*

BACKGROUND, RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

1. **The Cabo Verdean economy continues its strong macroeconomic performance in 2023 and the near-term outlook is favorable despite some downside risks**. Cabo Verde's economy rebounded strongly in 2021 and 2022 and the strong macroeconomic performance continues with projected growth of 4.5 percent in 2023. Tourism arrivals have surpassed pre-pandemic levels with positive impacts in tourism-related sectors, and the near-term outlook is favorable despite some downside risks. Inflation is decelerating and the current account deficit narrowed in the first half of 2023. Reserves were also boosted by the ECF disbursements, the World Bank and the African Development Bank. As a result, gross international reserves remained stable at around €626 million through end-June 2023, and it is expected to reach 6.1 months of prospective imports by the end of the year. The economy remains vulnerable to external shocks that impact tourism activity, as well as to climate change risks.

2. **The fiscal position overperformed in the first half of 2023**. Economic activity supported the policy measures we took to increase tax revenues (22.6 percent 1H2023/1H2022). Primary expenditure only grew by 6.1 percent (1H2023/1H2022). On the spending side, slower growth in the wage bill and a fall in other current expenditures allowed a temporary expansion in subsidies, for supporting poor families, and acquisition of goods and services. Capital spending was slower than expected due to the starting phase of new projects. As a result, the primary balance over 1H2023 registered a surplus of CVE 2,759 million, compared with the CVE -4,141 million target under the program.

3. **We are on track in reducing the debt-to-GDP ratio in 2023**. The public debt-to-GDP ratio decreased from 127.1 percent in 2022 to 119.9 percent in 2023, mainly due to higher nominal growth and aided by the fiscal overperformance. We remain committed to keeping debt on a steady downward path.

4. The Monetary Policy Committee (MPC) tightened monetary policy to safeguard the peg. The MPC raised the policy rate from 0.25 to 1.0 percent in early May 2023 and then again to 1.25 percent on October 27 to narrow the differential with the ECB policy rate and protect reserves. We are moving cautiously in the tightening cycle as we close the interest differential and monitoring carefully any signs of softening by the ECB. The monetary stance also considers the tightening impact of the reversal of the COVID-related credit moratorium and the Long-Term Financing Program. We consider the projected reserve cover of 6.1 months of prospective imports adequate to protect the peg. At end-September 2023, M2 grew at 5.2 percent (y/y), total deposits by 5.5 percent and credit to the economy by 2.9 percent.

5. In 2024, we project growth to continue at around 4.7 reflecting a downward revision in global growth and a return to pre-pandemic levels of exports. Inflation is projected at 2 percent at end-December 2024. The current account deficit is expected to widen to about 5.5 percent of GDP in 2023 as exports of goods and services, tourism, remittances and FDI stabilize from levels recorded in 2022.

6. Our Sustainable Development Strategy 2022-2026 (PEDS II) provides the foundation for growth under the sound macro-economic management supported by the ECF program. Real annual GDP growth is expected to average 4.6 percent during 2024–28, driven by continued growth in the tourism sector and increased public sector investment spending. PEDS II will support growth by providing a framework for structural reforms. These include developing inclusive tourism, benefitting all the islands; transforming Cabo Verde into an air transportation hub and international business center; building a modern public administration; creating an international finance platform; developing a digital platform for technological innovation; establishing a special economic zone for the maritime economy (blue economy); supporting the development of wave energy and desalination technologies and facilitating investment opportunities developed locally or by the diaspora. PEDS II is supported by the policy measures agreed to under the ECF, which includes sustaining ongoing tax administration reforms, improved compliance, and measures to reduce tax expenditures, which will be included in the 2025 budget proposal.

7. The outlook is uncertain and subject to downside risks (geopolitical and climate). We see downside risks from weakened demand in major tourism markets and external price shocks. Fiscal risks could also stem from difficulties in advancing State-Owned Enterprise (SOE) reforms or pressures on the budget. The effects of climate change—a key medium-term risk—are evidenced in the recent years of drought. The country's high risk of overall debt distress remains a concern and thus concessional financing to limit debt servicing cost is important. On the upside, stronger tourism growth could lead to higher overall economic activity. Thus, we are cognizant of the need to accelerate implementation of climate adaptation measures to mitigate this risk. We are working on balancing the need for fiscal consolidation to reduce debt levels with capital spending to accelerate investments in climate action and are seeking support from partners (including the Fund) to access green financing. On the upside, stronger tourism growth could lead to higher overall economic activity. However, if the macroeconomic outlook deteriorates, we commit to take additional measures in consultation with the IMF staff.

REFORMS UNDER THE ECF-SUPPORTED PROGRAM AND THE RSF

A. Strengthening Public Finances to Preserve Public Debt Sustainability

8. **Our fiscal program focuses on a 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 1.9 percent of GDP in 2022 to a close to zero balance by the end of the program and a surplus of close to 1 percent of GDP in 2028; the overall fiscal deficit would decline from 4.1 percent of GDP in 2022 to a small deficit of around 0.7 percent of GDP balanced position over the same period. Medium-term revenue is supported by the implementation of the tobacco and alcohol tax, increasing the rate of the tourism tax, and charging import duty on previously exempt goods. This ambitious fiscal consolidation plan will lead to a reduction in public debt levels, with the debt-to-GDP ratio declining from 127.1 percent in 2022 to 93.9 percent in 2028.

9. **The 2023 fiscal outcome is likely to overperform the budget and the program targets under the ECF**. Data up end-August of 2023 suggests a strong improvement in revenue performance as total tax receipts increased by 19.3 percent and are projected above the indicative target set under the program. We expect revenue growth to remain buoyant for the remainder of the year driven by continued improvements in the tourism sector and supported by the revenue measures implemented under the program. We received the property income associated with the airport concession in August. Expenditures remained contained in line with our program objectives. Capital expenditure, budgeted at 4.8 percent of GDP, has progressed more slowly than planned. As a result, we expect a primary deficit of 1.1 percent of GDP.

10. **As a consequence, financing needs in 2023 are now projected to be lower than at the time of the first review**. Financing needs are projected at 3.4 percent of GDP compared to 4 percent at the first review. Domestic financing (-0.6 percent of GDP) is also lower than projected at the first review and is expected to remain below the legal rule of 3 percent of GDP. External financing will be filled mostly with concessional and partially concessional loans, mainly from multilateral institutions, including the World Bank (2.4 percent of GDP), African Development Bank (0.8 percent of GDP), the resources provided under the ECF program, and official creditors.

11. **The draft 2024 budget submitted to the parliament is in line with the ECF-supported program**. The draft budget is based on our growth forecasts and assumes higher tax collection of CVE 1.3 billion than IMF staff's projections. Budgeted primary expenditures reverse the 2023

increase in energy subsidies and include an additional CVE 1 billion capital spending relative to the last review. As a result, the 2024 draft budget primary balance is CVE 1 billion higher previous projections. While the primary deficit under the draft budget is 0.7 percent of GDP, the ECF program forecasts a primary deficit of 1.1 percent of GDP. The higher investments (relative to the 2nd review) are financed through a combination of higher grants, concession fees, tax revenue and a slight increase in the primary deficit. The additional income allows higher investment over 2024 and 2025 before capital spending returns to the baseline path in 2026, which implies more adjustment in that year than under the 2nd review. SOE reforms are expected to reduce capitalization and on-lending starting in 2025, helping improve the fiscal position.

12. We are taking practical and institutional measures to boost domestic revenue mobilization. With support from IMF TA we plan to develop and publish an action plan to reduce tax expenditures, including published estimates of annual tax expenditures in the budget, and undertake phased implementation of the ECOWAS tariff, to increase revenue by 1 percent of GDP (**SB end-September 2024**). Furthermore, revenue administration improvements are expected to yield additional revenues, mainly through collection of tax arrears and heightened supervision. 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.

13. Over the medium-term, we will rationalize current expenditure and improve the delivery of investment spending with clear priorities. In the near-term, wages are projected to grow slightly above inflation to partially recover the purchasing power lost during in the last couple of years. Spending on social programs and subsidies to shield the vulnerable from the impact of higher cost of basic food items will increase. 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. Capital expenditure will be strictly prioritized. We will also review social welfare programs to ensure adequate coverage particularly in the context of rising prices and climate risks which disproportionately affect the most vulnerable. We recognize that to achieve our medium-term fiscal objectives additional policy measures will be required. Therefore, 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.

14. 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 (C-PIMA), we will improve projects in the near- to medium-term. 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.

15. 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.

16. Broader fiscal coverage will allow for the preparation of accounts at the level of the general government, as well as its transparency. This includes the publication of annual budget execution reports for the general government (**SB end-September 2023**). In addition, we plan to broaden the coverage of the fiscal risk analysis and reporting to include PPPs (**proposed new SB end-September 2024**).

17. We will continue other efforts to ease Cabo Verde's public debt burden. We have already reached an agreement with Portugal in principle to explore debt for climate swap initiatives. The debt legislation was updated in line with the 2018 review. It is intended to implement the debt management strategy for carrying out internal debt sustainability analysis (DSA). For this purpose, it is necessary to receive training from FAD experts, addressed to Ministry of Finance officials, during the first half of 2024, which will be important as a basis for preparing the 2025 budget guidelines. Furthermore, the Government undertook 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.

B. Reduce Fiscal Risks from SOEs and Improve Their Financial Management

18. Reforms to reduce SOE related fiscal risks will continue. In this regard, special focus was placed on 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 tools and quarterly monitoring report of SOEs' budget execution are being prepared since 2022. In October 2023 we launched the SOE Manager platform where the financial data of the majority of SOEs are available in real time. Ongoing reforms will 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 has been improved to include comparison of execution relative to the initial budget projection, evaluation of performance against medium-term plans, and data on government relations **(SB end-July 2023)**. Going forward, we will publish in the annual report on public companies the forward looking targets agreed between the Ministry of Finance and Business Development and the six largest SOEs, on improving financial performance and reducing the need for central government support (**SB end-June 2024**). We are analyzing the non-performing loans shown by the recent BCV study on the loan losses and provisions at the end of the credit moratorium, and the implications for government guarantees and other related fiscal risks.

19. Cabo Verde Airlines (TACV) is a key priority, and the Government intends to complete the reorganization of TACV and resume its privatization efforts. The Government is in the process of reorganizing the airline and is in negotiations with potential partners. Under the new plan, which was delayed, TACV started operations with one aircraft in 2022 with flights to Lisbon. A second aircraft started operating in August of 2023 and TACV is working on an interim and medium-term plan to increase the number of aircrafts and the number of flights to Europe, USA, Brazil and Africa to achieve breakeven. The Government is providing financing during the reorganization process to cover the projected gap in the amount of €30 million (about 1.6 percent of GDP) over a period of three years. We will seek the best restructuring options based on a design of an appropriate business plan covering at least five years.

C. Modernize the Monetary Policy Framework and Improve Resilience of the Financial System

20. The conventional fixed peg exchange regime continues to provide a stable anchor for monetary policy. Monetary policy continues to focus on safeguarding the peg and strengthening the monetary policy transmission mechanism. Despite the uncertain external environment, international reserves are projected to increase by 100 million euros in 2023 reaching a level equivalent to 6.1 months of imports of goods and services. Key drivers include the growth in tourism and the impact of grants, ECF disbursements, and remittances. In October 2023 we tightened rates to narrow the differential with the ECB and we will closely monitor economic developments in the euro area and stand ready to take further action if pressures on reserves become apparent. The economy continues to recover and shows excess liquidity in the banking system. However, the geopolitical shock warrants a cautious monetary policy stance approach. Over the medium-term, to support the peg, we will continue to target international reserves in the range of 5½–6 months of prospective imports.

21. Further strengthening the monetary policy transmission and our analytical capacity to track developments in the economy remains a priority. We have taken 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). At the same time, we continue to analyze the impact of managing liquidity and the cost of monetary policy. Policy analysis was reinforced, through the introduction of composite indicators of economic activity and strengthening near-term forecasting **(SB end-June 2023)**, although we will have to update the index again following the publication of the rebased GDP series. We will also develop a framework to guide the provision of emergency liquidity assistance, and currently working on the remaining legal framework. 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.

22. The BCV will closely monitor emerging risks to the banking sector. Available indicators show that the banking sector is well placed to withstand the end of the credit moratorium. We concluded a study of loan losses and provisions at the expiration of the credit moratorium covering the majority of the banking sector and have expanded that further this year. We are also monitoring risks from the SOE sector. We continue to encourage and facilitate prudent restructuring of loans, provide guidance on the prudential treatment of moratoria and NPLs management strategies and develop a common framework for bank resolution. In addition, we 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, we have done and internal analysis of a common framework for the resolution of crisis related NPLs, and in conjunction with other structural measures reflected in the FSAP done by the World Bank, we will elaborate more on this subject for a more comprehensive framework.

23. We plan to further improve AML/CFT effectiveness and technical compliance, in line with the recommendations found in the 2019 GIABA mutual evaluation report. Recent improvements in the AML/CFT framework include the establishment of a national AML/CFT committee and Cabo Verde's exit from the EU Grey List of non-cooperative jurisdictions for tax purposes in 2020 which have helped preserve correspondent banking relationships. Further improvements included the approval in 2023 of the National Strategy for 2023-2027 with seven major priority objectives, including the legal framework and proposals for changes, statistics and strengthening of the institutions geared towards a more comprehensive approach. In addition, BCV has embarked on a continuous process (human resources and institutional capacity) on effective risk-based supervision for financial institutions. Regarding the subject and the responsibility of the BCV AML/CFT framework to include virtual assets, and in line with the recommendations of the FATF, in particular Recommendation 15, a bill was approved by parliament in June of this year. This law regulates the provision of services with virtual assets and gives BCV the responsibility for regulation and supervision in matters of preventing money laundering and combating the financing of terrorism to entities that carry out activities with virtual assets. Furthermore, the law stipulates that the creation of digital banks depends on the authorization of BCV and that they are subject to compliance with the same duties applicable to conventional banks. As for the DNFBP's, the change regarding this matter is still ongoing with a process of developing capacities.

24. 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 (**SB end-December 2023**). In addition, the stress testing methodology will be revamped to include detailed banking data and cyber security risk assessment. We will submit to Parliament the legislation amending the BCV Organic Law to, inter alia, strengthen the BCV's decision-making structure, autonomy, accountability and transparency of the central bank in line with the IMF safeguards assessment, and supported by technical assistance from the IMF (**Proposed new SB end-July 2024**).

25. We will accelerate work towards the adoption of Basel II Pillar 1. During the last part of 2023, an evaluation will be undertaken on the implementation of the Basel principles through the BCP Self-Assessment.

26. We continue to improve 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.

D. Broad Structural Reforms: Supporting Private Sector-Led Growth and Resilience to Shocks

27. Structural reforms and policies should help build resilience to different protracted shocks, including climate change. Key priority areas in the new five-year development strategy include: (i) completing SOE reforms; (ii) facilitating access to finance; and (iii) improving the business environment. We are advancing a set of reforms to improve the business environment, mainly directed to the SMEs. Reforms are focused on plans to promote private sector-led economic diversification with the aim of supporting quality investments, employment and enhanced productivity. Efforts to reduce the high costs of finance, electricity, water and transport which are major impediments to private sector growth, will continue.

28. Diversification of activity continues to be critical for 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.

29. 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, we will digitalize the relevant information to facilitate ease of access to all parties, which will contribute to more timely settlement of disputes.

30. Providing financial support to vulnerable households remains a key priority. Social spending will be aided by funding from the social protection fund financed by the tourism tax and customs revenue for small parcels. Although Cabo Verde performs very well on social indicators, poverty and unemployment remain a challenge particularly in the rural areas. Social safety nets will be strengthened through improved targeting of social spending. In partnership with our external partners (World Bank and African Development Bank), 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. We aim to reform the national social security system to ensure that it evolves in alignment with best practices and the changing needs of the country.

31. 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 ECF-supported program as support for the most vulnerable and helping lift households out of poverty are key objectives of our strategy. 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.

E. Policies and Measures to Address Climate Change Challenges

32. **Sustainable socioeconomic development will depend on our ability to address the implications from climate change, which are amplifying our development challenges**. Scarcity of natural resources, namely water and arable land make our country susceptible to climate change implications. A heavy reliance on imported carbon-based energy is holding back economic development and poses an impediment to our plans for reducing GHG emissions and for addressing water scarcity through desalination. The interlinkages between climate change, energy, and water provide the context for our reform. In cooperation with our development partners, we are working towards energy transition, while improving service quality and access, as well as achieving the sustainability for the energy and water sectors. While our contributions to global emissions are minimal in absolute terms, under our NDC we commit to reduce GHG emissions by 2030 by 18 percent (24 percent conditional) compared to BAU and we aim to achieve net zero by 2050. At the same time, we work to enable the efficient and climate aware management of our public resources while supporting climate resilient private sector led development, including through climate aware investment in key sectors like tourism and renewable energies.

33. **The RSF will support our effort to implement macro-critical climate reforms and catalyze private finance for climate adaptation, and transition with a view to achieve the objectives we laid out in the PEDS II and NDC**. Recognizing the magnitude of the development challenge and its exacerbation coming from climate change, we will use the RSF to support us in accelerating the climate transition, by focusing on: (i) strengthening climate change policy governance; (ii) improving physical and fiscal resilience; (iii) strengthening mitigation and resilience through energy efficiency and transition; (iv) promoting adaptation by ensuring ecological and economic sustainability of water resources and planning for long-run climate impacts; and (v) financial sector resilience to climate change (Table 3). The RSF supports our PEDS II and NDC, and reflects the recommendations from the C-PIMA, the Climate Policy Diagnostics, and have been informed by the WB's Country Economic Memorandum and forthcoming DPF. Each reform area has reform measures (RMs, specified below) to be achieved by specified target dates under this facility. Additionally, RSF financing will provide budget support and replace more expensive financing. These savings will help us create policy space to support critical climate-related investments.

Reform Area 1. Strengthen Governance of Climate Change Policy

34. **We will improve the coordination of both, climate change related policies and disaster risk management**. The Climate Policy Diagnostic (CPD) noted that these functions require strong leadership and cross-government coordination, which we will provide through a coordination mechanism at the level of the Heads of Government (**RM1, by end-April 2024**). This will allow us to promote awareness of the implications of climate change, to ensure cross sectoral consistency of climate change related policies, and to provide strategic leadership for the coordination of disaster risk management (DRM), all with a view to build resilience and to manage climate change related

challenges effectively. We have taken important steps towards sectoral planning and to build technical capacity for managing climate change and natural disasters, including within the Ministry of Agriculture and Environment and through the National Civil Protection and Fire Service. However, we feel that more needs to be done to incentivize consistent participation from all parts of our public sector in coordinated planning and execution of climate change related policy measures, and in the effective mitigation of, and recovery from, climate-related hazards.

Reform Area 2. Improve Fiscal and Physical Resilience to Climate Change

35. To proactively assess the macro-fiscal implications of our climate change strategy, we are integrating climate risks into our budget planning. With the Luxembourg support, we are developing a methodology for tagging climate-related expenditure in budget and financial reporting. In 2022, we created a high-level fiscal risk coordination committee, explicitly tasked with managing fiscal risks associated with climate and disaster risk and we plan to revise its composition and permanently integrate critical national counterparts —such as, the Ministry of Agriculture and Environment, the National Institute of Meteorology and Geophysics and the National Civic Protection Service— to better assess, analyze, and quantify climate related risks. As a result, the 2023 Fiscal Risks Statement (RSF) identifies the main risks, namely, macroeconomic risk, risk associated with the state's business sector and risk associated with public debt. To further strengthen the management of fiscal risks arising from disasters and climate-related shocks and ensure that these actions efficiently inform fiscal policymaking, with the support of the WB, we will conduct and publish in the RSF the quantitative analysis of the fiscal risks generated by climate change **(RM2, by end-September 2024, and submitted with the budget proposal on October 1, 2024).** We are also committed to incorporate these risks into medium-term fiscal policy documents such as the medium-term fiscal frameworks (MTFFs), medium-term debt strategy (MTDS), and Debt Sustainability Analysis (DSA).

36. To build economic resilience to climate change we are promoting climate-proofing infrastructure and public investment management. We already made progress on a comprehensive climate change policy framework, spatial planning, coordination with municipalities and in planning for disaster risk financing. The PEDS II and some sectoral strategies are well aligned with the objectives and priorities of the 2021 NDC. The land management and territorial planning policy and regulations introduce resilience and climate change as one of the guiding principles for land use planning and urbanization. The 2012 Building Code has been revised to address concerns related to energy mitigation through improving energy efficiency in public buildings. We have also provided guidelines to municipalities to prepare strategic plans including investments aligned with PEDS and coordinated green and resilient climate investments at local level through the Environment Fund. In this context, we are committed to strengthening our institutional capacity to plan and manage efficiently green and resilient investment projects, building on the recommendations of the C-PIMA. To this end, and as part of our planned engagement with the WB under the new DPF, we will issue a PIM legal framework incorporating green and resilient considerations at the different stages of the capital project cycle (planning, appraisal, selection etc.). With AFRITAC West 2 support, we have developed an appraisal screening methodology. As the next step in project appraisal and as part of the new WB DPF, we will update the screening methodology to handle exposure and resilience of public works to natural disasters. Given the increased use of PPPs, we are resolved to amend the existing PPP legal framework to ensure climate requirements are reflected in PPP agreements and to develop a manual integrating these requirements throughout the PPP capital project lifecycle, from project identification to contract management stages **(RM3, by the end-April 2024)**. Building on the initiates undertaken by the Cabo Verde Infrastructure (*Instrastructuras the Cabo Verde (ICV))* we plan to georeference public assets and have a more efficient and proactive approach to capital maintenance.

37. We seek to improve green and resilient public investment in a constrained fiscal environment and are exploring opportunities for green finance from official and private sources. We have put in place a climate financing framework to provide liquidity during natural disasters and to support our climate adaptation and mitigation efforts. A combination of budget instruments, funds and contingent lines of credit from International Financial Institutions (IFIs) provides resources to respond to climate change challenges: (i) the annual budget has a provisional allocation for "unforeseen and unavoidable" expenditures (*dotação provisional*), set at a maximum of 2 percent of ordinary fiscal revenues; (ii) the Sovereign Emergency Fund (*Fundo Soberano de Emergência (FSE)*) to finance —among others— post-disaster rehabilitation and reconstruction of public infrastructure; (iii) the National Emergency Fund (*Fundo Nacional de Emergência (FNE)*) to cover recurrent emergency and recovery expenditures.; (iv) the Environment Fund and; (v) blue bonds recently launched in January 2023. Through the 2019 World Bank (WB) Disaster Risk Management Development Policy Financing, we also accessed the Catastrophic Deferred Drawdown Option (Cat-DDO). With WB support we are designing a Climate and Nature Fund. However, considering the climate financing gap remains large and, in an effort to rationalize the financing instruments based on a more robust assessment of explicit and implicit contingent liabilities, with the Luxembourg support, we are committed to adopt a national climate finance mobilization strategy that comprehensively identify the financing instruments to unlock climate finance sources. Once the strategy is adopted, we will proceed by reviewing or validating the existing instruments and adopting the newly identified ones. We will also develop and publish, a pipeline of appraised public capital projects, including climate-related projects, as part of the budget process **(RM4, by end-April 2025)**.

Reform Area 3. Strengthen Mitigation and Resilience Through Energy Efficiency and Transition

38. Energy efficiency and transition will support our mitigation goals, resilience and, through the link to water, adaptation. More than 80 percent of our electricity generation relies on imported fossil fuels products, and the majority of the GHG emissions come from the energy sector. This has fiscal implications as we shield households from the effect of pass-through costs. However, Cabo Verde has vast potential from renewable energy sources (RES). The energy transition will (i) contribute to emission reduction and the attainment our NDC objectives; (ii) allow for a cost-efficient response to growing energy demand including from the desalination reliant water sector; and (iii) yield favorable long-term impacts on our balance of payments as fossil fuel imports decline. Energy transition will require (i) substantial public investment in electricity grid infrastructure to build the capacity for higher RES in the electricity mix, and (ii) market conditions that encourage private investment in energy production. Our RSF (i) by ensuring that the tariff reflects the full cost of service provision will support energy efficiency, (ii) by ensuring the availability of financial resources will facilitate the upgrading of network infrastructure, and (iii) by promoting the technical stability of the system and the financial sustainability of the offtake promote the development of appropriate market conditions **(RM5, by end-April 2025)**. With support from the WB, we are taking important steps to unbundle the energy sector. We request FAD CD support on the designing tariff reforms including distributional impact assessment of policy measures in this field.

Reform Area 4. Promoting Adaptation by Ensuring Ecological and Economic Sustainability of Water Resources and Planning for Long-run Climate Impacts

39. Cabo Verde faces water shortages and climate related threats amplify water scarcity and pose a challenge for, and risk to, water availability and quality. Our RSF will support our efforts to improve the efficiency of water use and provision, and to expand water sourcing. We have a long history of using desalination for freshwater production and we are using this technology to address the increasing demand for water in light of declining freshwater resources. We need investment to tackle technical and commercial losses, which amount on average to about 50 percent of the total fresh water entering the system. Several of our publicly owned water operators are running operational losses and/or have negative equity. The RSF supports our plans to promote efficient use of water resources by introducing efficient price signals and to strengthen climate change resilience, by creating the preconditions for funding critical investment needed to enhance the long-term operational and financial sustainability of a sector critical to climate change adaptation **(RM6, by end-April 2025)**. Our RSF will also strengthen the social safety net (SSN) to allow the efficient provision of support in the context of climate related shocks and in case of adverse implications, for example, from the energy transition on the poor and vulnerable **(RM7, by end-November 2024)**. The WB is assisting us with strengthening the SSN and we request FAD CD support on the designing the tariff reforms including distributional impact analysis assessment of policy measures in this field.[1]

40. Effective preparation for climate change implications also requires generating information regarding what to expect. Our RSF will enable investment decisions based on reliable information on climate change related risks, such as sea level rise. To this end, we will

[1]The tariff reforms can be equity-enhancing by themselves, and a distributional impact assessment will be done using current household budget survey (not available for the CPAT assessment).

develop and share climate scenarios relevant to Cabo Verde and hazard vulnerability maps that include potential climate related hazards consistent with the climate scenarios **(RM8, by end-November 2024)**.[2] Understanding climate related risks will reduce information uncertainty, potentially lowering the risk premium required by investors and helping to avoid underinvestment in sectors such as tourism. Incorporating information on climate hazards in our land use and construction planning will help us to mitigate the implications of disaster risks, reducing private and public costs of climate related disasters. At the same time we are implementing an early warning systems that will allow us to identify risks early and inform our population to protect lives and livelihoods in case of a natural disaster.

Reform Area 5. Financial Sector Resilience to Climate Change

41. The RSF aims to support steering private finance towards a low-carbon climate-resilient economy, while strengthening financial sector resilience to climate-related risks. Given the strong role of the banking sector in Cabo Verde, this will include the adoption by the BCV of guidelines to monitor banks and disclosure of climate-related risks and opportunities **(RM9, by end-November 2024)**. Enhancing the financial sector's capacity to manage climate change risks is crucial for Cabo Verde, given that it is a tourism-dependent small island state where climate events could easily escalate. Proposed reforms include the design of a climate information architecture for banks (taxonomy and climate disclosures) and promote climate resilience among financial institutions. These could be the foundation to unlock private sector climate financing.

F. Financing and Program Monitoring

42. The program will be closely monitored through the proposed quantitative performance criteria, indicative targets, and structural benchmarks (Table 1 and 2). The Technical Memorandum of Understanding describes the definitions as well as data provision requirements. The fourth, fifth and sixth program reviews are scheduled to be completed by March 2024, October 2024, and March 2025 (based on end-December 2023, end June 2024, and end-December 2024 test dates, respectively). We requested a clarification of the definition of deposits under *other net liabilities* in the TMU (from a stock to a flow), and a modification of the PC on *other net liabilities* in December 2023 and June 2024 to reflect the delay in 2023 privatization receipts. The program will continue with monitoring on a semi-annual basis by the IMF Executive Board. Under the RSF, monitoring will be done by means of the reform measures. These are detailed in Table 3 of the MEFP.

[2] The work on climate scenarios and maps is ongoing and once the council is in place, it will officially cover the matter.

Table 1. Cabo Verde: Quantitative Performance Criteria Under the ECF, March 2023-June 2024[1]

(Millions of Escudos, unless otherwise indicated)

	2023									2024					
	end-March			end-June			end-September	end-December		end-March		end-June		end-September	end-December
	Indicative Targets (IT)	Actual	Status	Performance Criteria (PC)	Actual	Status	Indicative Targets (IT)	Performance Criteria (PC)	Revised Performance Criteria (PC)	Indicative Targets (IT)	Revised Indicative Target	Performance Criteria (PC)	Revised Performance Criteria (PC)	Indicative Targets (IT)	Performance Criteria (PC)
								Cumulative from the beginning of the calendar year							
Quantitative performance criteria															
Primary balance, floor [2]	-2,612.0	608.1	met	-4,141.0	2,759.2	met	-5,564.2	-6,298.0		-1,849		-2417		-2740.6	-3,063.9
Tax revenue, floor	9,550.1	13,228.8	met	19,095.0	24,669.9	met	31,483.0	45,849.0		8,088		21029		37501.4	53,973.7
Net other liabilities, floor [3]	-501.5	2,327.7	met	-625.3	593.2	met	-1,150.2	1,940.3	-1,368.2	-1,099	-418	-1259	-446.3	-502.12	-557.9
Net domestic financing, ceiling	5,651	820	met	5,886	1,728	met	4,920.5	4,179		3,093		4021		2241.25	462
Nonaccumulation of domestic arrears [4]	0	0	met	0	0	met	0	0		0		0		0	0
Non-accumulation of external payment arrears [4]	0	0	met	0	0	met	0	0		0		0		0	0
PV of new external debt, ceiling (in millions of US Dollars)	46	11.93	met	60	24	met	75	98.7	108.8	24		37		95.4	125.5
Nominal level of new nonconcessional external debt of central government, ceiling	0	0	met	0	0	met	0	0		0		0		0	0
Gross international reserves (in millions of euros), floor [2]	554	653.9	met	572	626.0	met	592	622		671		693		743.58	794
Indicative Targets															
Social spending, floor	2,923	3,135	met	6,180	6,982	met	10,009.0	17,304.0		3,690		7379		12934.5	18,490.1
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	413.3	15.6		827	47		1,286	1,653		116.6		136		165.209	194
Capitalization	300.0	1,955.1		765.3	1,366.4		880.1	2,200.4		1,100		1600		2100.2	2,600
Program assumptions															
Project and budget support grants	522.5	479.0		623.3	1,206.1		2,090.0	5,225.0		526		1121		3765.34	6,409.3
External debt service	3,664.8	2,557.5		6,445.4	3,420.2		10,664.6	12,921.0		2,409		4818		8424.69	12,031.9
Sales of assets	142.2	12.2		516.6	97.0		612.0	747.0		106		226		465.3	705.0
Project and budget support loans	913.9	2,758.1		5,887.7	5,590.6		13,523.5	16,663.0		1,816		4238		11995.3	19,752.2

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

[1] 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 2. Cabo Verde: Structural Benchmarks for 2022-24 Under the ECF

Actions	Target date	Objective	Status
Fiscal reforms			
1) Invoice electronically at least 50 percent of tax payers for VAT	End-December 2022	Improve revenue collection	Met
2) Submit to parliament the budget for 2023 that is in line with commitments under the program.	End December 2022	Support fiscal and debt sustainability	Met
3) Compile and publish historical series of government financial statistics for general government.	End-March 2023	Improve fiscal transparency	Met
4) Publish annual budget execution reports for the general government.	End-September 2023	Improve fiscal transparency	Met
5) Construct a Compliance Risk Management system to allow for the optimization of tax revenue collection by end-December 2023.	End-December 2023	Support fiscal and debt sustainability	
6) Submit to parliament the budget for 2024 that is in line with the primary balance commitment under the program.	End-December 2023	Support fiscal and debt sustainability	
7) Develop and publish an action plan to reduce tax expenditures by 1 percent of GDP and include published estimates of annual tax expenditures in the budget to improve transparency	End-September 2024	Support fiscal and debt sustainability	
8) Implement the action plan to reduce expenditures during in the 2025 budget	End-December 2024	Support fiscal and debt sustainability	
9) Broadening the coverage of fiscal risk analysis and reporting to include PPPs **(Proposed new SB)**	End-September 2024	Improve fiscal transparency and risk analysis	
SOEs reforms			
10) Conduct quarterly analysis of fiscal risk assessment using the IMF SOEs health check tool.	End-September 2022	Improve fiscal reporting and reduce fiscal risks	Met
11) Introduce a quarterly monitoring report on SOEs budget execution.	End-September 2022	Improve fiscal reporting and reduce fiscal risks	Met
12) 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 reduce fiscal risks	Met
13) Based on the July 2023 structural benchmark, publish in the annual report on public companies the targets agreed between the Ministry of Finance and Business Development and the six largest public companies , on improving financial performance and reducing the need for central government support.	End-June 2024	Improve fiscal reporting and reduce fiscal risks	
Monetary policy reforms			
14) Preannounce a schedule for TIM and TRM auctions.	End-June 2022	Support the development of the money market	Met
15) Introduce composite indicators of economic activity.	End-June 2023	Support monetary policy analysis	Met
Financial sector reforms			
16) 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	Met
17) Carry out a comprenhensive study of loan losses and provisions at the expiration of the credit moratorium.	End-December 2022	Strengthen financial stability	Met
18) Develop a common framework for the resolution of crisis related NPLs.	End-December 2022	Strengthen financial stability	Met
19) Increase the frequency of stress testing to twice per year (June 2023 and December 2023) to ensure the effectiveness of the supervisory process and revamp the stress testing methodology to include detailed banking data and cyber security risk assessment.	End-December 2023	Strengthen financial stability	
20) Submit the draft amendments to the BCV Law, in line with IMF recommendations, to parliament with a view to (i) establish an independent oversight process that is separate from executive management, (ii) strengthen the BCV's personal and financial autonomy, and (iii) enhance transparency and accountability mechanisms **(Proposed new SB)**	End-July 2024	Strengthen BCV institutional framework	

Table 3. Cabo Verde: RSF Reform Measures Matrix

KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TIMING
National coordination and management of climate change is under the MAE that is not able to ensure cross sector coordination	**RM1.** Government will establish a council/body for coordinating climate change policy planning and strategy, and DRM under the Heads of Government, with a clear tasks, responsibilities and procedures, including mechanisms for (i) holding entities accountable for consistency across sectoral plans in line with the national development strategy (PEDS II) and international commitments (NDC), and (ii) providing strategic oversight of DRM defined in the TORs, with implementation reflected in the protocols of regular meetings. The MAE serves as secretariate.	Climate Policy Diagnostic (CPD)		Integrated and effective coordination of climate change activities in the public administration, ensuring cross sectoral consistency of key reform plans, including for electricity and water (for human consumption and for irrigation), and in DRM	LuxDev is providing support to MAE for the climate management function	End-April 2024; 4th ECF Review
Natural disaster and climate related risk not adequately featured in fiscal planning	**RM2**. To improve fiscal risk management, the Ministry of Finance will conduct and publish in the annual Fiscal Risk Statement quantitative analysis of the fiscal risks generated by climate change.	C-PIMA; CPD	Follow up support from FADM2 on fiscal risk reporting	Improve awareness of climate -related matters in fiscal planning and budgeting	World Bank has prior actions and triggers in the latest DPF supporting a stronger PIM framework and aligned with the C-PIMA recommendations	End-September 2024; 5th ECF Review
Investments do not reflect needed physical resilience to Climate Change	**RM3**. The Ministry of Finance will enact amendments to the PPP legal framework to ensure climate requirements are reflected in PPP agreements and the Ministry of Finance will publish a manual integrating these requirements throughout the PPP capital project lifecycle, from project identification to contract management stages.	C-PIMA	FAD Support	Stronger PPP framework; reduced fiscal risks from PPPs; enhanced climate sensitive public investment planning and budgeting		End-April. 2024; 4th ECF Review

Table 3. Cabo Verde: RSF Reform Measures Matrix (continued)						
KEY CHALLENGE	**REFORM MEASURE**	**DIAGNOSTIC REFERENCE**	**IMF CD INPUT**	**RM EXPECTED OUTCOME**	**DEVELOPMENT PARTNER ROLE**	**TENTATIVE DATE**
	RM4. To scale up and systematize climate finance the Ministry of Finance will (i) adopt a national climate finance mobilization strategy that comprehensively identifies the financing instruments to unlock climate finance sources; and (ii) develop and publish, a pipeline of appraised public capital projects, including climate-related projects, as part of the budget process.	C-PIMA	Luxembourg and follow up support from FADM2	Generate a robust pipeline of projects and scale up climate investments		End-April 2025; 6th ECF Review
Mitigation, adaptation and resilience in the energy sector are held up by energy inefficiency and obstacles to transition	**RM5**. To support energy transition plans, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of electricity (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting electricity tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments. (Ministry of Industry, Trade and Energy and MoF)	CPD	FADEP support on the analytical study and distributional impact – TBC	Energy efficiency and facilitation of more renewable energy through development of appropriate market conditions and by ensuring funding for necessary infrastructure investment. Ensuring the financial soundness of electricity sector operator to create an environment conducive to private sector investment in RES production	WB energy projects are providing support on unbundling the energy SOE	End-April 2025; 6th ECF Review

Table 3. Cabo Verde: RSF Reform Measures Matrix (continued)

KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TENTATIVE DATE
Access to water resources and fiscal sustainability are vulnerable to long-run climate impacts due to lack of investment and non-ecological use	**RM6** To support reform initiatives, which will require substantial infrastructure investment the government will, (i) determine the cost-recovery rate for the provision of water (fully reflecting operational and capital cost), (ii) identify any discrepancy between the existing tariff and so defined cost recovery, (iii) undertake a distributional impact assessment, and (iv) publish and adopt regulations establishing a methodology for adjusting water tariffs to the identified cost-recovery rate, to be applied by the regulator (thereby achieving full cost recovery) by the test date, with transparent periodic adjustments, and/or by financing infrastructure investment transparently from the budget, with a view to ensure sustainability of the water sector. (National Water and sanitation Agency (ANAS) and MoF	CPD	FAD support for tariff review and the distributional impact – TBC	Sustainable use of water resources to improve adaptation to climate change effects, clarifying the source of funding for necessary infrastructure investment, ensuring the financial soundness of water sector operators to create an environment conducive to private sector investment in water and sanitation service provision	LuxDev is providing support in the water sector. TBC.	End-April 2025; 6th ECF Review
	RM7. The Unique Social Registry (USR) will be expanded to provide the basis for a social support system that can efficiently mitigate the implications of climate transition and climate hazard events. To this end, the Ministry of Family and Social Inclusion and the MoF will expand coverage of the USR to 100 percent of poor and vulnerable households (including from rural areas) as identified based on the latest household budget survey, and offer inclusion in the USR to 100 percent of the households in climate vulnerable areas.	CPD		Strengthen the social safety net to prepare for efficiently supporting the vulnerable and poor as needed (i) in case of adverse climate change related events, and (ii) through the climate transition.	WB	End-Nov. 2024; 5h ECF Review

Table 3. Cabo Verde: RSF Reform Measures Matrix (concluded)						
KEY CHALLENGE	REFORM MEASURE	DIAGNOSTIC REFERENCE	IMF CD INPUT	RM EXPECTED OUTCOME	DEVELOPMENT PARTNER ROLE	TENTATIVE DATE
	RM8 INGT or new unit/council for CC management and DRM will develop and disseminate natural disaster risk and vulnerability maps, including information on how and where climate hazards might affect the areas and regions, to assess risks and vulnerabilities of the population, infrastructure assets, sectors, and the economy/businesses. The land use planning regulation and construction code requirements will be amended to consider disaster risks and vulnerabilities for urban and rural development planning and for designing and constructing infrastructure and buildings.			Investment decisions that are resilient to climate change impacts such as sea level rise, flooding, and landslides.		End-Nov. 2024; 5th ECF Review
Green financing/Climate Finance	**RM9**. The BCV will develop a climate information architecture for banks, consisting of 1) the adoption of a climate change adaptation and mitigation taxonomy, and 2) the publication of climate risk and opportunities and disclosure guidelines, so that banks are expected to submit their internal roadmaps within six months from the effective date of application of the guideline, followed by progress reports every six months.		MCM CD (TBC)	Transparency on impact of climate change and disaster risks in the financial sector	[TBC]	End-Nov. 2024; 5th ECF Review

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 and extrabudgetary entities**. It does not include local government (municipalities), 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 the grants 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-23	623
31-Dec-23	5,225
30-Jun-24	1,121
31-Dec-24	6,409

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. Floor 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, other assets, and privatization proceeds. The floor of central government net other liabilities will be measured as cumulative over the calendar year. Deposits capture the changes in 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. Privatization proceeds refers to the income from the sale of central government assets to the private sector.

9. The floor of net other liabilities will be adjusted downward (upward) by the shortfall (surplus) in privatization proceeds relative to program projections.

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

Table 3. Cabo Verde: Privatization Income Projected Under the Program

Date	Privatization income projected under the program, cumulative from the beginning of the year
31-Dec-23	0
30-Jun-24	1,156
31-Dec-24	2,312

Sources: Cabo Verdean authorities and IMF staff estimates.

D. Ceiling on Net Domestic Financing of the Central Government

11. Net domestic financing (NDF) of the central government is defined as the sum of (i) the net position (difference between the government's claims and debt) vis-à-vis the central bank and commercial banks and (ii) financing of the government through the issuance (net of redemptions) of securities to individuals or legal entities outside the banking system. NDF at end-December 2023, end-June 2024, and end-December 2024 (PCs) must be equal to or less than the amounts indicated in Table 1 (of QPCs) attached to the MEFP.

12. External budgetary assistance is defined as budget loans, grants and non-earmarked debt relief operations (excluding project-related loans and debt relief under the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief (MDRI) Initiatives). It would include budget support loans from the IMF, World Bank, AfDB, European Union and others.

13. The NDF ceiling of the government will be adjusted downward (upward) if net external budgetary assistance exceeds (or falls short) of the program projections in Table 4 of external budget assistance:

Table 4. Cabo Verde: Budget Support Loans and Grants
(Million CV Escudos)

Date	Budget support loans and Grants (in million CV Escudos)
30-Jun-23	3,575
31-Dec-23	12,351
30-Jun-24	3,613
31-Dec-24	11,468

Source: Cabo Verdean Authorities: IMF Staff estimates

- If, at the end of a quarter, external budgetary assistance exceeds the program projections (cumulative since January 1 of the same year), the ceiling of NDF will be adjusted downward.
- If at the end of a quarter, external budgetary assistance falls short of the projected amounts (cumulative since January 1 of the same year), the NDF ceiling will be upward while respecting the limits established by the Budget law (including any waivers).

14. Reporting requirements. For program monitoring, data will be provided to the Fund by the DNP of the Ministry of Finance and BCV (for the net position of the government to the banking system) monthly with a lag of no more than six weeks from the end of-period.

E. Non-accumulation of Domestic Payments Arrears

15. 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.

16. 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.

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

17. 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.

18. 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.

19. 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. 16919-(20/103), adopted October 28, 2020.

(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.

20. 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.

21. 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.

[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.

22. 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.

G. Non-concessional External Debt Contracted or Guaranteed by the Central Government

23. 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.

24. 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.

H. Gross International Reserves of the Central Bank

25. 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.

26. 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 5. 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-23	6,445
31-Dec-23	12,921
30-Jun-24	4,818
31-Dec-24	11,195

Source: Cabo Verdean Authorities: IMF Staff estimates

Table 6. 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-23	6,511
31-Dec-23	21,888
30-Jun-24	5,360
31-Dec-24	26,162

Source: Cabo Verdean Authorities: IMF Staff estimates

I. Non-accumulation of External Payments Arrears

27. 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.

28. **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.

29. **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.

J. Memorandum Item: Floor on Central Government Social Spending

30. **The indicative floor on social spending of the central government 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.

31. **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.

K. RSF Reform Measures

32. **Cost recovery tariff under RM 5 and 6 should reflect the capital cost of infrastructure and the operational cost**. Infrastructure cost will cover the investment as needed during the transition, as well as the maintenance and replacement based on the useful life of such infrastructure. The operational cost will reflect the current and target energy mix.

33. **Climate vulnerability information under RM8 will cover**: (i) maps on vulnerability to sea-level rise projection based on identified climate scenarios with full coverage of territory; (ii) climate vulnerability maps for the seven (seven out of 22) most populated and/or most climate vulnerable municipalities; and (iii) maps including information on the occurrence of past climate hazards with additional information on the expected implications of climate change as implied by the identified climate scenarios. These maps will be made available online. The requirements for using information from vulnerability maps in land use and construction planning should be reflected in the National Regulations for Territory Management and Urban Planning (Decree-Law 61/2018) or the related regulations, and the Technical Building Code (Order 4/2012).

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

34. **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.

35. **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).

36. **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).

37. **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.

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

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

40. **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.

41. **Construct a Compliance Risk Management (CRM) system to allow for the optimization of tax revenue collection**. This reform target will be assessed as achieved when the MOF provides staff with a copy of methodology.

42. **Increase the frequency of stress testing to twice per year**: This reform target will be assessed as achieved when the central bank provides the findings of the second annual stress test.

43. **Develop and publish an action plan to reduce tax expenditures**. This reform target will be assessed as achieved when the MOF provides staff a copy of the approved action plan.

44. **Implement the action plan on tax expenditures in the 2025 budget**. This reform target will be assessed as achieved when the MOF provides staff a copy of the approved 2025 budget with the specification of the actions and impacts.

45. **Publish in the SOE report measurable metrics between the MOF and the 6 largest SOEs on financial performance**. This reform target will be assessed as achieved when the report is published in the MOF webpage.

INTERNATIONAL MONETARY FUND

CABO VERDE

November 22, 2023

THIRD REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA, AND REQUEST FOR AN ARRANGMENT UNDER THE RESILIENCE AND SUSTAINABILITY FACILITY—DEBT SUSTAINABILITY ANALYSIS

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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	Limited space to absorb shocks
Application of judgement	No

Cabo Verde's overall risk of debt distress remains high, consistent with the last joint WB/IMF Debt Sustainability Analysis (DSA) of June 2023,[1] *and the external debt risk continues to be moderate. The detailed risk rating for external debt distress shows that it has little room to accommodate shocks. The present value (PV) of public and publicly guaranteed (PPG) external debt-to-GDP ratio is below the threshold over the forecast horizon and breaches the threshold under the export stress test in line with the debt path of the last DSA. Liquidity indicators (debt service to revenue and to export ratios) continue to be below their respective thresholds under the baseline mainly due to the significantly concessional characteristics of Cabo Verde's external debt. The PV of total public debt-to-GDP ratio is projected to breach the threshold during 2023–2027 under the baseline scenario and breaches the threshold under the stress tests over the forecast period. The*

[1] Cabo Verde's debt-carrying capacity is assessed as "strong" as in the previous DSA with a composite index (CI) score of 3.24, which is based on the October 2023 WEO and the 2022 CPIA.

external and overall debt outlook is assessed to be sustainable contingent on meeting several assumptions. These include steady economic growth around potential, consistent fiscal consolidation in line with the ECF program, and significant structural reforms, especially related to State-Owned Enterprises (SOEs). Enhancing the performance of SOEs will help reduce critical fiscal risks and foster a better 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 is also needed for long-term debt sustainability.

PUBLIC DEBT COVERAGE

1. The debt coverage in this DSA comprises debt owed by the central government and certain government guarantees. Coverage of the public sector is in line with June 2023 DSA (Table 1). Government guarantees to SOEs' external borrowing are included in the baseline stock of debt (0.9 percent of GDP at end-2022), but publicly guaranteed domestic debt (8.2 percent of GDP at end-2022) and non-guaranteed domestic debt by SOEs are not included. Consistent with the fiscal accounts, social security funds and local governments[2] are excluded from the DSA. The coverage of extra budgetary funds (EBFs) is focused on government support to State-Owned Enterprises (SOEs) through on-lending and capitalization. Authorities are undertaking efforts to widen the coverage and reporting of public sector debt, including through support from the World Bank.[3] External debt is defined on a residency basis.

2. 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 kept at the default level consistent with the size of publicly guaranteed domestic debt of local governments.[4] The social security fund (INPS) financial position is strong, and fiscal risk is minimal, as a result the contingent liability stress test is not adjusted for its exclusion. Second, the default shock of 2 percent of GDP for SOEs' debt is raised to 28.2 percent of GDP to reflect vulnerabilities associated with publicly guaranteed domestic borrowing by all SOEs amounting to bout CVE 20 billion at end-2022 (8.5 percent of GDP); and non-guaranteed domestic debt of a subset of SOEs classified with "very high risk" of insolvency of about CVE 48 billion

[2] Government-guaranteed domestic borrowing of municipalities from the banking system stood at CVE 465 million at end-December 2022 (see Text Table 2 for more details) and it is not included in the contingent liability shock due to its low fiscal risk.

[3] Efforts to expand debt coverage have been supported by the World Bank through the Performance and Policy Actions under the Sustainable Development Financing Policy (SDPF). Specifically, the coverage of the quarterly public debt bulletin has been broadened to include debt of SOEs, the social pension fund, and guaranteed debt from municipalities.

[4] According to authorities, the stock of local government debt is either directly guaranteed by central government or indirectly via the use of future transfer from the central government as collateral.

(19.9 percent of GDP).[5] Third, the default shock of 1.1 percent of GDP is kept for public private partnerships (PPPs). Fourth, with mainly foreign-owned banks that are well-capitalized, Cabo Verde's financial sector appears sound and the default minimum value of 5 percent of GDP for the financial market shock seems appropriate.

3. Ongoing improvements in SOEs' risk assessment and broader fiscal transparency are key steps in the right direction. Financial reporting and governance of the SOEs has improved. Key reform measures include: (i) the adoption of the IMF's SOE Health Check Tool to strengthen the analysis and assessment of fiscal risks from SOEs by the SOEs unit (*Unidade de Acompanhamento do Sector Empresarial do Estado* - UASE) (Q1-2022); (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 dissemination of quarterly reports on SOEs' performance; (iv) adopting and publishing a comprehensive ownership policy to help further improve the ownership and oversight of the portfolio of SOEs; and (v) the establishment of PARPÚBLICA as the company managing the state's corporate investments and IMOPÚBLICA, as the company managing the state's immovable property. In addition, measures to enhance the set of publicly available information such as *Portal da Transparência* initiative and the *SOE Manager* are welcome.[6]

[5] The quarterly SOE report published by the Minister of Finance discloses the SOEs` risk assessment following the methodology provided by the IMF SOE Health Check Tool. The report assesses the risk of solvency distress through two liability ratios. The following SOEs were classified with very high risk in the Q4 2022 SOE report and included in contingent liability shock: ADR, ADS, AEB, CVFF, ELECTRA, INFORPRESS, NEWCO, TICV, and TACV.

[6] The 'SOE Manager' platform is a digitized ICT tool and database aimed to systematically capture data directly and in real-time from SOEs. Based on the inputs provided by SOEs, it automatically generates aggregate performance information and dashboards for the SOE ownership institution (UASE). This will facilitate the preparation of annual aggregate SOE portfolio and quarterly performance reports which UASE has prepared in recent years. The SOE Manager could also help anticipate potential SOE performance challenges more proactively and inform related fiscal risk analysis.

Figure 1. Cabo Verde: SOEs Risk Map, Q4-2022[1/]

Companies	Q42022					
	Profitability		Liquidity		Solvency	
	ROA	ROE	General	Reduced	Liabilities/Assets	Liabilities/Equity
AdR	Moderate Risk	Very High Risk			Very High Risk	Very High Risk
AdS	Moderate Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk
AEB	High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk
APN	Moderate Risk	Low Risk	Very Low Risk	Very Low Risk	High Risk	Very High Risk
ASA	Moderate Risk	Moderate Risk	Very High Risk	Moderate Risk	Moderate Risk	Moderate Risk
BVC	Low Risk	Moderate Risk	Very Low Risk		Very Low Risk	Very Low Risk
CABEOLICA	Low Risk	Low Risk	Low Risk		Moderate Risk	High Risk
CABNAVE	Moderate Risk	Moderate Risk	Very Low Risk	Very Low Risk	Low Risk	Low Risk
CCV	Moderate Risk	Moderate Risk	Very Low Risk	Very Low Risk	Very Low Risk	Very Low Risk
CERMI	Moderate Risk	Moderate Risk	Very Low Risk	Very Low Risk	Very Low Risk	Very Low Risk
CVB	Moderate Risk	Moderate Risk	Very High Risk	Very High Risk	Low Risk	Low Risk
CVFF	Moderate Risk	Very High Risk	Very High Risk		Very High Risk	Very High Risk
CVT	Moderate Risk	Moderate Risk	Very High Risk	High Risk	Moderate Risk	High Risk
ECV	Very Low Risk	Very Low Risk	Moderate Risk		Moderate Risk	High Risk
EHTCV	High Risk	High Risk	Very Low Risk	Very Low Risk	Very Low Risk	Very Low Risk
ELECTRA	Moderate Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk
EMPROFAC	Moderate Risk	Moderate Risk	Very Low Risk	Very Low Risk	Low Risk	Low Risk
ENAPOR	Moderate Risk	Moderate Risk	Very High Risk	Very High Risk	Moderate Risk	Moderate Risk
FIC	Very Low Risk	Very Low Risk	Low Risk	Very Low Risk	Low Risk	Low Risk
ICV	Moderate Risk	Low Risk	High Risk		High Risk	Very High Risk
IFH	High Risk	High Risk	Very Low Risk	Very High Risk	High Risk	Very High Risk
INCV	Moderate Risk	Moderate Risk	Very Low Risk	Very Low Risk	Moderate Risk	Very High Risk
INFORPRESS	Moderate Risk	Very High Risk	Very High Risk		Very High Risk	Very High Risk
LEC	High Risk	High Risk	Very Low Risk		Very Low Risk	Very Low Risk
NEWCO	Moderate Risk	Moderate Risk	Very Low Risk		Very High Risk	Very High Risk
NOSI	Very Low Risk	Very Low Risk	Low Risk		Moderate Risk	Very High Risk
RTC	High Risk	Very High Risk	Very High Risk		High Risk	Very High Risk
SCS	Low Risk	Very High Risk	Very High Risk	High Risk	Moderate Risk	High Risk
SDTIBM	High Risk	Very High Risk	Very High Risk	Very High Risk	Moderate Risk	Very High Risk
SISP	Very Low Risk	Very Low Risk	Very Low Risk	Very Low Risk	Low Risk	Very Low Risk
TACV	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk
TECHPARK	Very High Risk	High Risk	Very Low Risk		Very Low Risk	Very Low Risk
TICV	Very High Risk	Very High Risk	Very High Risk		Very High Risk	Very High Risk

Source: Cabo Verdien authorities; and IMF staff estimates.

1/ See Heath Check Tool user guide for a detailed discussion of methodology.

Box 1. Considerations on Broadening DSA Coverage in Cabo Verde

The coverage of the Debt Sustainability Framework (DSF) should be as broad as possible. According to the 2018 IMF Guidance Note on the Bank-Fund DSF for Low-income Countries (GNDSFLIC),[1] the debt perimeter should encompass almost the entirety of public sector debt including private sector debt guaranteed by the public sector, with the exception of public financial corporations. The number of IDA countries improving the transparency in their debt reporting practices is slowly increasing. The World Bank's Debt Reporting[2] heat map shows that in 2021, 13 countries disclose information on central government guarantees (including names of beneficiaries), account payables, collateralization details, and debt-related contingent liabilities. A limited definition of public debt in the DSA can contribute to unexpected increases in the level of debt explained by sources outside the defined perimeter.

If the public sector coverage of the DSA differs from fiscal accounts, additional adjustments are on the fiscal accounts will be necessary to ensure consistency. The debt service-to-revenue ratio, a key indicator of liquidity, requires its numerator and denominator to be consistent (i.e., in terms of scope). If SOEs, a key source of fiscal risk, are part of the public debt, whether directly or through guarantees, it's essential to include any net income they generate in the calculation, as it could be used to repay the debt. The IMF and WB are engaging with the authorities to expand the scope of debt coverage consistently. The launch of the SOE dashboard, an initiative supported by the WB, in October 2023 should pave the way for the inclusion of SOEs domestically guaranteed debt. The SOE manager provides the data needed to widen the DSA perimeter. Bank and Fund staff will engage with the authorities to prepare for the broadening of public debt coverage to include domestically guaranteed SOE debt in the next DSA cycle by separately identifying the debt servicing costs for the guaranteed debt.

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[1] For a detailed discussion see Paragraph 21 and Appendix III of the 2018 IMF Guidance Note on DSF for Low-income Countries.

[2] Debt Transparency: Debt Reporting Heat Map (worldbank.org).

Box 2. Further Reforms Are Needed to Reduce Fiscal Support from the Government to SOEs

Explicit subsidies to SOEs have increased since the pandemic. At end-2022, explicit subsidies to SOEs reached 0.2 percent of GDP and are projected to increase to 0.4 percent of GDP in 2023 according to the budget. The expansion in comparison to the pre-pandemic period is explained by the creation of a compensation to i) the inter-island transportation company and ii) energy/water SOEs to implement social tariff for energy and water targeted to poor households.

The combined fiscal support via on-lending and capitalization was, on average, about 2.4 percent of GDP between 2015 and 2022. During this period, on-lending loans to SOEs totaled on average around 1.4 percent of GDP that were mainly channeled to Electra and TACV. Capitalization flows, in turn, were on average about 1 percent of GDP mainly directed to support TACV.

Fiscal risks from SOEs' domestically guaranteed debt have grown over time. Before the Covid-19 outbreak in 2020, the stock of SOEs' domestically guaranteed debt remained stable, but there were significant quasi-fiscal transactions below the line to SOEs via on-lending and capitalization. After the pandemic, the stock of SOEs' domestically guaranteed debt jumped to about 8 percent of GDP, while quasi-fiscal flows decreased. The DSA for Cabo Verde captures the flows steaming from quasi-fiscal operations but does not capture the stock of SOEs' domestically guaranteed debt.

Recent improvements in data availability are a key step in the right direction to enhance SOE's risk assessment and policy design. In October 2023, the MoF launched the *SOE Manager*, an IT platform developed with the support of the WB and IMF that will allow for the monitoring and evaluation of the SOE sector's performance by automating data collection, processing, and analysis. The new SOE dashboard provides the needed conditions in terms of data to authorities properly design further reforms to reduce the support of the central government to SOEs through explicit subsidies, new guarantees, on-lending loans, and capitalization (Table 1).

Further improvements in the overarching strategy to reduce the fiscal support to SOEs are welcome. The Authorities have embarked on a new SOE reform agenda, adopted through the Council of Ministers Resolution 104/2022. The reform agenda includes uses a bottom-up approach to revising the business plan of key SOEs, aiming to increase their profitability. For example, capitalization expenditures to support TACV are projected to cease in 2025 reflecting the current company business plan which aims to increase routes. However, additional efforts to speed up the privatization agenda and improve the financial performance of loss-making enterprises are needed to reduce the fiscal support to SOEs.

Table 1. Cabo Verde: Fiscal Support to SOEs

Stock of SOE Guaranteed Debt (Percent of GDP)

	2015	2016	2017	2018	2019	2020	2021	2022
Domestic Debt (A)	5.4	5.5	5.7	5.5	6.3	8.5	9.8	8.5
External Debt (B)	0.4	0.3	0.9	0.8	0.2	0.9	1.2	0.9
Total SOE-Guaranteed Debt (A+B)	**5.8**	**5.8**	**6.6**	**6.3**	**6.4**	**9.4**	**11.0**	**9.4**

Flow of fiscal support for SOEs (Pecent of GDP)

	2015	2016	2017	2018	2019	2020	2021	2022
Explicit subsidies (C)	0.1	0.1	0.0	0.1	0.0	0.1	0.1	0.2
Total flow above the line (C)	**0.1**	**0.1**	**0.0**	**0.1**	**0.0**	**0.1**	**0.1**	**0.2**
Net increase in domestic guarantees (D)		0.1	0.2	-0.2	0.7	2.2	1.3	-1.3
Net increase in external guarantees (E)		0.0	0.6	-0.1	-0.6	0.8	0.3	-0.3
On-lending loans (F)	2.3	2.5	2.1	0.7	1.7	0.9	0.7	0.5
Capitalization (G)	0.8	0.8	0.6	1.9	2.0	0.4	0.4	1.2
Total flow below the line (D+E+F+G)	**3.1**	**3.3**	**3.5**	**2.4**	**3.8**	**4.3**	**2.7**	**0.0**
Total Flow of fiscal support for SOEs (C+D+E+F+G)	**3.2**	**3.4**	**3.5**	**2.4**	**3.9**	**4.4**	**2.7**	**0.2**

Source: Cabo Verdien authorities and IMF staff calculations.

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

A. Please select "X" for each subsector of the public sector below when it is covered in your public debt data.

	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

B. Please customize elements of the contingent liability tailored test, as applicable.

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	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	28.2	To reflect vulnerabilities associated with guaranteed and non-guaranteed domestic debt.
4	PPP	35 percent of PPP stock	1.2	
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)		34.4	

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. Cabo Verde experienced robust tourism driven growth in the pre pandemic period, which was supported by structural reforms, particularly in the SOE sector. Between 2016 and 2019, growth averaged 5 percent per year, supported by favorable global conditions coupled with important structural reforms, mainly impacting on the SOE sector. Public debt had decreased from its peak of 115.6 percent of GDP in 2015to 109.4 percent in 2019.

5. The COVID-19 pandemic contributed to a substantial increase in external and overall public sector debt levels. Total public sector debt reached 152 percent of GDP at end-2021 up from 109.4 percent in 2019 (Text Figure 1). The increase in the debt ratio was due to the large output contraction of 20.8 percent and a higher public sector overall deficit of 9.3 percent of GDP in 2020, which was financed mainly with increased external concessional borrowing, largely from multilateral institutions to mitigate the impact of the economic shock particularly on the most vulnerable groups.

6. A strong rebound in economic growth in 2022 coupled with fiscal policy tightening resulted in a decrease in the debt to GDP ratio. The tourism driven economic recovery from the pandemic induced recession was strong as the economy grew by 17 percent in 2022. The primary deficit sharply contracted to 2 percent of GDP in 2022 implying a solid fiscal consolidation impulse of 3.4 percent GDP, chiefly explained by a contraction of primary expenditures, vis-à-vis the 2021 primary deficit of 5.4 percent of GDP. The combined effect of robust fiscal consolidation and output recovery caused a significant reduction in the debt to GDP ratio to 127.1 percent of GDP at end 2022.

7. Public external debt is highly concessional and multilateral institutions are the main creditors (Text Table 1). The International Monetary Fund, World Bank, and the African Development Bank account for about 43.8 percent of external public debt. Bilateral creditors account about 19.7 percent of external public debt, of which Portugal is the largest creditor. Debt service cost is moderate with an average interest rate of about 0.93 percent and average maturity of about 17.2 years. The exchange rate risk is low due to the exchange rate peg. The external assessment suggests an undervaluation of the exchange rate and international reserves are at a comfortable level.

Text Table 1. Cabo Verde: External Debt Profile by Type of Creditors, 2022

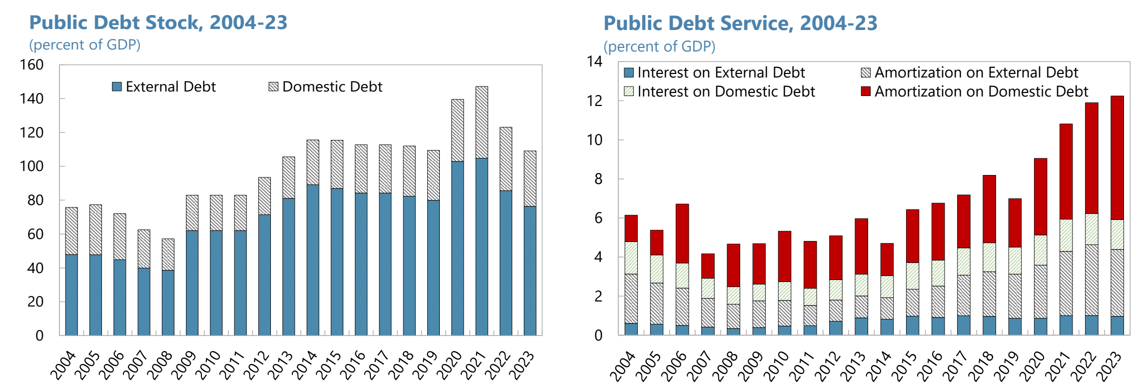
	Percent of GDP	Percent of external debt	Average maturity (in years)	Average interest rate
Multilateral	48.4	56.6	18.8	0.92%
Bilateral	16.8	19.7	11.2	0.85%
Commercial	20.3	23.8	11.4	1.59%
Total external debt	85.6	100.0		

Source: Cabo Verdean authorities and IMF staff estimates.

8. Commercial creditors hold 23.8 percent of external public debt, and commercial debt consists mainly of debt owed to Portuguese based Caixa Geral de Depósitos (CGD). CGD accounts for 82.8 percent of total commercial loans, provided under favorable terms with an average maturity of 11.4 years and average interest rate of 1.6 percent.

9. At end-2022, domestic debt accounted for 30.5 percent of total public debt (Text Figure 1), a slight increase from 29 percent at end-2021. Domestic debt is mostly held by the banking sector in the form of medium and long-term Treasury securities. Treasury bonds accounted for 96.2 percent, with an interest rate of about 3.8 percent. Commercial banks hold 64.2 percent of domestic government securities and non-banks hold 35.8 percent, most of which is with the national social security fund. Access to domestic debt is supported by excess liquidity in the banking system and interest rates on domestic debt remains moderate. The reliance on domestic debt has been largely steady over last decade around 30 percent of total public debt, and the refinancing risk is relatively low as the average maturity is around 7 years. In addition, the sizeable government deposits (about 10 percent of GDP) are an important risk mitigating factor that can be used in a stress event as a source of financing to the domestic debt.

Text Figure 1. Cabo Verde: Profile of Public Debt and Debt Service, 2004–23



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

10. Debt service on external public debt is moderate. The ratio of public external debt service to exports declined from 14.8 percent in 2021 to 6.3 percent in 2022, reflecting the strong rebound in exports as the tourism sector recovered. The ratio is estimated to decline steadily from 2024 onwards as the economy converges to potential and exports remain healthy due to the expansion of capacity in the tourism sector. The ratio of public external debt service to revenue decreased to about 10.4 percent in 2022 from 13.9 percent in 2021 and is projected to peak to about 17 percent of GDP by 2023 and average about 14 percent over the medium term (2025-2030), declining thereafter. Total public debt service absorbed about 31 percent of revenue and grants in 2022 and is projected to reach 39 percent in 2026 and steadily decline thereafter.

11. Publicly guaranteed debt stood at CVE 26.4 billion (11.2 percent of GDP) at end-2022 (Text Table 2). The State guarantee is mainly issued for SOEs' domestic debt.[7] For 2022, the stock of publicly guaranteed domestic debt consists primarily of liabilities of ELECTRA, Aguas de Santiago, TACV, Prog. Start-up/Ecosistema, NEWCO and ICV and AEB to the domestic banking system; and borrowing by a few municipalities. TACV, ELECTRA, NEWCO, and Prog. Start-up/Ecosistema were the recipients of the largest guarantees in 2022.[8]

Text Table 2. Cabo Verde: Publicly-Guaranteed Debt, 2019–2022

	2019			2020			2021			2022		
	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)	**395**	**0.2**	**100.0**	**1,655**	**0.9**	**100.0**	**2,243**	**1.2**	**100.0**	**2,121**	**0.9**	**100.0**
contracted by SOEs	395	0.2	100.0	1,655	0.9	100.0	2,243	1.2	100.0	2,121	0.9	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)	**14,231**	**6.4**	**100.0**	**15,618**	**8.8**	**100.0**	**22,157**	**11.9**	**100.0**	**24,255**	**10.3**	**100.0**
contracted by local governments	363	0.2	2.5	356	0.2	2.3	382	0.2	1.7	465	0.2	1.9
contracted by SOEs	13,858	6.3	97.4	14,972	8.5	95.9	18,175	9.8	82.0	19,865	8.5	81.9
contracted by private entities	9	0.0	0.1	290	0.2	1.9	3,601	1.9	16.3	3,925	1.7	16.2
Total Publicly-Guaranteed Debt (A+B)	**14,626**	**6.6**		**17,273**	**9.8**		**24,401**	**13.1**		**26,375**	**11.2**	

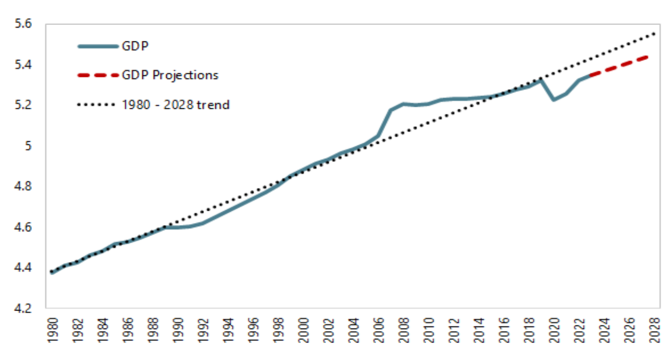
Source: Cabo Verdean authorities and IMF staff calculations.

12. Historical private external debt derived from international investment position (IIP) data indicate a stock of about 18.1 percent of GDP at end-2022. Private debt includes both bank and non-bank external debt.

B. Outlook and Key Macroeconomic Assumptions

13. Compared to the last DSA (June 2023) the macroeconomic assumptions underlying the projections have been kept roughly stable. Inflationary pressures are expected to remain elevated in 2023 although declining from the highs of 2022, as the pass through from international oil and food prices continue to affect Cabo Verde with imports accounting for about 80 percent of consumption products.

Text Figure 2. Cabo Verde: Real GDP
(Millions of 2015 CVE, log scale)



[7] While information about the stock of domestic guarantees granted to SOEs and its implied debt service is available, the lack of data on SOEs revenues and net income prevents its inclusion in the DSA baseline (Box 1). The WB and the IMF will work with Authorities to improve data with a view to inclusion of domestic SOE guarantees in the next DSA.

[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.

14. The level of GDP from 2019 to 2022 was revised in Q1 2023 to further finetune the completion of the rebasing of the national account statistics from 2007 to 2022.[9] The published data indicates nominal GDP in 2022 was 4.5 percent lower compared to the last DSA reflecting a more accurate measure of the services sector due to a further revision of the GDP rebasing from 2007 to 2015.

15. GDP growth is projected to be broadly in line over the medium term compared to the last published DSA (IMF Country Report No. 23/262). Real GDP contracted by 20.8 percent in 2020 due to the impact of the COVID19 pandemic. Economic growth rebounded strongly over the next two years to reach 5.6 percent in 2021 and 17 percent in 2022, with output surpassing the pre pandemic level. The real growth rate is projected to decelerate to 4.5 percent in 2023 moving towards around 4.7 percent over the medium and thereafter converging to potential growth of 4.5 percent. (Text Figure 2 and Text Table 3).

Text Table 3. Cabo Verde: Assumptions for Key Economic Indicators, 2022–43

	2022	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.	2028 - 32 Proj.	2033 - 43 Proj.
Real GDP growth								
Current DSA	17.1	4.5	4.7	4.7	4.6	4.6	4.5	4.5
June 2023 DSA	17.7	4.4	4.5	4.6	4.6	4.7	4.5	4.5
2022 ECF Request	4.0	4.8	5.7	5.5	5.0	4.5	4.5	4.5
GDP Deflator								
Current DSA	7.7	4.7	2.0	2.0	2.0	2.0	2.0	2.0
June 2023 DSA	6.4	4.5	2.0	2.0	2.0	2.0	2.0	2.0
2022 ECF Request	4.5	2.6	2.0	2.0	2.0	2.0	2.0	2.0
Fiscal balance (including grants)								
Current DSA	-4.3	-3.4	-3.4	-2.1	-1.2	-0.4	-0.9	-1.5
June 2023 DSA	-4.2	-4.4	-3.2	-2.4	-2.4	-0.6	-0.7	-2.1
2022 ECF Request	-6.3	-5.6	-4.0	-2.1	-0.9	-0.8	-1.4	-2.9
Overall financing needs (including onlending)								
Current DSA	-4.3	-4.0	-3.6	-2.3	-1.3	-0.4	-0.9	-1.5
June 2023 DSA	-4.2	-3.7	-4.0	-2.4	-2.4	-0.6	-0.7	-2.1
2022 ECF Request	-7.0	-6.2	-4.2	-2.3	-1.1	-0.8	-1.4	-2.9
Current account balance (including grants)								
Current DSA	-3.7	-5.9	-6.1	-6.3	-5.8	-5.4	-3.7	-1.5
June 2023 DSA	-3.6	-5.6	-4.6	-4.4	-4.4	-3.7	-3.2	-1.9
2022 ECF Request	-14.1	-6.2	-5.9	-4.7	-4.6	-4.2	-3.6	-3.2
Total Debt/GDP Ratio								
Current DSA	127.1	119.9	116.2	111.2	105.4	99.4	83.5	58.3
June 2023 DSA	121.2	112.8	109.7	106.0	102.2	96.6	81.4	59.0
2022 ECF Request	145.9	139.7	132.5	124.0	116.2	109.5	94.2	73.9
Cv$/USD exchange rate (e-o-y)								
Current DSA	104.1	99.7	99.4	99.0	99.1	99.5	99.9	99.9
June 2023 DSA	104.1	104.3	104.7	105.1	105.5	106.4	107.5	107.5
2022 ECF Request	98.5	96.9	95.8	95.0	94.5	94.2	94.2	94.2

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

16. 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 recently completed a new five-year development strategy (*Plano Estratégico para o Desenvolvimento Sustentável* – PEDS II) building on the long-term development plan (Cabo Verde Ambition 2030). Priority areas include (i) completing SOE reforms, including through privatization, and improving the efficiency of

[9] The rebasing involved changing the base year from 2007 to 2015 and the updated accounts were published in March 2023.

public enterprises; (ii) promoting economic diversification by leveraging the potential of the blue economy; (iii) reducing the level of informality; and (iv) facilitating access to finance, particularly for small and medium-sized enterprises. The implementation of key reforms will be supported through technical assistance and project financing from the World Bank and the ongoing ECF arrangement. The key macroeconomic assumptions are:

- *Real GDP growth*. Cabo Verde's real GDP expanded by 17 percent in 2022.[10] Growth is projected to decline to 4.5 percent in 2023 and gradually converge to long-term growth of 4.5 percent (which will be supported by key structural reforms described above in paragraph 16).[11]

- *Tourism services*. The framework assumes continued growth in the tourism sector reflecting in part an increase in hotel capacity linked to the opening of new hotels, diversification of markets and steady FDI inflows. The framework assumes continued moderate impact of Russia's invasion of Ukraine as pent-up demand for travel and Cabo Verde being viewed as safe destination will continue to lure visitors. UK, Portugal, Germany, and Belgium are the most common countries of origin of tourists arriving in Cabo Verde. The impact of continued growth in the tourism sector will be evidences through higher services exports and increased tax revenues – with a positive impact on debt sustainability.

- *Inflation*. Inflation increased to 7.9 percent and the GDP deflator to 7.7 percent in 2022 in line with the increase in fuel and commodity prices, due to the impact of the Russia war in Ukraine. Inflation and the GDP deflator are projected to ease to 5 percent and 4.5 percent, respectively in 2023 and 2 percent by 2024 in line with euro area forecast.

- *The use of RSF resources and climate related risks*. RSF disbursements increase external financing by about CVE 2.1 billion in 2024 and CVE 1 billion in 2025. The RSF substitutes more expensive domestic financing. From 2026 onwards, the funding substitution ends and net domestic issuance returns to its prior path. From the balance of payment standpoint, RSF disbursements increase international reserves by CVE 2.1 billion and CVE 1 billion in 2024 and 2025, respectively. The additional reserve buffer supports the authorities' climate-related investments and reforms and helps catalyze financing for climate change mitigation and adaptation strategies. The public investment path is constrained by the need to put public debt dynamics on a firm downward path. Thus, it is below the Nationally Determined Contribution (NDC) estimation of the total funding required to support climate adaptation and mitigation activities. The NDC estimates investment needs (public and private) between now and 2030 at about 6.1 percent of GDP per year. The macro-framework assumes productivity-enhancing and climate-related reforms help lift potential growth.

[10] The 2022 growth rate is mainly explained by the economic activity recovery as the GDP rebasing chiefly impacted the nominal level of GDP but not its trend.

[11] The long-term historical trend growth rate (1980-2019) was 4.8 percent and 4.5 percent considering also the post-COVID period (1980-2022).

- *Public sector deficit*. The current framework is predicated on an ambitious and steadfast revenue-driven fiscal consolidation path. From the expenditure side, the medium-term expenditure path entails a gradual decrease of primary expenditures-to-GDP, taking in to account consistency with the climate agenda, and the reforms needed to lay the groundwork for such policies, with a smooth increase of capital expenditures coupled with the wage bill and use of goods and services growing below inflation after the 2024 increase in both items to partially attenuate the impact from the nominal freezing in the last couple of years. The overall fiscal deficit improved from 7.7 percent of GDP in 2021 to 4.3 percent of GDP in 2022 and is projected to improve further over the medium-term to reach 0.7 percent of GDP in 2027. The fiscal effort in the near and medium term is assumed to be underpinned by improved domestic revenue mobilization and current expenditure restraint. 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 have already been implemented. In addition, the authorities have committed to reviewing tax expenditures that would net up to1 percent of GDP in 2025 and help fill the gap due to the delay of the ECOWAS common external tariff. Fiscal adjustment will be implemented with safeguards to protect and broaden support for the vulnerable. Reforms to SOEs are expected to result remove capitalization and on lending expenditures from 2025 and 2027, respectively. The additional income from grants and other revenues will allow for higher investment over 2024 and 2025 before capital spending returns to the baseline path in 2026, which implies more adjustment in that year than under the 2nd review due to the higher-than-expected revenue collection in 2024. The projected improvement in the fiscal balance from a deficit of -4.3 percent of GDP in 2022 to -0.4 percent of GDP by 2027 is expected to result in a reduction in government financial support and would bring net fiscal financing needs[12] to about 0.7 percent of GDP by 2027.

- *Current account deficit*. The medium-term current account deficit is forecasted to be broadly about the same as in the previous DSA and is projected to remain above 5.9 percent of GDP from 2024–26. The baseline scenario assumes a current account deficit of 5.5 percent in 2023 and 6.1 percent in 2024. This reflects the impact of moderate growth in tourism driven by increased capacity, higher fuel, and commodity prices, as well as continued investments in the tourism sector on imports. The current account deficit is projected to decline to about 5.1 percent of GDP in 2027 supported by tourism receipts and steady growth in remittances. Strong export performance and increased remittances, together with higher FDI inflows and IMF financing under ECF and RSF would help sustain international reserves at about 6 months of prospective imports. In comparison with the last DSA, the current account is projected to worsen due to an increase in imports associated with the implementation of the climate reform agenda and the importing of low carbon technologies, while FDI is

[12] Net financial needs take into account the net impact of new borrowing and refinancing of principal payments in line with authorities' fiscal accounts.

projected to improve in the medium term in line with the catalytic impact of the RSF and growth in the tourism sector (which has been the main beneficiary of FDI inflows).

17. 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 2023 budget will be filled mostly with concessional and semi-concessional loans, mainly from multilateral institutions including the World Bank, African Development Bank, other bilateral partners. Multilateral and bilateral funding for budget support around US$95 million, about 3.6 percent of GDP is expected to be provided during 2023. 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 in line with the profile of domestic debt portfolio at end-2022. The average interest rate is set to 3 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 (1.2 percent of GDP) of the recent SDR allocations to finance the 2022 and 2023 budget.

18. 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, and expenditure restraint supported by average growth near potential. The proposed primary balance adjustment path of about 2 percent of GDP over 2023–25 is at the lower bound of the top quartile of the historical distribution for LICs. However, the authorities have identified and implemented some of the policy measures which they estimate could increase revenue collections by close to 1 percent of GDP. In that regard the authorities increased the rate of the tourist tax, implemented the 5 percent duty on previously exempted imports and continue to advance revenue mobilization efforts including from electronic tax invoicing. The adjustment will be supported by relatively persistent and steady growth at about the historical average. 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 5). Tools for assessing the realism of the baseline scenario do not flag significant and systematic deviations from historical experience.

- Drivers of debt dynamics (Figure 4). 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 but the impact is smaller, while price and exchange rate changes are projected to exert downward pressure on debt accumulation to a larger extent than the historical experience. For total public debt, the projected contribution of real GDP growth to public debt reduction is higher compared to the historical five-year change, reflecting a gradual return to potential growth. 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 primary deficit, current account/prices, and exchange rates were the main drivers of past forecast errors of debt dynamics.

- Consistency between fiscal adjustment and growth (Figure 5). The projected growth path for 2023 and 2024 is not consistent with multiplier-based projections due to the large one off rebound in growth in 2022. 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 a steady increase in economic activity following the return to pre pandemic growth levels, on account of strong activity in the tourism and transportation sectors. In addition, additional growth impetus is expected from structural reforms under the strategic plan for sustainable development (PEDS II).

- Consistency between public investment and growth (Figure 5). The realism tool shows that like historical figures, the contribution of public investment to real GDP growth remains marginal across the 2022 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 average about 4.5 percent of GDP in the medium term, lower than the 2022 DSA, while private investment is expected to average about 30 percent of GDP over 2023-27.

C. Country Classification and Determination of Stress Test Scenarios

19. Cabo Verde's debt-carrying capacity is assessed as "strong" as in the June 2022 DSA for second review of the Policy Coordination Instrument (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 2023 World Economic Outlook (WEO) vintage and the 2022 CPIA, the CI score for Cabo Verde stands at 3.24, 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 (31 percent), world growth (12 percent), remittances (7 percent) and country real growth rate (5 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	3.807	1.47	45%
Real growth rate (in percent)	2.719	5.602	0.15	5%
Import coverage of reserves (in percent)	4.052	56.081	2.27	70%
Import coverage of reserves^2 (in percent)	-3.990	31.450	-1.25	-39%
Remittances (in percent)	2.022	10.912	0.22	7%
World economic growth (in percent)	13.520	2.856	0.39	12%
CI Score			3.24	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

20. **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

21. **Under the baseline scenario, the PV of PPG external debt-to-GDP ratio remains below its threshold throughout the projection period (Figure 2, Tables 2 and 4)**. This represents an improvement driven by robust growth, compared to the 2022 DSA when the threshold was breached for one year, and is broadly in line with the June 2023 DSA. The risk of external debt is assessed as moderate, as was the case in the last DSA. 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, decreasing continuously through the projection period.

22. **The PV of PPG external debt-to-GDP ratio however breaches its threshold for an extended period under the stress test scenarios (Figure 2, Tables 2 and 4)**. Under the

most extreme shock, to depreciation, it rises to about 75.1 percent in 2025 before gradually decreasing to the threshold of 55 percent of GDP up to 2030. The threshold is also breached under four of the remaining six standardized bound tests, albeit to different extents with the breach being more protracted under the exports bound test, and under the tailored combined contingent liabilities test from 2023-33.

23. The PV of PPG external debt-to-exports ratio and debt service to export ratio exceeds the respective thresholds from 2023–33 under the export stress test. The projected trajectories of PPG external debt burden indicators appear vulnerable to exports 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.

24. Cabo Verde is at moderate risk of external debt distress and has limited space to absorb shocks (Figure 6). Cabo Verde's baseline debt burden indicators are below their respective thresholds, but the PV of the debt to GDP ratio is close enough to its respective threshold in the short- and medium-term. The stress test scenarios particularly to exports pushes three of the indicators protractedly above their respective thresholds (Table 4). As a result, Cabo Verde has limited space to absorb shocks.

B. Total Public Debt

25. The PV of total public debt-to-GDP ratio exceeds the 70 percent benchmark through 2027 under the baseline scenario (Figure 3, Tables 3 and 5) giving rise to a mechanical high-risk signal. The prescribed benchmark is also breached under each of the seven standardized bound tests and the tailored combined test, with combined contingent liabilities shock associated with SOEs' debt being the most severe with the threshold being breached throughout the projection period. Furthermore, the debt outlook, as shown by the other public DSA indicators, is particularly vulnerable to export, growth shocks, and climate disaster shocks.[13] The impact of the shocks, including the climate disaster shock, can be seen in Tables 4 and 5.

C. Risk Ratings and Vulnerabilities

26. Cabo Verde's DSA is classified as "moderate" risk of external debt distress. The PV of PPG external debt-to-GDP ratio remains below threshold for the projection period under the baseline scenario, thereby signaling a moderate risk of external debt distress and is particularly sensitive to export and growth shocks.

27. 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 2027, suggesting a high risk of debt distress. Debt service is

[13] The standardized climate disaster shock assumes an increase of public debt of 10 percent of GDP at the second year of the forecast horizon.

projected to average about 37 percent of revenues over the next five years, which represents a moderately large share of future fiscal revenues. Stress tests indicate that Cabo Verde is most vulnerable to a combined contingent liabilities shock associated with SOEs' debt and growth shock. Under these shocks, public debt would remain above the threshold for a prolonged period. The risk of debt distress is partly mitigated by support from Portugal, the main bilateral creditor through an agreement to swap debt service payments on some debt to Portugal (worth on average about 6.6 million Euro per year) up until 2025 for climate-related investments that was agreed before the RSF negotiations.[14]

28. 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 efforts to mobilize additional revenues and continue the strategy of only incurring concessional borrowing.

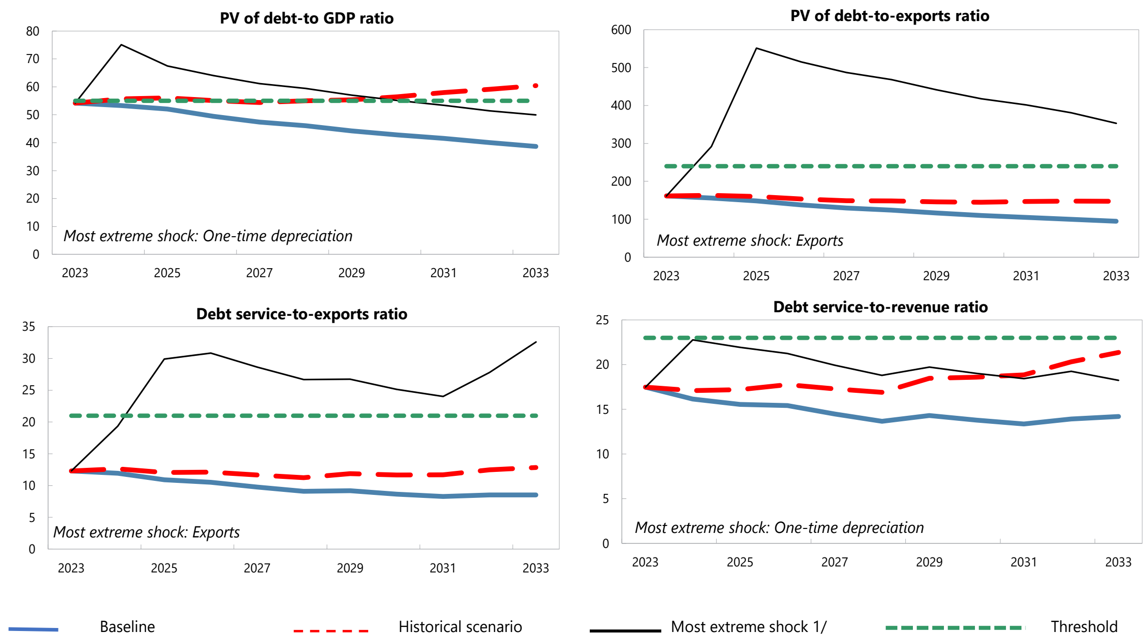
29. There are significant risks to the assessment. The outlook depends primarily on a broadly stable global environment that continues to support a vibrant tourism sector. However, higher fuel and commodity prices and weaker than expected economic outlook in key markets could reduce the rate of economic growth. 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

30. The authorities concurred on the immediate need to both adapt to and mitigate climate risks. They underlined the necessity of progressing with a transformative reform agenda to enhance the climate related fiscal policy and build resilience in the energy and water sector. They highlighted their aim to draw in both private and concessional public funding for investments to reinforce climate-focused policies to foster widespread, inclusive, and resilient economic expansion. They again stressed the significance of diminishing poverty and investing in human capital as integral parts of this transformative plan. Additionally, they indicated their plan to define specific areas of reform and align their requests with the proposed RSF program.

[14] Portugal agrees to swap Cape Verde's debt for environmental investment | Reuters.

Figure 2. Cabo Verde: Indicators of Public and Publicly Guaranteed External Debt Under Alternatives Scenarios, 2023–33



Customization of Default Settings		
	Size	**Interactions**
Standardized Tests		Yes
Tailored Stress		
Combined CL	Yes	
Natural disaster	No	No
Commodity price	n.a.	n.a.
Market financing	n.a.	n.a.

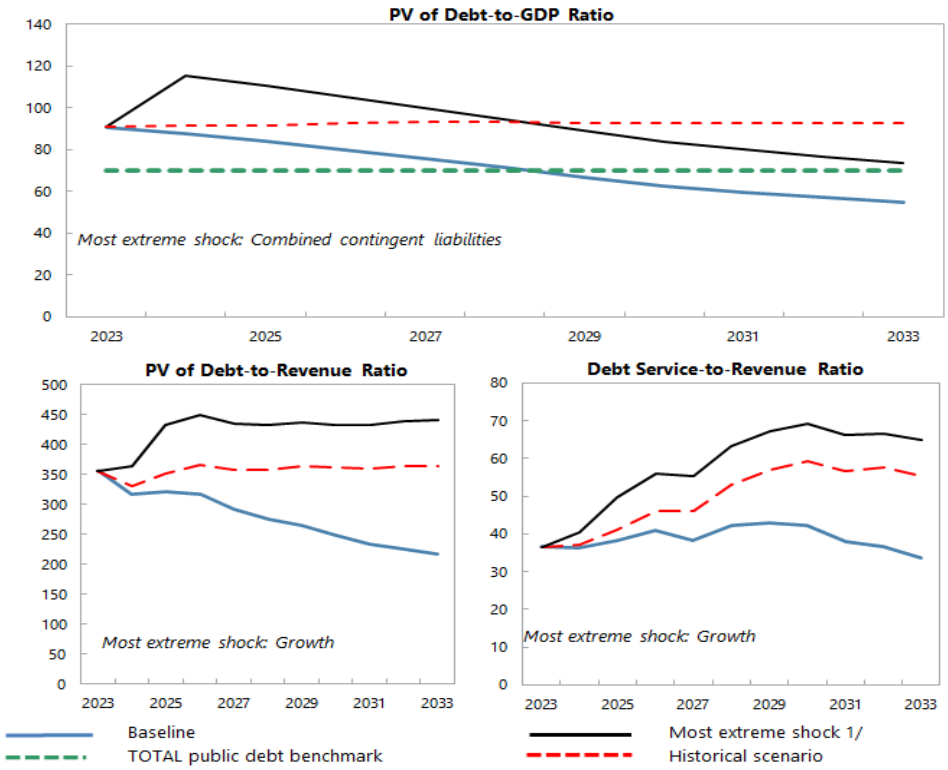
Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the 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	1.4%	1.4%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	23	23
Avg. grace period	7	7

* 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 2033. 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: Indicators of Public Debt Under Alternative Scenarios, 2023–33



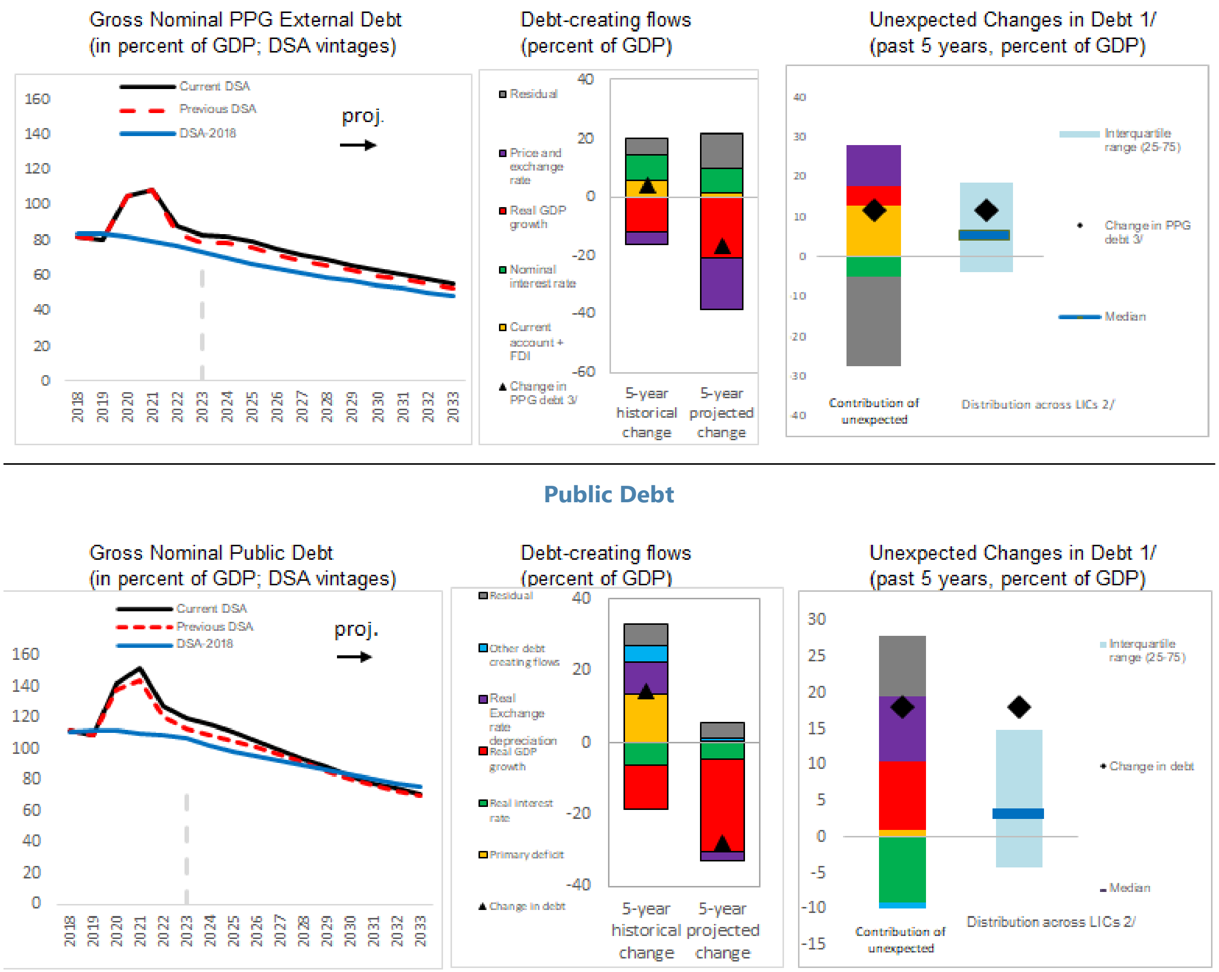
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	50%	50%
Domestic medium and long-term	49%	49%
Domestic short-term	1%	1%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.4%	1.4%
Avg. maturity (incl. grace period)	23	23
Avg. grace period	7	7
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	1.0%	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 2033. 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 4. Cabo Verde: Drivers of Debt Dynamics - Baseline Scenario



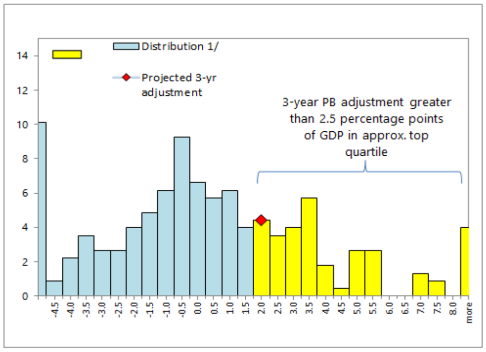
1/ Difference between anticipated and actual contributions on debt ratios.

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.

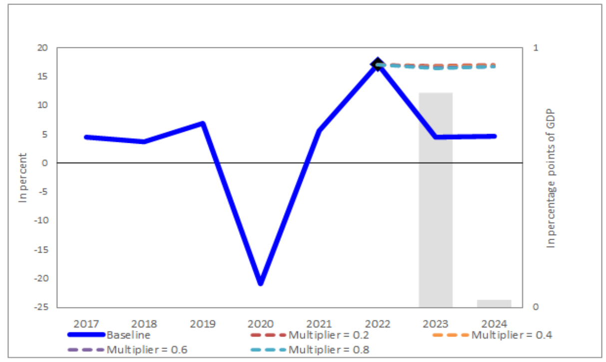
Figure 5. Cabo Verde: Realism Tools

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



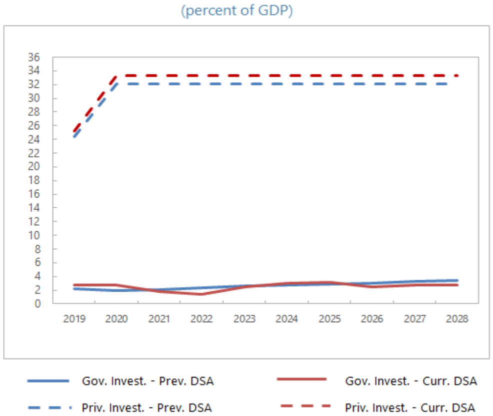
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

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
(percent of GDP)



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

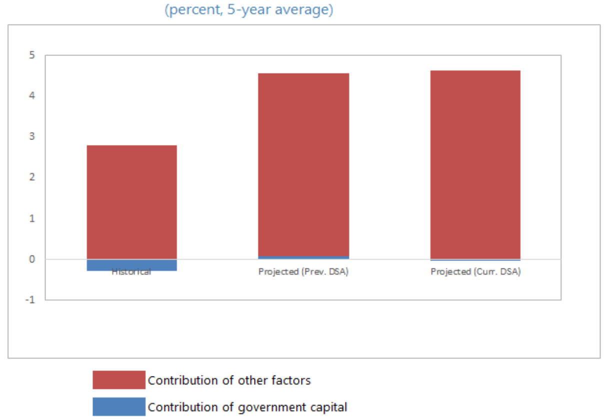


Figure 6. Cabo Verde: Qualification of the Moderate Category, 2023–33[1/]

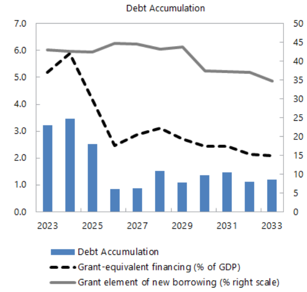
Sources: Country authorities; and staff estimates and projections.

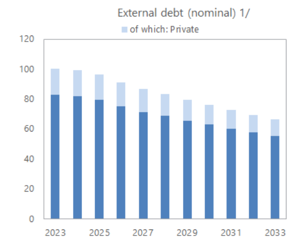
1/ For the PV debt/GDP and PV debt/exports thresholds, x is 20 percent and y is 40 percent. For debt service/Exports and debt service/revenue thresholds, x is 12 percent and y is 35 percent.

Table 2. Cabo Verde: External Debt Sustainability Framework, Baseline Scenario, 2020–43
(Percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
External debt (nominal) 1/	125.9	128.8	106.1	100.4	99.3	96.5	91.3	86.7	83.4	66.4	36.9	101.7	83.8
of which: public and publicly guaranteed (PPG)	105.1	108.2	88.0	82.7	81.9	79.4	75.1	71.3	68.8	55.2	36.9	87.6	69.2
Change in external debt	32.2	2.9	-22.7	-5.8	-1.1	-2.7	-5.2	-4.6	-3.3	-3.0	-2.5		
Identified net debt-creating flows	32.5	-3.0	-15.4	-2.6	-2.4	-2.0	-2.1	-2.2	-2.9	-2.9	-6.3	-0.3	-2.8
Non-interest current account deficit	13.1	10.6	2.6	4.1	4.4	4.6	4.1	3.8	3.0	1.8	-3.5	4.2	3.1
Deficit in balance of goods and services	32.0	32.4	20.3	22.7	23.7	22.9	21.3	20.3	18.8	14.9	7.1	19.4	19.1
Exports	23.2	20.4	35.6	33.6	34.2	35.0	35.9	36.6	37.1	40.9	56.8		
Imports	55.2	52.8	55.9	56.3	57.8	57.9	57.2	56.9	55.9	55.9	64.0		
Net current transfers (negative = inflow)	-18.9	-21.6	-17.9	-16.2	-16.5	-16.3	-15.7	-15.4	-15.1	-13.2	-10.9	-15.8	-15.0
of which: official	-2.7	-2.5	-1.4	-0.3	-0.8	-0.7	-0.6	-0.6	-0.6	-0.4	0.0		
Other current account flows (negative = net inflow)	0.0	-0.1	0.2	-2.4	-2.8	-2.0	-1.5	-1.1	-0.7	0.1	0.3	0.6	-1.0
Net FDI (negative = inflow)	-3.4	-4.6	-4.9	-4.3	-4.1	-3.9	-3.8	-3.7	-3.7	-3.4	-2.6	-4.8	-3.7
Endogenous debt dynamics 2/	22.8	-9.1	-13.1	-2.4	-2.6	-2.7	-2.5	-2.3	-2.1	-1.4	-0.2		
Contribution from nominal interest rate	2.2	1.6	1.1	1.8	1.8	1.6	1.6	1.6	1.6	1.5	1.4		
Contribution from real GDP growth	23.8	-6.5	-19.6	-4.2	-4.4	-4.4	-4.2	-3.9	-3.7	-2.9	-1.6		
Contribution from price and exchange rate changes	-3.3	-4.2	5.5	...	...	...	...	...	...	...	...		
Residual 3/	-0.3	6.0	-7.3	-3.2	1.3	-0.7	-3.1	-2.4	-0.4	-0.1	3.9	3.3	-0.8
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	...	...	58.3	54.2	53.3	52.0	49.5	47.4	46.1	38.7	26.6		
PV of PPG external debt-to-exports ratio	...	...	163.8	161.4	156.1	148.6	137.8	129.5	124.1	94.5	46.7		
PPG debt service-to-exports ratio	18.2	14.8	6.3	12.3	11.9	10.9	10.5	9.8	9.1	8.5	4.8		
PPG debt service-to-revenue ratio	19.3	13.9	10.4	17.48	16.2	15.6	15.4	14.5	13.7	14.2	10.6		
Gross external financing need (Million of U.S. dollars)	696.0	530.9	308.2	474.6	517.1	563.0	591.3	614.0	616.7	834.4	1109.3		
Key macroeconomic assumptions													
Real GDP growth (in percent)	-20.8	5.6	17.1	4.5	4.7	4.7	4.6	4.6	4.5	4.5	4.4	2.4	4.6
GDP deflator in US dollar terms (change in percent)	3.6	3.4	-4.1	8.6	3.3	2.4	2.2	1.6	1.6	2.0	2.0	-0.1	2.7
Effective interest rate (percent) 4/	2.0	1.3	1.0	1.9	1.9	1.8	1.8	1.9	2.0	2.4	3.8	2.1	2.0
Growth of exports of G&S (US dollar terms, in percent)	-57.5	-4.0	96.5	7.1	10.0	10.0	9.6	8.3	7.7	9.0	11.0	6.6	8.7
Growth of imports of G&S (US dollar terms, in percent)	-21.0	4.5	19.0	14.3	11.1	7.5	5.6	5.5	4.5	7.7	4.2	1.7	7.4
Grant element of new public sector borrowing (in percent)	...	...	...	42.9	42.7	42.4	44.7	44.6	43.1	34.8	33.2	...	41.0
Government revenues (excluding grants, in percent of GDP)	21.9	21.8	21.5	23.6	25.2	24.6	24.5	24.7	24.7	24.6	25.7	21.7	24.5
Aid flows (in Million of US dollars) 5/	221.8	199.6	106.4	185.0	202.6	153.1	115.4	134.7	141.9	130.5	215.5		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	5.2	5.9	4.2	2.5	2.9	3.1	2.1	2.0	...	3.2
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	54.0	55.3	53.1	53.6	58.3	54.6	43.8	42.8	...	51.7
Nominal GDP (Million of US dollars)	1,830	1,999	2,246	2,550	2,757	2,958	3,163	3,361	3,569	4,903	9,219		
Nominal dollar GDP growth	-18.0	9.2	12.4	13.5	8.1	7.3	6.9	6.2	6.2	6.6	6.5	2.1	7.4
Memorandum items:													
PV of external debt 7/	...	...	76.4	71.9	70.7	69.2	65.7	62.8	60.7	49.8	26.6		
In percent of exports	...	...	214.6	214.1	206.9	197.6	182.9	171.5	163.6	121.7	46.7		
Total external debt service-to-exports ratio	122.3	100.8	45.1	56.0	54.1	52.3	51.0	49.6	48.6	45.4	32.0		
PV of PPG external debt (in Million of US dollars)			1309.4	1382.0	1470.0	1539.6	1564.9	1592.3	1643.8	1896.9	2449.8		
(PVt-PVt-1)/GDPt-1 (in percent)				3.2	3.5	2.5	0.9	0.9	1.5	1.2	-0.1		
Non-interest current account deficit that stabilizes debt ratio	-19.1	7.7	25.3	9.9	5.4	7.3	9.4	8.4	6.3	4.8	-1.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**Yes**





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) + Εα (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, Ε=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.

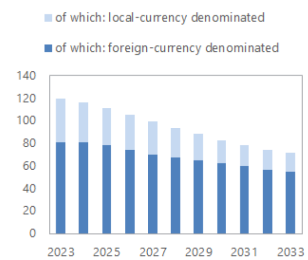
Table 3. Cabo Verde: Public Sector Debt Sustainability Framework, Baseline Scenario, 2020–43

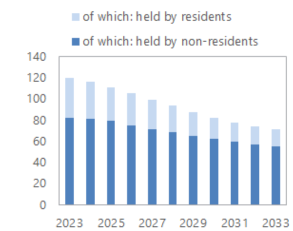
(Percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
Public sector debt 1/	142.6	152.0	127.1	119.9	116.2	111.2	105.4	99.4	93.9	71.3	44.5	118.6	94.6
of which: external debt	105.1	108.2	88.0	82.7	81.9	79.4	75.1	71.3	68.8	55.2	36.9	87.6	69.2
Change in public sector debt	33.2	9.4	-24.9	-7.3	-3.6	-5.1	-5.8	-6.0	-5.6	-3.1	-4.1		
Identified debt-creating flows	28.4	7.6	-21.7	-7.0	-4.9	-5.5	-5.8	-6.1	-5.6	-2.6	-2.1	4.5	-5.0
Primary deficit	6.6	5.4	2.0	1.1	1.1	0.0	-1.0	-1.0	-1.0	0.6	-0.2	2.7	-0.2
Revenue and grants	25.2	23.9	22.4	25.5	27.6	26.0	25.3	25.9	25.8	25.3	26.4	24.0	25.7
of which: grants	3.3	2.1	0.9	1.9	2.3	1.5	0.7	1.2	1.1	0.7	0.7		
Primary (noninterest) expenditure	31.8	29.3	24.4	26.7	28.7	26.0	24.3	24.9	24.8	25.9	26.1	26.7	25.5
Automatic debt dynamics	20.6	3.1	-23.9	-8.7	-6.2	-5.6	-4.9	-5.1	-4.6	-3.2	-1.9		
Contribution from interest rate/growth differential	30.4	-9.2	-29.1	-8.7	-6.2	-5.6	-4.9	-5.1	-4.6	-3.2	-1.9		
of which: contribution from average real interest rate	1.7	-1.7	-6.9	-3.2	-0.8	-0.4	0.0	-0.5	-0.3	0.0	0.1		
of which: contribution from real GDP growth	28.7	-7.6	-22.2	-5.5	-5.4	-5.2	-4.9	-4.6	-4.3	-3.2	-2.1		
Contribution from real exchange rate depreciation	-9.8	12.3	5.2	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	1.2	-0.9	0.2	0.5	0.2	0.1	0.1	0.0	0.0	0.0	0.0	1.8	0.1
Privatization receipts (negative)	0.0	0.0	0.0	0.0	-0.8	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	1.2	-0.9	0.2	0.5	1.0	0.1	0.1	0.0	0.0	0.0	0.0		
Residual	4.8	1.8	-3.2	-0.3	1.3	0.4	0.0	0.1	0.1	-0.5	-1.9	0.0	-0.1
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	97.1	90.8	87.5	83.7	79.9	75.6	71.2	54.8	34.2		
PV of public debt-to-revenue and grants ratio	...	...	433.3	356.0	317.6	321.5	316.3	291.8	275.8	217.1	129.8		
Debt service-to-revenue and grants ratio 3/	39.3	36.9	31.8	36.5	36.3	38.4	40.9	38.3	42.2	33.6	20.6		
Gross financing need 4/	17.7	13.4	9.3	11.0	11.3	10.1	9.4	8.9	9.9	9.1	5.2		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	-20.8	5.6	17.1	4.5	4.7	4.7	4.6	4.6	4.5	4.5	4.4	2.4	4.6
Average nominal interest rate on external debt (in percent)	1.4	0.8	0.5	0.7	0.7	0.6	0.6	0.7	0.7	1.0	1.6	1.1	0.7
Average real interest rate on domestic debt (in percent)	4.1	5.2	-3.4	-0.8	2.6	3.1	3.5	1.5	1.9	3.1	3.2	3.4	2.3
Real exchange rate depreciation (in percent, + indicates depreciation)	-9.7	12.8	6.0	...	...	...	...	...	...	...	...	3.4	...
Inflation rate (GDP deflator, in percent)	0.7	-0.3	7.7	4.7	2.0	2.0	2.0	2.0	2.0	2.0	2.0	1.6	2.2
Growth of real primary spending (deflated by GDP deflator, in percent)	-0.3	-2.5	-2.7	14.2	12.7	-5.0	-2.6	7.3	4.4	6.2	4.3	0.0	5.3
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-26.6	-4.0	26.9	8.4	4.7	5.1	4.8	5.0	4.6	3.8	3.9	-1.2	4.9
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**Yes**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.
1/ Coverage of debt: The central government plus social security and 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 2023–33

(Percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of debt-to GDP ratio											
Baseline	54	53	52	49	47	46	44	43	42	40	39
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	54	**56**	**56**	**55**	54	55	**55**	**56**	**58**	**59**	**60**
B. Bound Tests											
B1. Real GDP growth	54	**60**	**66**	**63**	**60**	**59**	**56**	54	53	51	49
B2. Primary balance	54	55	**55**	53	51	50	48	47	46	45	43
B3. Exports	54	**61**	**73**	**70**	**68**	**66**	**64**	**62**	**60**	**58**	55
B4. Other flows 3/	54	**56**	**58**	55	53	51	49	48	46	45	43
B5. Depreciation	54	**75**	**68**	**64**	**61**	**59**	**57**	**55**	53	51	50
B6. Combination of B1-B5	54	**65**	**69**	**66**	**63**	**61**	**59**	**57**	**56**	53	51
C. Tailored Tests											
C1. Combined contingent liabilities	54	**64**	**63**	**62**	**60**	**60**	**59**	**58**	**57**	**56**	54
C2. Natural disaster	54	**57**	**56**	54	52	51	50	49	48	46	45
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	161	156	149	138	129	124	116	110	105	100	95
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	161	163	160	153	149	148	146	145	147	148	148
B. Bound Tests											
B1. Real GDP growth	161	156	149	138	129	124	116	110	105	100	95
B2. Primary balance	161	160	158	147	140	135	127	121	117	111	105
B3. Exports	161	**292**	**551**	**515**	**487**	**468**	**442**	**418**	**401**	**381**	**353**
B4. Other flows 3/	161	165	164	153	144	138	130	122	117	112	105
B5. Depreciation	161	156	137	127	119	114	106	100	96	91	87
B6. Combination of B1-B5	161	222	171	**252**	238	228	215	203	194	184	172
C. Tailored Tests											
C1. Combined contingent liabilities	161	187	181	172	165	161	155	149	144	139	133
C2. Natural disaster	161	171	164	153	146	141	134	128	123	118	113
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	240	240	240	240	240	240	240	240	240	240	240
Debt service-to-exports ratio											
Baseline	12	12	11	11	10	9	9	9	8	9	9
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	12	13	12	12	12	11	12	12	12	12	13
B. Bound Tests											
B1. Real GDP growth	12	12	11	11	10	9	9	9	8	9	9
B2. Primary balance	12	12	11	11	10	9	9	9	8	9	9
B3. Exports	12	19	**30**	**31**	**29**	**27**	**27**	**25**	**24**	**28**	**33**
B4. Other flows 3/	12	12	11	11	10	9	9	9	9	9	10
B5. Depreciation	12	12	11	10	10	9	9	8	8	8	8
B6. Combination of B1-B5	12	15	18	17	16	15	15	14	14	16	16
C. Tailored Tests											
C1. Combined contingent liabilities	12	12	12	11	10	10	10	9	9	9	9
C2. Natural disaster	12	12	11	11	10	10	10	9	9	9	9
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	17	16	16	15	14	14	14	14	13	14	14
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	17	17	17	18	17	17	18	19	19	20	21
B. Bound Tests											
B1. Real GDP growth	17	18	20	20	18	17	18	17	17	18	18
B2. Primary balance	17	16	16	16	15	14	15	14	14	15	15
B3. Exports	17	16	16	17	16	15	16	15	15	17	21
B4. Other flows 3/	17	16	16	16	15	14	15	14	14	15	16
B5. Depreciation	17	23	22	21	20	19	20	19	18	19	18
B6. Combination of B1-B5	17	17	19	18	17	16	17	16	16	18	19
C. Tailored Tests											
C1. Combined contingent liabilities	17	16	16	16	15	15	15	15	14	15	15
C2. Natural disaster	17	16	16	16	15	14	15	14	14	14	15
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/ A bold value indicates a breach of the threshold.
2/ 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.
3/ Includes official and private transfers and FDI.

Table 5. Cabo Verde: Sensitivity Analysis for Key Indicators of Public Debt, 2023-33

(Percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of Debt-to-GDP Ratio											
Baseline	**91**	**88**	**84**	**80**	**76**	**71**	67	63	60	57	55
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**91**	**91**	**92**	**93**	**93**	**93**	**93**	**92**	**92**	**92**	**92**
B. Bound Tests											
B1. Real GDP growth	**91**	**101**	**114**	**114**	**114**	**113**	**112**	**111**	**111**	**111**	**112**
B2. Primary balance	**91**	**91**	**92**	**87**	**83**	**78**	**73**	69	65	63	60
B3. Exports	**91**	**96**	**105**	**101**	**96**	**91**	**87**	**82**	**78**	**75**	**71**
B4. Other flows 3/	**91**	**90**	**89**	**85**	**81**	**76**	**72**	68	64	62	59
B5. Depreciation	**91**	**109**	**103**	**98**	**92**	**87**	**81**	**76**	**72**	68	66
B6. Combination of B1-B5	**91**	**97**	**100**	**97**	**94**	**90**	**86**	**83**	**80**	**77**	**75**
C. Tailored Tests											
C1. Combined contingent liabilities	**91**	**115**	**110**	**105**	**100**	**94**	**89**	**84**	**80**	**77**	**74**
C2. Natural disaster	**91**	**97**	**93**	**89**	**85**	**80**	**76**	**71**	68	65	63
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.
TOTAL public debt benchmark	70	70	70	70	70	70	70	70	70	70	70
PV of Debt-to-Revenue Ratio											
Baseline	356	318	322	316	292	276	264	247	235	226	217
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	356	330	351	366	358	358	364	362	361	364	364
B. Bound Tests											
B1. Real GDP growth	356	363	433	450	434	432	437	432	432	438	441
B2. Primary balance	356	330	352	346	319	302	289	271	257	248	238
B3. Exports	356	347	404	399	371	354	342	323	309	297	282
B4. Other flows 3/	356	328	343	338	312	296	284	267	254	244	234
B5. Depreciation	356	394	395	386	356	335	320	299	283	271	260
B6. Combination of B1-B5	356	349	382	384	360	347	339	324	312	305	296
C. Tailored Tests											
C1. Combined contingent liabilities	356	419	423	417	385	366	351	330	314	303	292
C2. Natural disaster	356	352	357	353	327	310	299	281	268	259	251
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	37	36	38	41	38	42	43	42	38	37	34
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	37	37	41	46	46	53	57	59	57	57	55
B. Bound Tests											
B1. Real GDP growth	37	41	50	56	55	63	67	69	66	67	65
B2. Primary balance	37	36	40	45	43	47	47	47	42	39	37
B3. Exports	37	36	39	43	40	44	44	44	39	40	40
B4. Other flows 3/	37	36	39	41	39	43	43	43	38	38	35
B5. Depreciation	37	40	45	49	46	50	52	52	48	48	45
B6. Combination of B1-B5	37	39	44	49	47	53	55	56	53	52	49
C. Tailored Tests											
C1. Combined contingent liabilities	37	36	54	56	53	57	58	58	46	44	41
C2. Natural disaster	37	37	44	46	44	48	49	48	42	41	37
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/ A bold value indicates a breach of the benchmark.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

CABO VERDE

November 22, 2023

THIRD REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA, AND REQUEST FOR AN ARRANGEMENT UNDER THE RESILIENCE AND SUSTAINABILITY FACILITY

WORLD BANK ASSESSMENT LETTER FOR THE RESILIENCE AND SUSTAINABILITY FACILITY

A. Country Vulnerability to Climate Change Including Human, Social and Economic Costs

1. As a Small Island Developing State (SIDS), Cabo Verde is among the countries most vulnerable to climate change. The country is exposed to episodes of long-term droughts, desertification of land, erosion, and extreme rainfall events leading to floods particularly in urban areas. Moreover, sea level rise and loss of biodiversity and ecosystems pose existential threats to the archipelago. The country has recently suffered five consecutive years of drought, which caused significant land degradation. In terms of vulnerability to climate change, the Notre Dame Global Adaptation Initiative ranks Cabo Verde 77 in 2021,[1] which places the country well below its aspirational peers such as Mauritius, Saint Kitts and Nevis, or Saint Lucia.[2]

2. Losses from adverse natural events have already had a significant impact, and could worsen in the absence of climate action. The Annual Average Loss (AAL) from adverse natural events have been estimated at almost 1 percent of gross domestic product (GDP),[3] and quickly implemented (CEM, 2023). These losses are mainly driven by flood-related risks which account for almost 70 percent of the aggregated AALS, and

[1] The ND-GAIN Country Index summarizes a country's vulnerability to climate change and other global challenges in combination with its readiness to improve resilience. It aims to help governments, businesses and communities better prioritize investments for a more efficient response to the immediate global challenges ahead. The higher the rank, the better.

[2] Mauritius, Saint Kitts and Nevis, or Saint Lucia rank 48, 58, 68, respectively, by the Notre Dame Global Adaptation Initiative.

[3] AAL correspond to the expected direct loss per year, averaged over 1980-2020. It covers flood, drought earthquake, and volcanic eruptions, considering only current climate patterns.

are based on current climate patterns. Two structural factors exacerbate the negative impacts of adverse natural events. First, lack of a disaster and climate informed urban development leading to a steady expansion of cities and physical assets into risk-prone areas causing an increased exposure of assets and people to adverse natural events. Second, the lack of copying capacity of vulnerable population, particularly those living in rural areas. Without adaptation efforts, negative impacts and losses are likely to worsen as climate change unfolds.

3. Climate change is expected to have a disproportionate impact on poor households in Cabo Verde due to their higher exposure to natural hazards and the vulnerability of their income. Remote sensing data and the 2015 Household Expenditure and Income Survey (IDRF-III) show that 67 percent of the population lives in an area that could be affected by high-damage pluvial floods. Income of poor households are associated to sectors that are highly affected by the impact of climate change increasing their vulnerability, such as agriculture. Climate change is expected to reduce crop and livestock yields and cause heat stress for workers who primarily work outdoors. These will have negative effects on labor productivity which may also reduce the wage bill for agricultural workers, leading to negative externalities that reduce local demand in rural economies, where 50 percent of poor households live.

4. Increasing the resilience of the existing growth model—and future nodes of growth—is thus crucial. Tourism is the driver of growth and will continue to be the mainstay of the economy – with the Tourism Operational Plan (2022-2026) outlining policies for a more diversified tourism offering.[4] Beyond tourism, as outlined in the second Strategic Plan for Sustainable Development 2022-2026 (PEDS II), the authorities are pursuing gradual economic diversification through investments in the ICT, energy, and blue economy (including fisheries) sectors.[5] Coastal areas—the backbone of the tourism sector and home to valuable fisheries ecosystems—are increasingly exposed to climate change. Equally important are the country's transport infrastructure, which play a vital role in supporting economic activity. While modelling estimates of the impact on climate change on growth are still underway, the economy's reliance on sectors vulnerable to climate change—and exposure of potential nodes of growth—suggests the negative impact on the economy and livelihoods could be significant, especially if adaptation measures are not quickly implemented.

B. Government Policies and Commitments in Terms of Climate Change Adaptation and Priority Areas to Strengthen Resilience

5. Cabo Verde demonstrates strong political commitment to sustainable and climate-resilient development, and has made considerable progress in outlying its priorities. The

[4] The Tourism Operational Plan (2022-2026) aims to catalyze more tourism flows to emerging islands and segments beyond the core sun & sea offering, notably hiking/nature and cultural niches.

[5] Interventions in the blue economy are guided by the National Investment Plan for the Blue Economy, which lists critical enabling investments to increase the sustainable economic contribution of fisheries and connected activities, with a specific nexus with tourism.

PEDS II, launched in May 2023, has a strong focus on climate through its pillar on decentralization, regional development, and territorial convergence, including environmental sustainability, climate resilience, biodiversity and geodiversity. In its Nationally Determined Contribution (NDC) of April 2021, the Government of Cabo Verde (GoCV) committed to achieving a decarbonized net-zero emissions economy by 2050. The island of Brava is expected to be a pilot and aims for decarbonization by 2040. It also committed to strengthening climate resilience in six priority sectors i) water; ii) agriculture; iii) oceans and coastal zones; iv) spatial planning; v) disaster risk reduction; and vi) health. In its National Climate Change Adaptation Plan (NCCAP) 2022-2030, the GoCV aims to (i) create an enabling environment to facilitate climate change adaptation mainstreaming in planning and budgeting processes, (ii) improve the capacity for data and information management and sharing, and access to technology and financing for adaptation, and (iii) implement adaptation action toward an increased resilience of the most vulnerable. The National Disaster Risk Reduction Strategy (ENDRR) 2018-2030 provides a framework for managing risks focusing on preventing disasters, minimizing damage and associated losses, and avoiding the creation of new risks. With the NDC, NCCAP and ENDRR the country has built the necessary framework for enabling resilience to disaster and climate shocks. The key challenge ahead is to mobilize the financing for implementing the critical measures and actions prioritized under these plans and commitments.

6. The Government envisions investing in agroforestry and pastoral resilience, with interventions in reforestation and the restoration of environmental ecosystems, prioritizing the mobilization of water associated with decentralized renewable energy solutions, while recognizing challenges imposed by the tourism sector. The GoCV aims to reduce dependency on rainfall (through the massification of sea water desalination) and strengthen the circular water economy (through the re-generation of used water) mainly for use in agriculture, to combat climatic adversities and thus create resilient structures. The rapid expansion of the tourism sector has taken a toll on the country's natural resources and marine biodiversity.[6]

7. Disaster Risk Management (DRM) and Adaptive Social Protection Programs are important tools to build a proactive approach to managing risks and potential impacts of disaster and climate shocks on population. The country has progressively moved from a DRM system originally focused on emergency preparedness and response activities towards a more comprehensive approach to disaster and climate-related risk management. These reforms have enhanced the institutional capacity to develop a risk-informed territorial and sectorial planning system with the objective of reducing existing risks and avoiding the creation of new ones. Likewise, the Ministry of Finance has taken a leading role to proactively increase its financial capacity to respond to disaster and climate-related shocks through the establishment of the National Emergency Fund (FNE) and strengthen its capacity to manage fiscal risks associated with disaster and climate-related shocks under its broader Fiscal Risk Management framework,

[6] Tourism is the backbone of Cabo Verde's economy, with the industry driving economic growth for the past three decades.

supported by the first and second DRM Development Policy Financing with a Catastrophe Deferred Drawdown Option (Cat DDO).

8. The nation heavily relies on its ocean resources, particularly in tourism and fisheries, with a significant portion of its population depending on these sectors for their livelihoods. While the tourism sector is the mainstay of Cabo Verde's economy, it's rapid expansion has taken a toll on the country's natural resources and marine biodiversity. Concentrated development has resulted in poor coastal management and increased pressure on the environment. Recognizing these challenges, the GoCV is now actively pursuing a more diversified, sustainable, inclusive, and resilient tourism model to reduce the negative impact on the environment while continuing to foster economic growth.

9. The fisheries sector plays a strategic role in Cabo Verde's economy. The sector is crucial for the country's exports, nutrition, and the socio-economic well-being of rural coastal fishing communities. Fish products account for over 60 percent of the nation's exports and are a dominant force in the manufacturing sector, contributing 9 percent of GDP in 2021. Fish also serves as a critical source of micronutrients and animal protein, second only to poultry. Furthermore, the fisheries sector has a substantial impact on coastal communities, particularly women, with 80 percent of fishers deriving their livelihoods from fishing, predominantly on the smaller and less affluent islands. Climate change and its associated impact on fish ecosystems pose a threat to fish stocks and challenge the long-term sustainability of the sector.

C. Government Policies and Commitments in Terms of Climate Change Mitigation and Priority Areas to Reduce Greenhouse Gas Emissions

10. While Cabo Verde already has one of the lowest GHG emissions per capita rates in the world, [7] it has made an ambitious commitment to climate action in its revised NDC. Most of the country's GHG emissions are generated by the energy sector, particularly the transport sector.[8] With growing demand for energy projected to reach approximately 364,000 toe by 2030, associated emissions are expected to increase from 223kt in 2019 to 500kt CO_2eq under a business-as-usual scenario. Cabo Verde is responding by aiming to reduce GHG emissions by 18 percent below the business-as-usual scenario, and by 24 percent with adequate international support, ultimately reaching the goal of a decarbonized net-zero emissions economy by 2050. The island of Brava is expected to be a pilot and aims for decarbonization by 2040. Mitigation efforts will focus on increasing renewable energy

[7] GHG emissions per capita in Cabo Verde showed a rate of just under 1tCO_2eq in 2010.

[8] The transport sector is expected to generate the highest emissions, averaging about 373 kt CO_2eq per year between 2020 and 2030.

generation, improving energy efficiency, shifting from fossil fuel-engineered to electrified transport, enhanced land restoration and blue carbon.[9]

11. The National Program for Sustainable Energy was launched within the framework of the country's first PEDS (2017-2021). It aims to accomplish the transition to a secure, efficient and sustainable energy sector, reducing dependence on fossil fuels and ensuring universal access and energy security. It focuses on five key areas: (i) institutional strengthening and improvement in business environment; (ii) energy market reform; (iii) investment in strategic infrastructure; (iv) renewable energy development; and (v) promotion of energy efficiency; and is underpinned by the Power Sector Master Plan (2018-2040) with the objective to have 54 percent of the country's power generation come from variable renewable energy (VRE) sources by 2030. Currently only 18 percent of power generation comes from VRE (31.5 MW out of a total current installed capacity of 176 MW). High off-taker risk, insufficient funding and incentives to attract the private sector, and renewable energy projects that are small in size are among the key challenges that impede the development of renewable energy at scale. The GoCV identified investments of €518 million for the period 2019-2030 for VRE integration, grid reinforcement and modernization, a risk mitigation facility, distributed generation, and e-mobility. The majority of new VRE capacity is expected to be financed by the private sector as independent power producers. De-risking investments and aggregation of smaller projects to attract private sector, investments in grid modernization and reinforcement, storage and ancillary services are hence critical for Cabo Verde's energy transition.

D. Other Challenges: Financing; Institutional Capacity; and Risk Management

12. Efforts are being made to mobilize financing, but the needs are large. Cabo Verde has been a pioneer in the region on a number of climate finance instruments such as blended financing loans, ESG bonds, blue bonds, sustainable bonds, debt for climate swap, and is considering carbon credit monetization structures as well as the establishment of a Climate Investment Fund.[10] In 2019–20, an average of US$21 million were invested in climate-related activities from public sectors, with a marginal contribution from the private sector (only about 2 percent). However, this is still insufficient, compared to the US$213 million needed per year, as defined by the latest NDC (around US$2 billion in the period 2020-2030). Given limited fiscal space and high level of public debt, public investment will need to be selective, with international funding and private sector participation becoming increasingly important. This said, enhancing the role of the private sector to boost investment requires alleviating key

[9] National Renewable Energy Plan, 2015.

[10] Country Focus Report 2023: Cabo Verde Mobilizing Private Sector Financing for Climate and Green Growth.

cross-cutting constraints: (i) transport and logistics (ii) energy, and (iii) business environment, including competition.[11]

13. Successful achievement of Cabo Verde's development and climate targets require strengthening institutional capacity and leveraging new sources of financing, particularly from the private sector. Cabo Verde made significant achievements in advancing a framework for Climate Finance, but its implementation has yet to fully materialize.[12] Moreover, high cost of capital due to perceived risk and high public debt, is a barrier for mobilizing private sector investments and reforms to address these will be key. Achieving Cabo Verde's development and climate ambitions may entail economic and social trade-offs. Mobilizing adequate private and public financing, as well as building local technical capacities and knowledge to manage a just transition can reduce trade-offs and maximize development outcomes.

14. The interplay between social exclusion and climate impact requires targeting the most vulnerable, mobilizing and enhancing household adaptive capacities, resilient systems, and livelihoods. The combination of exclusion and climate vulnerability exacerbates the social fabric, creating poverty cyclical traps, weakening social cohesion, and increasing social tensions and volatility. Greater investments in the country's human capital will be critical to build resiliency to climate change and preparedness of the population to adapt, address challenges as they arise and take opportunities from the transition. The creation of a culture of climate preparedness, especially through education reforms and specific training programs, would enhance national capacities for climate resilience. In order to raise a climate-conscious generation, it is critical to start early and instill values of shared responsibility and environmental stewardship. As Cabo Verde prepares a new strategy for its skills development sector, prioritizing programs that prepare workers for careers in adaptation and low-carbon technologies ("green jobs") presents an opportunity to boost its future competitiveness.

15. Adequate disaster and climate hazard and risk information play a critical role in decision making to effectively managing impacts of natural disasters and climate change. Having access to accurate and up-to-date information about potential hazards and risks allows decision-makers to make informed choices and take proactive measures to protect communities, infrastructure, and the environment. Not only targeted hazard and risk information allows decision-makers to prioritize and allocate resources effectively but by understanding the potential impacts and vulnerabilities associated with different hazards, they can identify areas and sectors that require immediate attention and investment. Access to comprehensive hazard and risk information enables decision-makers to develop long-term strategies for resilience and adaptation. This would be a crucial challenge for the country when moving towards a more climate resilience development and growth.

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[11] Country Private Sector Diagnostic for Cabo Verde (2023).

[12] Amongst others, the forthcoming Country Climate Diagnostic Report (CCDR) will look assess whether Cabo Verde has sufficiently conducive institutional and legal frameworks and capacity to address the transition to low-carbon and resilient development pathways.

E. World Bank Engagement in the Area of Climate Change

16. The World Bank's engagement in the area of climate change covers both financing and technical assistance. To date, the Bank has supported reforms to strengthen the institutional and legal frameworks to ensure risk-informed sectoral and territorial planning and increasing financial capacity to manage disaster and climate impacts.[13] The Bank is also supporting the authorities' ongoing efforts to enhance the resilience of public investments to climate change, which includes the incorporation of climate and disaster risk considerations in the evaluation of all new public investment projects.[14] At the sectoral level, the Bank is supporting reforms to enhance the climate resilience of key sectors, including energy, blue economy and transport.[15] The Bank is also involved in key climate related sectors The Bank also provided technical assistance to the GoV on the option for the creation of a nature and climate-dedicated fund, aimed to catalyze additional and longer-term and low-cost climate financing.

[13] This has been achieved through the engagement under the *Disaster Risk Management Policy Financing DPF with Cat DDO*, as well as the *Second Resilient and Equitable Recovery DPF,* which includes a Cat DDO that provides contingency funds in the event of a disaster.

[14] This is being supported through the ongoing *Fiscal Space and Sustainable Growth DPF series.*

[15] This includes project financing such as the *Renewable Energy and Improved Utility Performance* project - with focus on promoting on-grid solar PV - and the *Resilient Tourism and Blue Economy Development* project – to address vulnerability in the tourism, fisheries, and urban sectors.

Statement by Mr. Afonso Bevilaqua, Executive Director for Cabo Verde and Mr. Bruno Saraiva, Alternate Executive Director, and Mr. Pedro Miranda, Senior Advisor to the Executive Director
December 11, 2023

On behalf of our Cabo Verdean authorities, we thank Mr. Tyson and his team for the comprehensive report. The authorities appreciated staff's close engagement and candid policy dialogue, including through the ECF review mission in October-November. These discussions have continued the fruitful engagement of the Fund with the authorities, which has been enhanced by the presence of the newly installed IMF Resident Representative in Praia, Mr. Rodrigo Garcia-Verdu, who hit the ground running.

Recent economic developments and outlook

After the strong rebound in 2021-22, GDP growth continued at a robust pace into 2023 before decelerating, while inflation has receded faster than anticipated. In the first half of 2023, the year-on-year growth rate posted a strong 5.8 percent, but available indicators suggest that economic activity has moderated in the third quarter led by weaker domestic demand compared to previous quarter. Investment dropped substantially due to tighter financing conditions and high construction and production costs, while private consumption has decelerated due to the impact of inflation on real income. The external environment was also less benign in the third quarter, with growth slowing in major trading partners. Fiscal conditions tightened, with the primary balance posting a surplus of CVE 2.8 billion (1.1 percent of GDP) in the first half of the year, driven by robust growth in revenues. Inflation has fallen significantly to 2.6 percent in September (y-o-y), led by weaker demand and declining international energy and, to a lesser extent, food prices. In addition, underlying inflation (ex-food and energy) has converged to international levels. Preliminary data indicate an improvement in external accounts in the third quarter, with net international reserves (NIR) increasing by 13 million euros in the period.

The economic outlook remains positive, with growth converging to potential despite uncertainty and risks mainly associated to exogenous shocks. Effective macroeconomic management and progress in the reform agenda have created favorable conditions for a strong and sustainable pace of economic development. Moreover, the climate-related agenda presents opportunities to increase the rate of potential output growth. However, as a small, insular economy, Cabo Verde is vulnerable to external shocks, including those associated with climate change, and developments in key global economies.

Program performance

Ownership and resolve have underpinned remarkably strong program performance. All quantitative performance criteria (QPCs), indicative targets (ITs) and structural benchmarks (SBs) for this review have been met, some of which with very substantial margins. The overperformance in revenues and spending restraint led to a primary balance in the first half of the year almost CVE 3 billion above the program target. The strong fiscal performance continued in the third quarter, with the government posting an overall surplus of CVE 2.6 billion. The net international reserves floor was also exceeded by almost 10 percent. The combination of macroeconomic improvement and strong program performance attests to Cabo Verde's program as a successful example of good design, with focused conditionality that is based on the government's own plans and geared at measures that are critical to ensure the desired results. The request for the modification of PCs is purely technical and is supported by staff. Changing the PV of new external debt for end-December 2023 is needed to accommodate a new schedule of World Bank disbursements, while the modification on other net liabilities reflects the intrinsic uncertainty in privatization receipts. The disbursement released by this review will support the implementation of the government's policies and reform agenda under the Sustainable Development Strategic Plan 2022-2026 (PEDS II).

Fiscal and debt policies

Fiscal performance has surprised on the upside so far this year. Given the outstanding revenue performance, the central government has posted a significant primary surplus in the year to the third quarter. Fiscal revenues have continued to increase at a robust 2-digit pace (15.7 percent y-o-y) in the third quarter, while expenditure growth has been contained to 3.7 percent y-o-y. Even if some accommodation on revenue growth takes place in the remaining of the year, together with an improvement in budget execution, the primary balance will close the year stronger than initially anticipated, meeting the QPC by a wide margin.

The 2024 budget is in line with program commitments and will deliver the required primary result without compromising social and economic needs. Further spending rationalization, including by reducing subsidies and tax expenditures, will play an important role on the fiscal performance next year. The authorities are also confident that GDP growth and revenue collection will underpin better than anticipated results in the 2024 budget. Moreover, resources are being committed to support coordinated action to meet the goal of eradicating extreme poverty by 2026. Concessional resources will support critical investment in infrastructure and human capital to bring the Cabo Verdean economy to a new stage of sustainable, equitable, digital development. Aware of the risks entailed by SOEs, the authorities are fully committed to accelerate reforms leading to a more streamlined and efficient SOE sector. They are also proceeding with enhancing monitoring and assessment of SOE performance with integrated digital platforms, which will enable data-driven management of these enterprises, reducing the risk of recurring losses. Completing the reorganization of Air Cabo Verde (TACV) and resuming its privatization is a key goal.

Sustained consolidation will keep public debt on a downward path. Debt reached almost 145 percent of GDP in 2021 and is set to fall below 120 percent this year, due to consistent efforts to increase primary surpluses without compromising GDP growth. In addition, other avenues to reduce the debt burden are being pursued and the authorities have reached an agreement in principle with Portugal to explore the possibility of debt-for-nature swaps. The goal for the next four years is to reach a debt to GDP ratio of under 100 percent and to continue on a downward path until a more sustainable level is attained. Fiscal overperformance in 2023 and consistent implementation of the reform agenda augur well for meeting these targets ahead of schedule.

<u>Monetary and financial policies</u>

The Bank of Cabo Verde (BCV) has acted to protect the peg, strengthen monetary policy transmission, and ensure financial sector stability. Interest rates have been raised this year to narrow the differential with respect to the ECB. The BCV will follow developments in the euro area closely and adjust its stance accordingly to avoid undue pressure on international reserves. Reserves are currently above the target range of 5½ to 6 months of projected imports. The authorities are strengthening monetary policy transmission by pre-announcing a schedule for bond auctions and enhancing statistical and analytical capabilities, including for macroeconomic forecasts.

Cabo Verde’s financial sector has shown resilience and remains stable, adequately capitalized, and liquid. The authorities have concluded a comprehensive study of loan losses and provisions at the expiration of the credit moratorium and found that the banking system is well placed to withstand it. Further work is underway to enhance NPL monitoring procedures and support the resolution of crisis related NPLs. Revamped stress tests will be applied twice a year, contributing to increasing financial system resilience. Additionally, the authorities intend to develop a national fintech strategy, with support from the World Bank, to establish the pillars for financial technologies that embrace innovation, foster competition and lower financial transaction costs. Furthermore, draft legislation on amending the BCV Organic Law in line with IMF safeguards assessment recommendations, aiming at enhancing central bank independence, accountability, and transparency, will be submitted by mid-next year to the National Assembly.

Reform Agenda and RSF Request

Cabo Verde is one of the most vulnerable countries in the world to climate change, despite being one the lowest per capita GHG emitter. Structural features of Cabo Verde's insular economy, including territorial discontinuity, eco-system fragility, and scarcity of potable water and arable land, add to vulnerability and developmental challenges. This is exacerbated by dependence on food and energy imports. Recently, five years of drought have led to significant drops in food production and losses of grazing land, the effects of which were magnified by the economic fallout from the pandemic and the ripple effects from the war in Ukraine, resulting in 10 percent of Cabo Verdean population facing acute food insecurity. The poorest households are the most vulnerable to climate change hazards such as desertification, erosion, and floods. Slow-onset sea level rise and biodiversity loss pose an existential threat to the archipelago and require immediate action and planning.

Transitioning to a green, circular economy presents an opportunity for Cabo Verde. While the current energy-water-climate nexus is a drag to Cabo Verde's development, coping with it by transforming the economy on sustainable grounds offers a critical opportunity for the country. Moving to an energy matrix based on renewable sources (solar and wind) will address the vulnerability stemming from reliance on imported fuel and also allow for extensive water desalination, which will reduce vulnerability in food production. Water reuse will also be a critical piece of this transformed economy. Ultimately, even without being the focus of Cabo Verde's climate action, mitigation will be a result of the transition efforts being envisaged.

The RSF will leverage private and other partners' resources and support a comprehensive reform agenda. The climate agenda is the core of Cabo Verde's reform program. The RSF will cover five main reform areas, namely, (i) governance of climate change policy, (ii) fiscal risk and climate-resilient public investment frameworks; (iii) policies to foster energy efficiency and transition; (iv) long-term planning for water resources and climate impacts; and (v) financial sector resilience to climate change. This reform agenda is guided by important IMF and World Bank diagnostics including the C-PIMA and the CCPA and is in line with Cabo Verde's Sustainable Development Strategy 2022-2026 (PEDS II). Despite the comprehensiveness of the reform agenda, the focus is on measures that are critical to address the main developmental challenges of Cabo Verde. Indeed, many of the actions to promote these reforms are already in the pipeline and will be supported by other development partners, such as the World Bank, the AfDB and bilateral agencies.

Concluding remarks

Cabo Verde has benefitted from consistent engagement with the Fund over the past few years. First under the PCI and now under this ECF arrangement, Cabo Verde's macroeconomic stabilization and reform efforts have been supported by candid and fruitful policy dialogue with Fund staff. The authorities' steadfast commitment and high ownership of policies and reforms underpin the strong performance of Cabo Verde under these IMF arrangements, even when facing extremely adverse circumstances. Despite the auspicious economic performance, there is more to be done, and the reform agenda entailed by the ECF is now being joined by a comprehensive, but critical, reform agenda to cope with the challenges posed by climate change. These are complementary efforts, and the authorities count on the continued support of the Fund in order to achieve these key strategic goals.