

Cape Verde: Selected Issues and Statistical Appendix

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CAPE VERDE

Selected Issues and Statistical Appendix

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Approved by the African Department

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Contents	Page
Determinants of Emigrant Deposits in Cape Verde.....	3
I. Introduction.....	3
II. Evidence on Emigrant Deposits.....	4
A. Evolution and Structure of Emigrant Deposits	4
B. Determinants of Emigrant Deposits.....	7
C. Impact of Migration on Emigrant Deposits	9
III. Data and Methodology.....	10
IV. Empirical Findings.....	12
V. Conclusions and Policy Implications.....	13
Appendix	15
References	26
Financial Sector: Institutions, Oversight, Risks, and Vulnerabilities	27
I. Introduction.....	27
II. Overview of the Financial Sector	29
III. Market Infrastructure and Intermediation Spreads	31
IV. Regulation and Supervision	35
V. Safety Nets.....	35
VI. Macroeconomic Risks and Vulnerabilities	35
VII. Enhancing Efficiency of the Financial System.....	39
VIII. Challenges Ahead	40

Contents	Page
IX. Conclusions.....	42
Appendix	43
References	46
Statistical Appendix Tables	
1. Selected Economic and Financial Indicators, 1999–2003	47
2. Selected Social and Demographic Indicators, 1999–2003	48
3. Sources and Uses of Resources, 1999–2003.....	49
4. Gross Domestic Product at Current Prices, 1999–2003.....	51
5. Gross Domestic Product by Major Sector at Constant 1980 Prices, 1999–2003.....	52
6. Consumer Prices, 1999–2003	53
7. Fiscal Operations of the Central Government, 1999–2003	54
8. Central Government Revenue, 1999–2003.....	56
9. Selected Indicators of Central Government Revenue, 1999–2003	57
10. Economic Classification of Central Government Expenditure, 1999–2003.....	58
11. Public Domestic Debt of Central Government, 1999–2003	59
12. Monetary Survey, 1999–2003.....	60
13. Summary Accounts of the Bank of Cape Verde, 1999–2003.....	61
14. Summary Accounts of the Commercial Banks, 1999–2003.....	62
15. Interest Rate Structure, 1999–2003.....	63
16. Balance of Payments, 1999–2003.....	64
17. Merchandise Exports, 1999–2003	65
18. Merchandise Imports, c.i.f., 1999–2003	66
19. International Trade in Services, 1999–2003	67
20. Direction of Trade, 1999–2003.....	68
21. External Trade with CEDEAO Countries, 1999–2003.....	69
22. Factor Income, 1999–2003	70
23. Private and Public Transfers, 1999–2003	70
24. External Public Debt Outstanding, 1999–2003	71
25. Summary of the Tax System	72

DETERMINANTS OF EMIGRANT DEPOSITS IN CAPE VERDE¹

I. INTRODUCTION

1. Over the last decade, emigrant deposits (ED) have provided a substantial source of foreign exchange to the Cape Verdean economy and have been vital in maintaining the fixed exchange rate. In light of the difficulties in accumulating reserves, stemming from a high dependency on imports and a narrow export base, understanding the long run determinants of ED is essential to reserve sustainability and is a prerequisite for efficient reserve management.
2. Along with a number of countries with fixed exchange rate systems and massive development needs, Cape Verde faces today an important policy dilemma: while fostering private initiative to spur growth implies the need for significantly lower interest rates, reserve accumulation essential to maintaining investors' confidence requires keeping interest rates high and credit growth strictly in check.
3. In this already fragile framework, the need to increase fiscal expenditure to meet Millennium Development Goals exacerbates the "impossible trinity," leading to higher dependency on foreign aid. However, with the anticipated graduation of Cape Verde from the LDC group, the country may experience increasing difficulty over time in obtaining international aid at concessional terms.
4. Since the sustained suppression of demand to address balance of payments needs is not a long term policy option, and the domestic resources necessary to spur growth are not sufficient, further accumulation of reserves will continue to rely on emigrants savings. How these saving are to be channeled into the country will depend on the understanding of the forces that have driven ED in the past.
5. The paper studies the long run determinants of ED with respect to risk, wealth and return variables. It draws partly on previous research on remittances published in the 1996 IMF Recent Economic Developments paper (RED), but focuses on the subsequent decade and partly on the research on emigrant deposits (Gordon and Gupta, 2004). In addition to the variables treated in the RED, this study encompasses risk indicators for domestic institutional events (such as change in the government and introduction of the foreign exchange law) and major economic episodes at home (devaluation fears, slippages in the fiscal policy) as well as events in the host countries (introduction of the euro, September 11). Return variables considered include interest rates in the host and the home country and stock market returns in the host country.

¹ Prepared by Ms. Izabela Karpowicz.

6. The empirical evidence suggests that the long-run determinants of ED in Cape Verde are country specific, reflecting the different rationale of flows generated by temporary versus permanent migrants.

7. The paper is organized as follows: Section II describes the evolution of ED, from the reform introduced in 1995 until recently; Section III presents the data set and the methodological approach to estimation of determinants of ED; Section IV reports results from the econometric estimation; and Section V concludes.

II. EVIDENCE ON EMIGRANT DEPOSITS

A. Evolution and Structure of Emigrant Deposits

8. While a great deal of literature has focused on short-term capital flows and on remittances, very few studies have concentrated specifically on determinants of ED and their impact on recipient countries. This topic is however of extreme importance in Cape Verde, where deposits flows not only provide a large source of foreign currency and potential investment capital, but also, being partly co-owned by residents, represent a domestic liability. As such, ED represent a double vulnerability for the country, having the potential to influence banking system stability as well as the exchange rate policy.

9. A large part of remittances arrives in the country through the banking system, a result in part of the preferential treatment and tax incentives conceded to these deposits until recently, and also reflecting the fact that Cape Verde has a healthy banking system that is free of political interference.² The stock of ED represents that part of remittance inflows arriving through the banking system that are kept in special deposits regulated by the law. With gross remittance flows accounting for 20 percent of GDP in 2004, the net accumulation of ED was almost 4 percent of GDP.

10. As a result of the cumulative buildup of ED in Cape Verde, these deposits represent a considerable share of banking system liabilities, accounting for 40 percent of broad money in

² Flows arriving to rural areas with limited access to banks, are not captured by ED. Their size is not known but it is likely to be rather small. This is quite an unfortunate circumstance, common to poor areas of most developing countries that are recipients of large remittance flows. While poverty is the major driving force of migration, which is a prerequisite for remitting, extreme poverty is also the greatest deterrent. In fact, the poorest strata of the society are most often cut out of remittance flows due to the fact that they do not dispose of the minimal financial wealth that would allow them or their relatives to emigrate. Moreover, where initial wealth is not a problem, the tightening of opportunities for migration (in particular in the US and the EU in the last quarter of the century) usually is. In a recent paper on migration in Cape Verde, (Carling, 2004) describes the Schengen visitors' visa application process. Visas are issued restrictively with the aim of identifying potential overstayers. Carling shows that the socio-professional situation criteria for obtaining a visa brings about a social stratification of migration where the profile of a migrant worker tends to be that of an individual who disposes of some initial wealth, a permanent occupation, some education and most likely relatives abroad. Thus, although more than half of the population in Cape Verde receives some kind of remittances, only a small minority of transfers reaches the poor. (The World Bank Report, June 2004, ch. 4 discussion draft)

2004. Their contribution to M2 growth increased from slightly over 2 percent on average in 1996 to over 7 percent in 2002 but has been on a downward trend since then (see Table 1).³

11. The level of ED decreased substantially only in the period that preceded the introduction of the peg to the Portuguese escudo in June 1998, which fuelled fears of devaluation for several months.⁴ The annual growth rate since then has averaged over 20 percent, reaching a peak in June 2003 and accounting for 73 million U.S. dollars or 5 percent of GDP. Since then the accumulation rate has slightly decreased, and was 15 percent in 2004.

Regarding the composition of ED, the share of time deposits in the total has averaged over 80 percent throughout the 1990s, while demand and foreign exchange deposits constituted less than 20 percent of the total, with the latter amounting to less than 4 percent of the total at end-2004 (see Figure 1 and Table 1).

Table 1. Cape Verde: Emigrant Deposits Indicators, 1995–2004

Year 1/	Composition of ED			Share of ED in M2		Contribution to M2 growth		Interest rate spread on deposits 3/		Volatility of ED flows 4/	
	Demand	Time	Forex	Total	Escudo 2/	M2	ED	EU	US	Mean	Stdev
1995	6.1	77.3	16.6	21.0	17.6	n.a.	n.a.	4.0	3.3	n.a.	n.a.
1996	5.6	81.7	12.7	23.3	20.3	12.3	5.0	5.4	3.5	105.0	401.2
1997	9.9	90.1	0.0	23.5	23.5	10.3	2.6	5.5	3.1	61.7	130.3
1998	9.3	79.3	11.4	25.1	22.2	2.5	2.2	6.0	3.6	57.0	95.0
1999	10.5	79.5	10.0	27.2	24.5	15.4	6.4	6.1	2.6	170.3	104.0
2000	11.1	80.3	8.6	29.9	27.3	12.9	6.5	3.7	1.2	201.4	85.5
2001	11.3	81.3	7.4	34.0	31.5	9.8	7.5	6.4	7.5	259.0	110.8
2002	11.2	83.1	5.7	36.4	34.3	14.3	7.5	5.7	7.1	288.1	113.7
2003	9.9	85.4	4.7	38.9	37.1	8.6	5.9	5.1	5.7	259.3	128.2
2004	10.3	85.8	3.9	39.9	38.4	10.5	5.2	5.0	4.2	244.9	109.5

Sources: Banco de Cabo Verde; and IFS.

1/ End of year data.

2/ Demand and time deposits.

3/ Nominal interest rates in escudo terms, EU deposit rate and US CD (3 and 6 months average).

4/ Annual net flows in millions of escudos.

12. The reason for such a structure, as well as the stability of domestic ED flows, can be traced back to the preferential treatment of time deposits conferred by the decree-law of September 1995 (Law). The Law reformed the existing special emigrants' deposits

³ As a share of imports of goods and services ED have grown from 20 percent to over 40 percent over the last decade and have been consistently above 200 in percent of gross international reserves (Figure 3). The sharp decrease in the ratio in December 1999 stems from a significant inflow of FDI related to privatization and large disbursement of bilateral and multilateral credits that led to strong accumulation of reserves of more than two months of imports of goods and services.

⁴ Devaluation fears spread from the last quarter of 1997 throughout the first half of 1998. The currency of Cape Verde, the Cape Verde escudo, was pegged to the Portuguese escudo from mid-1998 to end-1998. From January 4, 1994 it has been pegged to the euro at a rate of CVEsc 110.27 per EUR 1.

established by the Decree No. 51/84 of June 9, 1984 with the purpose of attracting additional emigrants savings and channeling them into investments. In view of that, three types of deposits were established: “emigrant deposits in foreign currency,” “emigrant savings deposits” and “emigrant deposits in escudos.”

13. The first type of deposits can be denominated in any of the 4 currencies specified in a notice issued by the BCV.⁵ The interest rate applied to these deposits is only slightly above the market rate. Thus the share of foreign currency deposits in total ED has been small since their institution, and has declined throughout the years to account for less than 4 percent in 2004.

14. Emigrant savings deposits are intended to finance investment in industry, tourism, transportation, agriculture and fisheries, as well the construction, acquisition and improvement of residential or rural property. These deposits, with maturity of six months and one year, are denominated in escudos and allow owners to borrow up to twice the amount of the deposit. Tax incentives are granted by the Law to their holders.

15. The third type of deposits, the emigrant deposits in escudos, focus on attracting foreign currency, which accrues to the central bank after conversion into escudos.⁶ They can be co-owned by residents and have been particularly attractive due to the high interest rate spread with deposits in the euro area and in the United States. In the past, the government offered a 1 percent interest rate subsidy on these deposits. Due to its excessive fiscal cost, however, which reached 0.2 percent of GDP, this subsidy was eliminated in November 2003.⁷

16. Hence, while foreign exchange deposits do not bear an implicit exchange rate risk, deposits in escudos have proved more attractive to emigrants—reflecting their relatively high return (with the implied exchange rate risk) compared with U.S. or euro deposits.⁸

17. Nominal and real interest rate spreads with euro area deposit rates, which have helped sustain ED flows, have been stable throughout 1995–2004, apart from some fluctuation in 2000 (Table 1 and Figure 4). Interest rate differentials with US certificates of deposit (CDs) have been more volatile, reflecting in particular a decrease in US interest rates in recent years.

⁵ U.S. dollar, French franc, German mark, and Dutch guilder.

⁶ The foreign exchange accrues to the commercial bank that holds the account. However, due to domestic liquidity requirements, the local commercial bank often sells the foreign exchange to the BCV.

⁷ The Decree Law 45/2003 repealed the Ministerial Order 63/95, which granted 1 percent annual bonus to ED. Commercial banks withdrew the bonus as from the renewal date of domestic currency ED. However, they continued to pay higher interest on ED than on residents' deposits.

⁸ Convertibility of time and demand deposits back into foreign currency is not guaranteed and has to be approved by the BCV. However, the few attempted conversions in the past have all been performed.

18. The growth of ED net flows in escudo terms has been stable over the period under consideration. Time deposits are the most volatile in terms of standard deviation. However, their mean is also the largest and thus the coefficient of variation is the smallest. The coefficient of variation for total deposits has been consistently around 0.5 percent from 1999 until recently.

19. ED net flows display some seasonality. However, seasonality seems to be significant only for the month of December once values for the period with devaluation fears are excluded, which may be an indication of a “Christmas effect” in ED flows.⁹

20. At first glance, political and economic events in the country and abroad seem to have very little impact on ED flows. Table 2 shows average net flows in the periods when deposits are expected to be under stress. Apart from the period characterized by devaluation fears that preceded the change in the exchange rate peg, average monthly flows have been quite stable in spite of the introduction of the Euro, September 11 and the slippage in fiscal policy.¹⁰

B. Determinants of Emigrant Deposits¹¹

21. There are reasons to believe that ED and their uses are comparable in some respects both to short-term capital flows, which are typically speculative in nature, and to remittances based on altruistic considerations (Reinhart et al., 2003). If the rationale behind ED is closer to the one of speculation, or more generally self-interest, then ED would be expected to increase with the widening of real interest rate differentials between the home and the migrants’ host countries, and decrease in case of economic or political instability at home. To the extent that ED are driven by altruistic considerations, one would expect them to increase when the economic situation in the home country worsens and/or the economic situation in the host country improves.

22. The distinction between the underlying motivations for saving and remitting is essential since the effect the flows have on capital accumulation may differ accordingly. Generally, flows motivated by altruism are more likely to be spent on consumption whereas flows supported by self-interest are converted by the banking system into investment credit.

23. The use of ED is not tracked, but evidence from recent studies on remittances (Bourdet, 2003, World Bank 2004, Carling 2004) suggests that these flows are mostly used

⁹ In order to check for seasonality, a simple regression is performed of net ED flows on three dummies, which take the value of 1 in the month of May, September, and in the month of December, respectively, when average ED flows appear to be higher.

¹⁰ The outflow in the month corresponding to the introduction of the new foreign exchange law overlaps with devaluation fears.

¹¹ Potential, long run determinants of ED are depicted in Figure 4.

for residential construction and for education.¹² Given the incentives to ED granted by law, as mentioned above, it is likely that ED are used in the same way (which makes it difficult to separate the forces behind them).

24. Altruism seems to have driven remittances in the period following the independence of Cape Verde in 1975 until 1985 when ED were instituted. That period was characterized by high inflation and negative real interest rates, which could not have supported the self-interest hypothesis.¹³ In contrast, the period from the mid-80s to the mid-90s was characterized by positive interest rates, remarkable real GDP per capita growth and exchange rate stability, which would suggest a lower need for transfers based primarily on altruism.¹⁴

25. The substantial increase in growth of ED in the second half of the 1990s, in particular from 1998 on, should be at least partly explained by the shift from the exchange rate system based on a target of a broad basket of currencies to the peg with the Portuguese escudo and later to the euro, which provided more stability and credibility in the system. In addition, the relaxation of exchange controls on the purchase and sale of foreign currencies might be another measure that positively affected ED, sharply reducing the need for a black market for financial transactions and shifting the ED flows from informal to formal channels. However, high interest rate differentials in favor of Cape Verde and the interest rate subsidy conceded by the Treasury might have been the main policies responsible for the surge in ED.

26. Aside from the variables determined by policies at home, international developments beyond the control of Cape Verdean authorities also have the potential to influence ED. Undoubtedly, real GDP growth in host countries is one of them, with higher productivity and real wages of emigrants boosting ED via the wealth effect. Conversely, changes in policies abroad are capable of influencing those flows that are generally driven by self-interest. In addition, positive developments in foreign stock markets can provide an attractive alternative investment outlet, and hence may divert ED away from Cape Verde.

27. The recent slow down in the accumulation of emigrant deposits could be at least partly explained by the weaker performance of labor market indicators in the host countries as well as by the depreciation of the U.S. dollar, which contributed to lower inflows from the diaspora in the United States. The recent decrease in domestic interest rates conceded to ED

¹² In particular Bourdet (2003) reports that half of the credits is granted to individuals for residential construction and thus has limited impact on capital accumulation.

¹³ As documented by the RED, only flows from Portugal, and to a small extent from Netherlands, decreased sharply in that period until interest rate parity was restored.

¹⁴ Although the RED reveals the role of income differentials as determinants of remittances, it fails to detect the significance of interest rate differentials in the analyses, possibly due to a structural break introduced in the series by the introduction of the high interest rate policy which is unaccounted for in the estimation.

should not have contributed substantially to a decrease in the accumulation thanks to the still high spreads with euro area and United States deposit rates.

C. Impact of Migration on Emigrant Deposits

28. The evolution of ED is likely to be determined by opportunities at home and prospects for migration. Thus, the size of the diaspora and the pattern of migration across time, but also the status of emigrants abroad and their identification with the home country, will potentially influence ED.

29. The initial conditions in favor of migration in any country may well be easy to define. Some of them include the menace of war, the proximity to the host country, the capacity to borrow for the trip or the presence of relatives abroad who can provide help, the level of development at home, and job prospects. The freedom of movement, however, as defined by legislation in the host country, is the chief force able to deter or encourage migration.

30. Aspects of migration that determine remittances and thus ED are in turn much more complex and dynamic in nature. The gender composition of migration may determine the size of remittances, although its overall impact is the result of opposite forces and thus difficult to predict. While men who emigrate alone are likely to send money to wives and children at home, the recent feminization of migration, documented by Carling (2004),¹⁵ has been found to increase flows. In fact, women are believed to be more likely to remit even though they often earn less.

31. The decision to return, which distinguishes permanent from temporary emigrants, is one aspect of transnationalism influencing remittances which characterizes ties to the home country. First generation migrants are those who maintain strong identification with the home country and see themselves as temporary emigrants. These individuals are believed to be more likely to remit and save at home (RED). Nevertheless, the decision to return and/or remit changes through time, depending on the accomplishments of the migrant (that is, securing a pension or a large inheritance) as well as on the restrictiveness of migration laws.¹⁶ Finally, strong national identification can yet be abstract and symbolic, with no concrete ties and no determination to remit or invest.

32. Cape Verdean emigration to the United States began in the early 20th century, but slowed in the 1990s when the U.S. introduced immigration quotas. Cape Verdeans emigrated

¹⁵ While Cape Verdean emigration was heavily male dominated in the early years, the proportion of women increased significantly in the 1960s and 1970s and continued to be high in the 1990s.

¹⁶ Exchange rate stability and the enhanced convertibility of ED is a new situation characteristic of the late 1990s that potentially blurs the distinction between permanent and temporary migrants inclination to remit as assumed in the RED paper. The latter paper presupposes that permanent migrants are not willing to bear the sunk cost stemming from the non-convertibility of ED back into original currency, thus choosing to save exclusively abroad.

to Portugal, West Africa and South America in the 1940s, while emigration to the north, in particular to Western Europe, occurred in the 1960s and culminated in the period around independence in 1975. Since then, the destination of the majority of Cape Verdean emigrants has been Europe (Carling, 2004).

33. Despite the lack of reliable statistics on migration, the Cape Verdean population abroad is believed to exceed the number of nationals at home, with most emigrants residing in the U.S. However, these emigrants are the 4th generation of Cape Verdean in the U.S. and see themselves already as permanent residents and thus not returning home. Consequently, they save less in Cape Verde than more recent emigrants to other countries, even though they may be richer (see also RED). Thus, at present, Cape Verdeans in Europe, who account for only a third of the total diaspora, account for more than half of all remittances (World Bank, 2004).

III. DATA AND METHODOLOGY

34. Following the discussion above, indicators of both altruistic and self-interested motivations are incorporated in the analyses of long-run determinants of ED. The selected data set covers monthly indicators for the period December 1995–December 2004. The dependent variable LDEP is the logarithm of the end of month stock of time, demand and foreign currency deposits in domestic currency provided by the central bank (Banco de Cabo Verde, BCV).

35. Among the explanatory variables are interest rates on ED in Cape Verde, as well as interest rates on United States certificates of deposit and Euro Area deposits. Rather than looking at the real interest rate differential as the determinant of portfolio choices, the analysis considers nominal interest rates, inflation at home and abroad, and the escudo/U.S. dollar exchange rate. Other explanatory variables include wages in the U.S. and the Euro Area as a proxy for the wealth effect and the stock market index, which should capture the portfolio adjustment effect.

36. In contrast with the RED study, this paper introduces several dummies in the estimation in order to capture the effect of September 11, the introduction of the euro (which forced individuals without bank deposits to convert savings held in notes from euro-zone countries to euros), the introduction of the foreign exchange law and the change in exchange rate peg, as well as the fiscal policy slippage that preceded the 2001 election.¹⁷

37. In order to capture the wealth effect for Cape Verde residents, a variable such as GDP per capita or index of industrial production should be included. A negative sign associated with this indicator would support the altruistic assumption. However, such data are not

¹⁷ This tests the possibility that increases in fiscal spending might have deterred both altruistic driven flows, by signaling to emigrants the lowering of needs of Cape Verdean residents, as well as speculative flows, by raising concerns about the sustainability of the exchange rate peg due to the decrease in the level of reserves.

available at high frequency in Cape Verde and could not reasonably be included in the estimation. Nevertheless, a simple plot of annual real GDP growth and ED flows shows a negative lagged correlation between these two variables in the period 1996–2004, suggesting that a decrease in GDP induces altruistic flows into the country.¹⁸

38. In addition, the change in the composition of migration, which has characterized the recent period, could be one of the reasons for the change in the level of deposits.¹⁹ This could not be accounted for in the estimation, however, as detailed data on the break down of deposits by currency and on migration are unavailable.²⁰ As a matter of fact, foreign exchange inflows are converted by the BCV into national currency before being deposited into emigrant deposits, and the original currency composition is not published. Building this information from migration flows would not be advisable, due to the possible inverse relationship between the size of the emigrant community and quantity of remittances as noted above. Data sources and a detailed description of variables can be found in Table 2.

39. The regression analysis draws on the framework of Gordon and Gupta (2004) and can be represented as follows:

$$LDEP_t = c + \alpha Int_t + \sum \beta_i X_{it} + \varepsilon_t, \quad \varepsilon \sim N(0, \sigma^2) \quad t = (1, 2, \dots, T)$$

where LDEP is the logarithm of deposits,²¹ Int is the interest rate on deposits and X is the vector of non interest variables (inflation, stock market index, wages, seasonal and functional dummies). Two separate estimations are carried out, one for the variables pertaining to the Euro Area and one for the United States, the area where most of remittances originate. While various specifications have been attempted, including the one with Euro Area and United States variables together, this approach was deemed more appropriate due to the fact that differences between permanent vs. temporary migrants are at the center of the analysis.

¹⁸ The correlation coefficient is -0.4.

¹⁹ Caused by the change in the euro-dollar exchange rate.

²⁰ The U.S. Bureau of Statistics and the OECD both record inward migration. However, their methodologies differ substantially (Adams, 2003).

²¹ Logarithms are used in order to interpret the coefficients from the estimation as elasticities.

IV. EMPIRICAL FINDINGS

40. Cointegration analysis appears to be the most appropriate technique for the study as all variables are integrated of order (1) according to the ADF statistic presented in Table 4. Misspecification tests are presented in Table 5.²²

41. The cointegration tests presented in Table 6 for both the Euro Area and the United States specifications indicate the presence of two cointegrating vectors at a 1 percent significance level. Together with the Granger-causality tests reported in Table 7,²³ these findings suggest the existence of two long-run relationships:

- The functional form of the long-run behavior of ED.
- The relationship among variables of the areas where ED originate.

42. Restrictions imposed correctly identify the two cointegrating vectors and the LR test does not reject over identifying restrictions. The long run relationship between ED and the explanatory variables is depicted in Tables 8 and 9. In both specifications, one cointegrating vector represents the functional form of the behavior of ED while the other contains only variables pertaining to the Euro Area or the United States. The coefficients in the two cointegrating vectors are significant, but do not all bear the expected signs.

43. On the *altruistic* side, the estimation based on the Euro Area variables shows a positive long-run relationship between ED and wages in the Euro Area, which supports the altruistic hypothesis discussed above and found in RED on remittances. This finding is in line with our expectations regarding the temporary character of Cape Verdean emigrants in Europe and their stronger ties with the home country. In contrast, wage increases in the United States do not have a positive impact on ED, possibly reflecting a negative wealth effect from emigrants who increasingly see themselves as permanent diaspora.

44. *Speculative* variables show contradictory signs on the nature of ED across the two samples.

- **Euro Area:** consistent with the speculative motive, an increase in the stock market index (representing an alternative investment opportunity) decreases ED, and an increase in the CPI (which widens real interest rate spreads) boosts ED. Unexpectedly, however, a rise in European Union deposit rates increases ED.

²² Normality tests for the two specifications indicate that the hypothesis of normality of the residuals is rejected. However, Paruolo (1997) shows that in instances where normality is rejected due to excess kurtosis rather than skewness, as in the present case, the Johansen cointegration results are not affected.

²³ As would be expected, the Granger-causality tests indicate that inflation, interest rates and ED in Cape Verde do not influence any variable of the Euro Area and the United States. On the other hand, inflation, wages, the stock market index and the exchange rate in the United States Granger-cause interest rates in the United States. Similarly, albeit to a weaker extent, Granger-causality is detected among Euro Area variables.

- **United States:** as expected, ED is boosted by a depreciation of the escudo, an increase in the U.S. CPI, and a decrease in the U.S. interest rates. However, an increase in the stock market index appears, unexpectedly, to increase ED.

Most interestingly, the interest rate applied to ED in Cape Verde does not appear to be significantly related to the accumulation of ED in the Euro Area estimate while, in the United States estimate, this interest rate appears to have an unexpected negative effect.

45. The short run effects are mostly insignificant across the estimates. Only the term representing the announced change in exchange rate policy (the devaluation dummy) is found to be significant, and bears the expected negative sign.

V. CONCLUSIONS AND POLICY IMPLICATIONS

46. The empirical findings have to be interpreted with extreme caution, as indicated by the mixed results reported above and by underlying limitations in the data (with ED measured from changes in end of period stocks, which include capitalized interest). However, the analysis suggests the following qualitative interpretation.

47. With regard to the speculative motive for holding ED, four risks to the future accumulation of ED can be identified:

- An increase in interest rates in the Euro Area and the United States, which reduces spreads with ED rates in Cape Verde;
- A decrease in interest rates on ED (which, while possibly lowering ED, may be needed to support stronger growth of credit to the private sector);
- Sluggish growth in host countries, which could lower the accumulation of wealth and leave less room for savings and investment;
- Exchange rate credibility, reflected in Cape Verde's capacity to generate foreign exchange reserves.

48. The first three events are already taking place and could be partly indicative of the recent slow down in the rate of accumulation of ED. On the other hand, exchange rate credibility appears to be high. This strength needs to be maintained, given that the one and only episode of massive withdrawal of ED in the past was associated with devaluation fears.

49. Risks associated with the altruistic motive could arise from the following:

- An increase in the restrictiveness of immigration laws in Europe and the United States;
- An increase in per capita income in Cape Verde and the country's move to middle income status;

- A decline in the relative wealth of emigrants—stemming, for example, from wage or exchange rate changes.

50. The future evolution of ED should closely reflect the pattern of migration flows, determined by conditions at home and legislation in host countries, as well as by changes in the status of emigrants (temporary migration turning to permanent). Prospects for growth in Cape Verde are improving and immigration legislation abroad is tightening. Both trends argue against further accumulation of ED. However, the composition of migration—shifting toward an increasing share of women—should support an increase in flows based on altruism. Moreover, a potential decrease in flows might be delayed by some years due to the fact that some emigrants are returning home and are sending more money to Cape Verde in view of their imminent retirement.

51. Among the developments in favor of ED, of considerable importance is their past stability, the limited convertibility of deposits, the favorable business outlook, and the stable political climate. While, for reasons mentioned above, ongoing reliance on ED should be viewed with caution, the persistent accumulation of ED through numerous adverse events in the past suggests that robust inflows will likely continue into the future.

52. Notwithstanding data limitations, the empirical estimates suggest that emigrants residing in the Euro Area behave in an altruistic manner, while the flows generating in the United States are driven more by self-interest. If the speculative aspect of ED is to continue in the future, including from Europe as migrants there gradually become permanent, the economy's ability to attract such flows, while also achieving the desired reduction in domestic interest rates spreads, will depend on the effectiveness with which ED are channeled into productive uses and hence generate adequate returns. In this context, progress with structural reforms and macroeconomic policies directed at ensuring economic confidence will be of primary importance. Such measures are also desired both to underpin the employment growth that will be needed to offset the effects of slower migration, and to support diversification of the economy into a wider range of export-oriented activities. Over the longer term, the latter will be a key determinant of Cape Verde's need for external financing, including from ED.

Figure 1. Cape Verde: Evolution of ED, 1995–2004

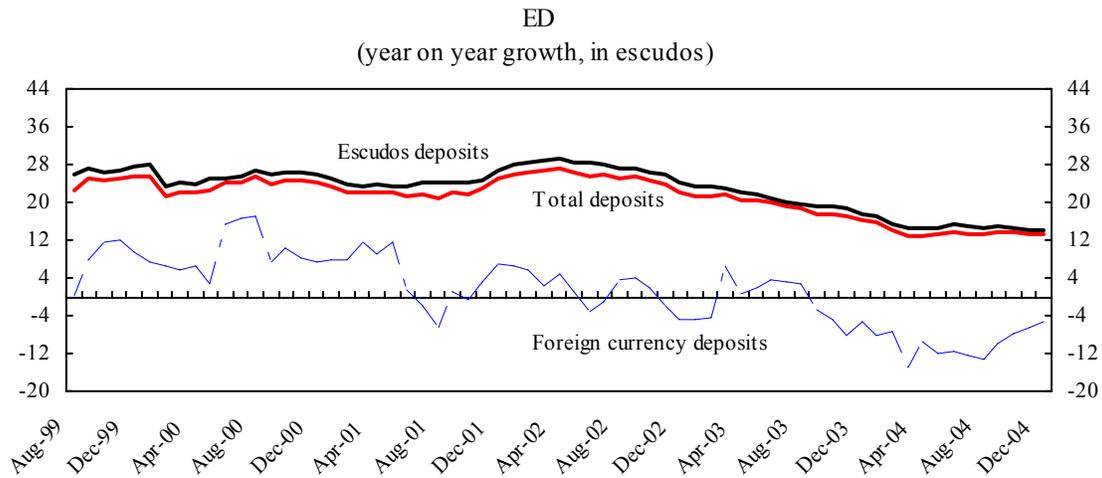
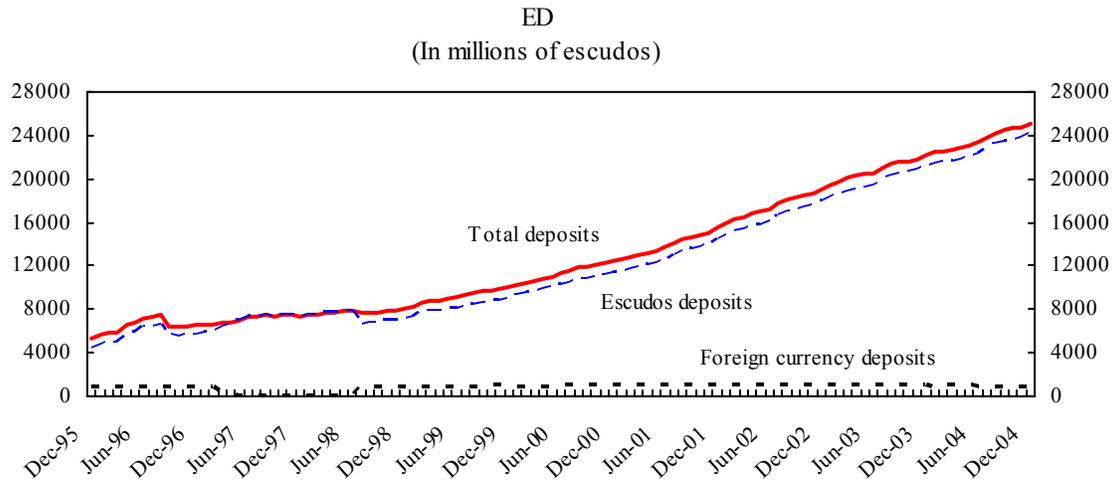
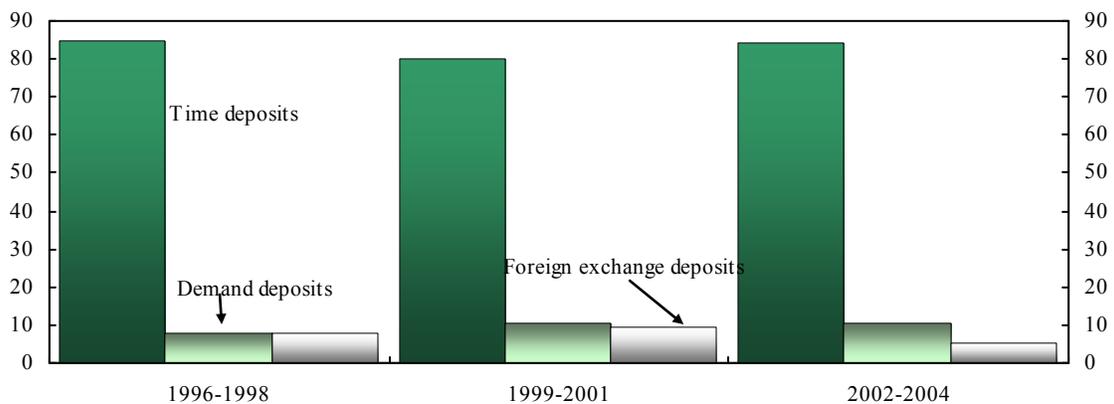
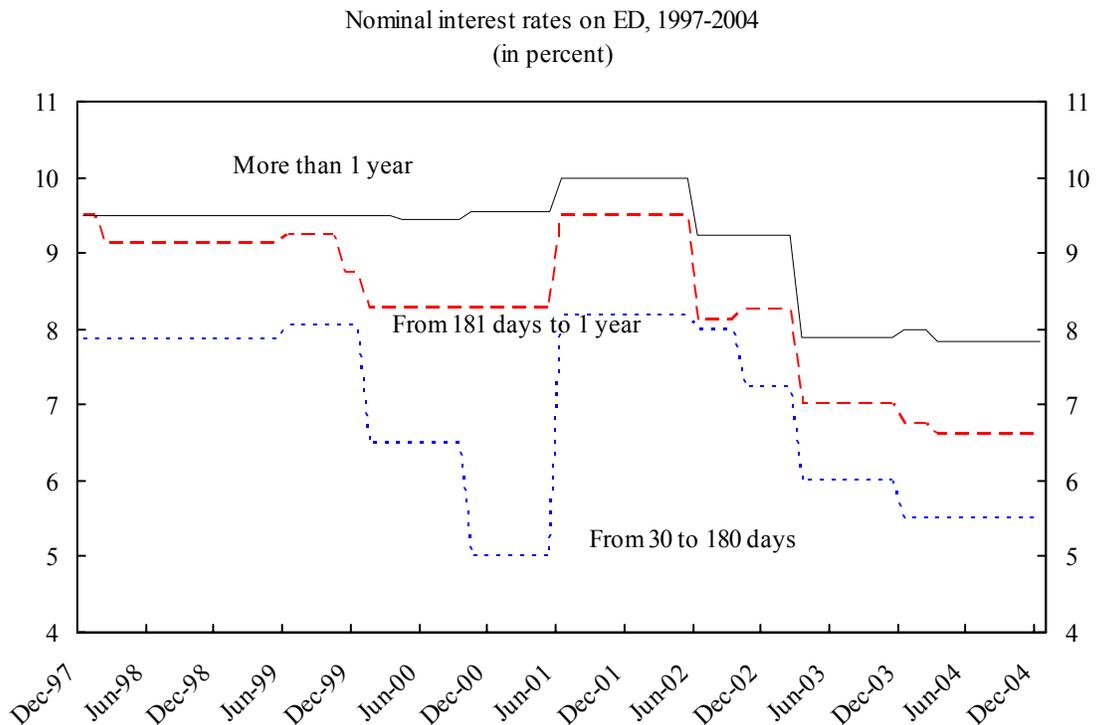
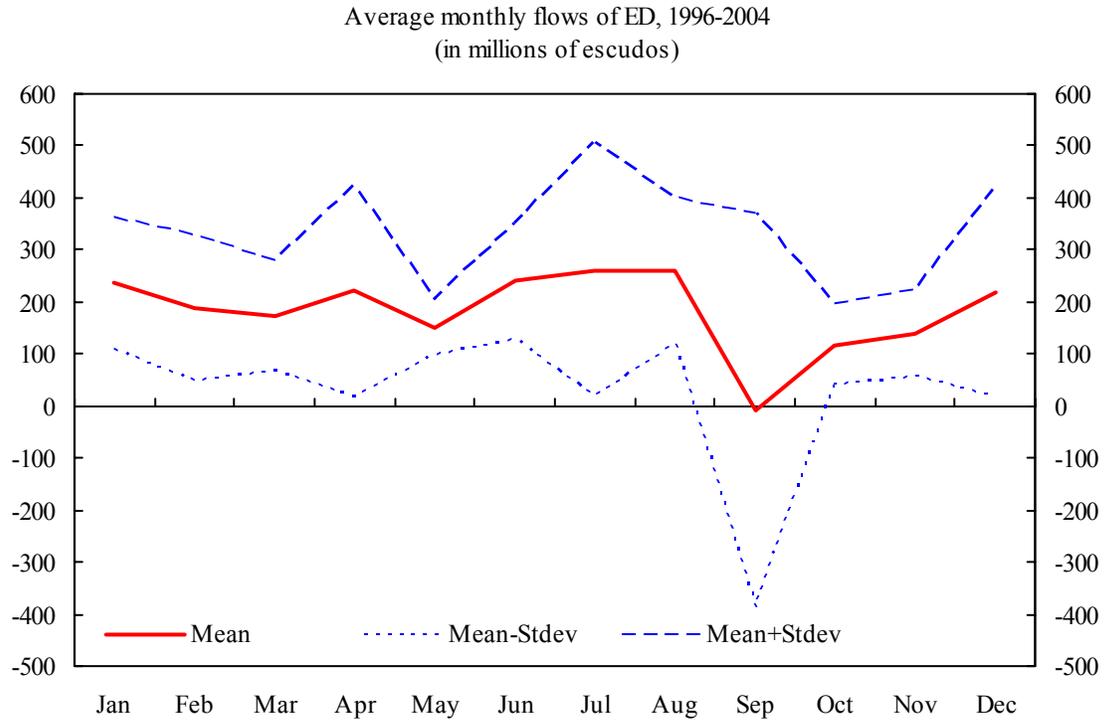


Chart 3. Structure of ED
(in percent)



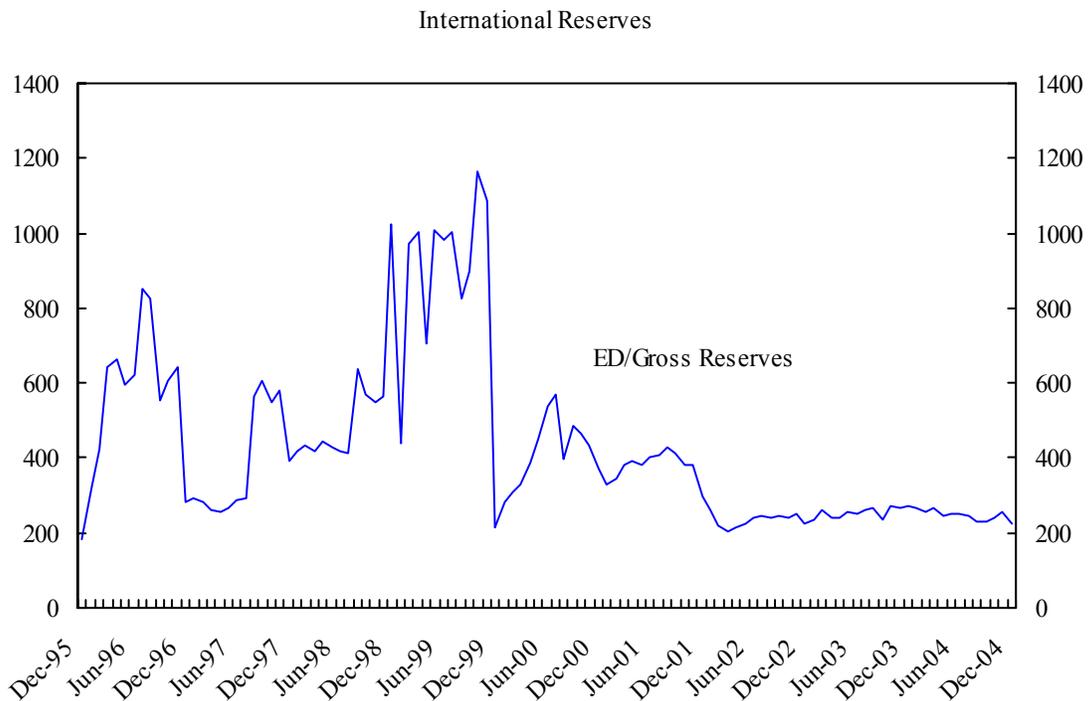
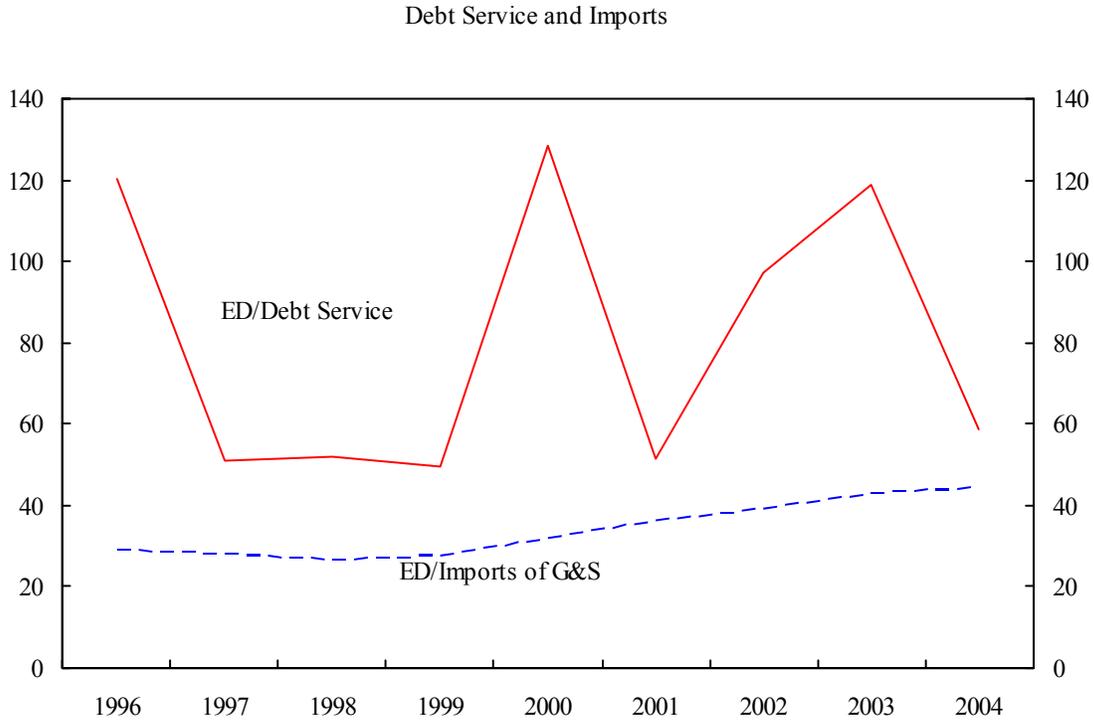
Sources: Cape Verde authorities; and estimates.

Figure 2. Cape Verde: Mean monthly ED net flows and interest rates, 1996–2004



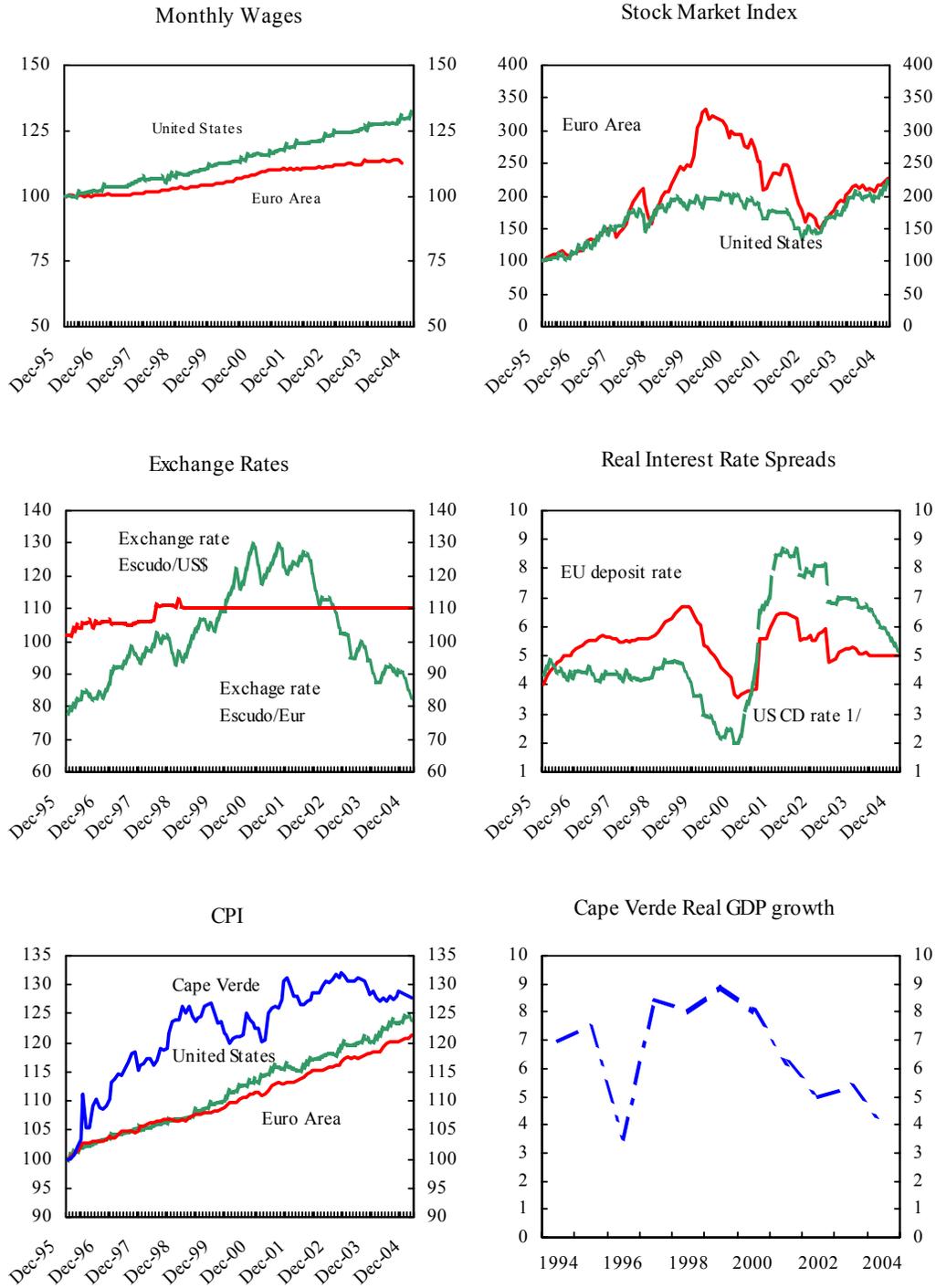
Sources: Cape Verde authorities; and estimates.

Figure 3. Cape Verde: ED Indicators, 1995-2004
(in percent)



Source: authorities and estimates.

Figure 4. Cape Verde: Determinants of ED, 1995-2004



Source: IFS, Datastream, authorities and estimates.

1/ 3 months and 6 months average

Table 2. Cape Verde: Data Sources and Description of Variables

<i>Variable</i>	<i>Source</i>	<i>Description</i>
<i>DEP</i>	BCV	Total emigrant deposits (time, demand, and foreign currency) expressed in millions of escudos at end of month.
<i>INT_CV</i>	BCV	Average nominal interest rate on nonresident deposits (from 1 to 6 months, from 6 months to 1 year and from 1 year).
<i>INT_EU</i>	ECB and IFS (16360LZM and 16360LHSZI)	Euro Area deposit rate (households).
<i>INT_US</i>	FRCDS3M and FRCD6M	United States secondary market CDs' rate, 3 and 6 months average
<i>SM_EU</i>	WEFA-Intline M163PISED	Euro Area stock index (Dow Jones industrial) from ECB monthly bulletin\end of month.
<i>SM_US</i>	WEFA-Intline (M111PISET)	United States share prices index\ NYSE composi\end of month.
<i>WA_EU</i>	WEFA-Intline (M163PLTTW)	Euro Area index of gross wages and salaries seasonally adjusted.
<i>WA_US</i>	IFS (11165EYZF)	United States index of hourly earnings.
<i>ESC_USD</i>	IFS (624RFZF)	Escudo/U.S. dollar end of period monthly official exchange rate.
<i>CPI_CV</i>	BCV	Consumer price index for Cape Verde.
<i>CPI_EUG</i>	IFS (16364HZF)	Harmonised consumer price index for the Euro Area. For the period before introduction of the Euro the CPI for Germany is used to splice the series.
<i>CPI_USD</i>	IFS (11164Zf)	Consumer price index for the United States.
<i>DUM0911</i>	Constructed	Dummy for September 11, 2001.
<i>DUMDEV</i>	Constructed	Dummy for the period characterized by devaluation fears that preceded the change of the peg from the basket of European currencies to the Portuguese escudo.
<i>DUMF_LAW</i>	Constructed	Dummy for the introduction of the foreign exchange law in August 1998 that liberalized foreign exchange transactions.
<i>DUMEURO</i>	Constructed	Dummy for the introduction of the euro that coincides with the first change in government democratically elected (January 2001).

Table 3. Cape Verde: Monthly Average Net ED Flows During Specific Events

Event	ED Flow	Months
Devaluation fear	24	11
Introduction of the Euro	185	2
Increase in fiscal expenditure that preceded 2001 election	171	3
September 11	185	2
Introduction of the new foreign exchange law	-199	1
Total 1/	183	108

1/ Average monthly flows over the whole period.

Table 4. Cape Verde: ADF Statistics Unit Root Test

Euro Area			United States		
Variables	t-ADF	lag (AIC)	Variables	t-ADF	lag (AIC)
<i>Log Levels 1/</i>			<i>Log Levels 1/</i>		
dep	0.806	4	dep	0.806	4
int_cv	-0.846	2	int_cv	-0.846	2
int_eu	-1.550	3	int_us	-1.010	3
cpi_cv	-1.995	5	cpi_cv	-1.995	5
cpi_eu	0.575	5	cpi_us	-0.203	3
wa_eu	-1.497	6	wa_us	0.038	4
sm_eu	-1.959	3	sm_us	-2.004	3
			esc_usd	-1.166	3
<i>First differences</i>			<i>First differences</i>		
dep	-5.957	4	dep	-5.957	4
int_cv	-5.757**	3	int_cv	-5.757**	3
int_eu	-3.230*	3	int_us	-3.043*	3
cpi_cv	-3.795**	5	cpi_cv	-3.795**	5
cpi_eu	-5.236**	5	cpi_us	-5.844**	3
wa_eu 2/	-2.297	6	wa_us	-5.181**	4
sm_eu	-5.171**	3	sm_us	-5.671**	3
			esc_usd	-4.823**	3

1/ Interest rates are expressed in levels.

2/ Not stationary in first differences according to ADF. However, the Phillips-Peron test suggests stationarity at 1 percent significance level.

Table 5. Cape Verde: Misspecification Tests
(Chi-squared test statistics)

A. VEC Test for Skewness, Kurtosis and Normality of Residuals 1/2/

	Euro Area			United States		
	Degr. of freedom	Statistic	Probability	Degr. of freedom	Statistic	Probability
Skewness	7	2.959	0.889	8	8.448	0.391
Kurtosis	7	207.737	0.000	8	72.137	0.000
Normality	14	210.696	0.000	16	80.584	0.000

1/ The null hypothesis is that of residuals with no Skewness, no Kurtosis, and Normal.

2/ Ortoogonalization is based on Cholesky (Lutkepohl) test; Skewness and Kurtosis is based on joint Chi-square test; Normality is based on joint Jarque-Bera test.

B. VAR Residual Serial Correlation LM Tests 1/

(Chi-squared test statistic)

Lags	Euro Area		United States	
	LM-Stat	Prob	LM-Stat	Prob
1	47.683	0.527	48.303	0.501
2	57.678	0.185	57.988	0.178
3	29.694	0.987	28.831	0.990
4	43.767	0.685	44.265	0.665
5	49.960	0.435	50.223	0.425

1/ The null hypothesis is that of no serial correlation at lag order h.

C. VEC Lag Exclusion Wald Test 1/2/

	Euro Area	United States
Lag1	537.131 [0.000]	378.625 [0.000]
Lag2	71.712 [0.019]	49.539 [0.908]
Lag3	...	85.285 [0.039]
Lag4	...	92.079 [0.0123]
Lag5	...	91.026 [0.015]
degrees of freedom	49	64

1/ The null hypothesis is that the coefficients of the lags are jointly non-significantly different from 0.

2/ Numbers in [] are probabilities.

Table 6. Cape Verde: Test Statistics for the Cointegrating Rank 1/

Euro Area					
Null	Alt	Trace statistic	Null	Alt	λ_{\max} statistic
$r=0^{**}$	$r \geq 1$	161.326	$r=0^{**}$	$r=1$	54.767
$r \leq 1^{**}$	$r \geq 2$	106.559	$r=1$	$r=2$	38.178
$r \leq 2$	$r \geq 3$	68.381	$r=2$	$r=3$	23.792
$r \leq 3$	$r \geq 4$	44.589	$r=3$	$r=4$	19.546
$r \leq 4$	$r \geq 5$	25.043	$r=4$	$r=5$	15.007
$r \leq 5$	$r \geq 6$	10.037	$r=5$	$r=6$	6.766
$r \leq 6$	$r \geq 7$	3.270	$r=6$	$r=7$	3.270

1/ The unrestricted Var was estimated with 2 lags following the results from the lag exclusion test in Table 5. The adjusted sample is 1996M12-2004M09. Probability values are in square brackets. * (**) denotes rejection of the null hypothesis and 5 (1) percent significance level.

United States					
Null	Alt	Trace statistic	Null	Alt	λ_{\max} statistic
$r=0^{**}$	$r \geq 1$	250.828	$r=0^{**}$	$r=1$	100.273
$r \leq 1^{**}$	$r \geq 2$	150.555	$r=1^{**}$	$r=2$	53.162
$r \leq 2^*$	$r \geq 3$	97.393	$r=2^*$	$r=3$	39.724
$r \leq 3$	$r \geq 4$	57.668	$r=3$	$r=4$	26.510
$r \leq 4$	$r \geq 5$	31.158	$r=4$	$r=5$	16.548
$r \leq 5$	$r \geq 6$	14.610	$r=5$	$r=6$	7.002
$r \leq 6$	$r \geq 7$	7.608	$r=6$	$r=7$	5.742

1/ The unrestricted Var was estimated with 4 lags following the results from the lag exclusion test in Table 5. The adjusted sample is 1996M06-2004M09. Probability values are in square brackets. * (**) denotes rejection of the null hypothesis and 5 (1) percent significance level.

Table 7. Cape Verde: Granger Causality Tests

Null Hypothesis: variable in (1) does not Ganger-Cause variable in (2)		F-Statistic	Probability
(1)	(2)		
a. Cape Verde - Euro Area			
INT_CV	INT_EU	0.186	0.905
INT_CV	LCPI_EUG	0.216	0.885
INT_CV	LSM_EU	1.349	0.263
INT_CV	LWA_EU	0.829	0.481
LCPI_CV	INT_EU	1.439	0.236
LCPI_CV	LCPI_EUG	1.633	0.187
LCPI_CV	LSM_EU	0.791	0.502
LCPI_CV	LWA_EU	2.642	0.054
LDEP	INT_EU	1.500	0.219
LDEP	LCPI_EUG	3.750	0.014
LDEP	LSM_EU	0.072	0.975
LDEP	LWA_EU	0.058	0.981
b. Cape Verde - United States			
INT_CV	INT_US	0.071	0.975
INT_CV	LCPI_US	0.811	0.491
INT_CV	LESC_USD	0.339	0.797
INT_CV	LSM_US	2.417	0.071
INT_CV	LWA_US	0.431	0.731
LCPI_CV	INT_US	2.132	0.101
LCPI_CV	LCPI_US	1.318	0.273
LCPI_CV	LESC_USD	0.822	0.485
LCPI_CV	LSM_US	0.621	0.603
LCPI_CV	LWA_US	1.090	0.357
LDEP	INT_US	2.302	0.082
LDEP	LCPI_US	1.102	0.352
LDEP	LESC_USD	2.196	0.094
LDEP	LSM_US	1.095	0.355
LDEP	LWA_US	1.964	0.125
c. United States			
LCPI_US	INT_US	3.241	0.025
LESC_USD	INT_US	6.219	0.001
LSM_US	INT_US	4.052	0.009
LWA_US	INT_US	2.920	0.038
d. Euro Area			
LCPI_EUG	INT_EU	1.111	0.348
LSM_EU	INT_EU	3.236	0.026
LWA_EU	INT_EU	1.339	0.266
LWA_EU	LCPI_EUG	3.388	0.021
INT_EU	LWA_EU	6.346	0.001
LSM_EU	LWA_EU	7.424	0.000

Table 8. Cape Verde: Selected Results of the VECM

Euro Area				
Cointegrating Equation:	CointEq1	t-statistics	CointEq2	t-statistics
LDEP(-1)	1.000			
INT_CV(-1)	0.002	[0.274]		
INT_EU(-1)	-0.084	[-2.920]	0.590	[2.852]
LCPI_CV(-1)	0.000			
LCPI_EU(-1)	-5.189	[-4.725]	-0.679	[-0.207]
LSM_EU(-1)	0.083	[2.834]	1.000	
LWA_EU(-1)	-4.265	[-4.061]		
C	34.058		-2.743	
Estimates of the speed of adjustment of emigrant deposits				
CointEq1	-0.047	[-2.371]		
CointEq2	0.000	[NA]		
Estimate of the effect of the change in the exchange rate peg on ED				
DUMDEV	-0.011	[-2.966]		
LR test for binding restrictions (rank = 2):				
Chi-square(7)	11.982			
Probability	0.101			
R-squared	0.371			
Sum sq. resids	0.007			
S.E. equation	0.010			
F-statistic	1.520			

Table 9. Cape Verde: Selected Results of the VECM

United States

Cointegrating Equation:	CointEq1	t-statistics	CointEq2	t-statistics
LDEP(-1)	1.000			
INT_CV(-1)	0.092	[3.774]		
INT_US(-1)	0.128	[7.284]	1.000	
LCPI_CV(-1)				
LCPI_US(-1)	-8.095	[-4.848]	-133.864	[-7.759]
LSM_US(-1)	-0.063	[-0.875]	-3.567	[-5.809]
LWA_US(-1)	4.123	[2.812]	132.068	[9.734]
LESC_USD(-1)	-0.764	[-5.083]	-5.484	[-7.088]
C	11.419		44.946	
Estimates of the speed of adjustment of emigrant deposits				
CointEq1	-0.087	[-2.566]		
CointEq2	0.000	[NA]		
Estimate of the effect of the change in the exchange rate peg on ED				
DUMDEV	-0.016	[-3.795]		
LR test for binding restrictions (rank = 2):				
Chi-square(3)	2.192			
Probability	0.534			
R-squared	0.754			
Sum sq. resids	0.009			
S.E. equation	0.013			
F-statistic	4.083			

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FINANCIAL SECTOR: INSTITUTIONS, OVERSIGHT, RISKS, AND VULNERABILITIES²⁴

The level of financial intermediation in Cape Verde is relatively high. Improving confidence in the exchange rate, development of the banking sector, as well as several measures to strengthen the financial sector should support growth and deepening of the sector and contribute to Cape Verde's economic development. The main conclusions are the following. The financial sector is important for economy diversification and promotion of economic growth. Further efforts are needed to improve the money market and to expedite the development of the domestic capital market. A financial system with an active financial sector and domestic capital market will require a comprehensive regulatory and supervisory framework to maintain its integrity.

I. INTRODUCTION

1. Sound monetary and exchange rate policies and improved financial regulations have contributed to strengthening the financial sector in Cape Verde. Price stability and accumulation of international reserves remain the main objectives of the monetary policy of the Bank of Cape Verde (BCV). The financial sector is seen by the government as playing a key role in supporting economic growth and development. The banking sector continues to dominate financial intermediation. Although it is highly concentrated²⁵ and needs to improve efficiency, at present, the financial soundness indicators (FSI) compare favorably relative to international norms, and they are better than the average for Africa. The ratio of non-performing loans net of provision relative to capital declined in recent years. However, the share of non-performing loans in the gross total loans remains high by international standards.
2. **The level of financial intermediation in Cape Verde is relatively high.**²⁶ Credit to the private sector and deposits of commercial banks were 34 and 60 percent of GDP respectively at end-2003. Both these indicators were much higher than the average for sub-Saharan Africa and for all individual countries in the region (see Table 1).
3. **This chapter first provides an overview of the financial sector in Cape Verde** and then turns to discuss the regulatory environment, the main areas of risks and vulnerabilities in Cape Verde's financial sector, and financial soundness indicators (FSIs). In addition the chapter indicates how these vulnerabilities could be reduced, and more generally, how the challenges of strengthening the financial sector could be met in the medium term.

²⁴ Prepared by Elena Loukoianova.

²⁵ Two-firm concentration ratio in Cape Verde is higher than three-firm concentration ratio in other African countries (see Table 1).

²⁶ The description of the structure of the financial sector in Cape Verde is provided in Appendix I.

Table 1. Cape Verde: Regional Comparisons of Selected Financial Indicators, 2003

(In percent)

Country	Domestic credit/ GDP	Total deposits/ GDP	Foreign liabilities/ GDP	Credit to private sector/GDP 1/	Concentration ratio 2/
Cape Verde 3/	67.3	60.2	2.8	34.0	89.0
Benin	9.8	17.6	3.8	14.5	88.4
Cameroon	16.0	14.5	0.7	10.2	75.6
Chad	11.3	4.7	0.9	4.4	1.0
Ghana	25.9	20.5	1.9	11.7	59.1
Guinea-Bissau	12.8	6.4	0.001	1.9	...
Malawi	17.2	16.7	1.0	5.9	71.3
Mali	16.1	17.6	2.4	19.0	84.4
Mozambique	11.0	27.6	1.2	2.2	86.0
São Tomé & Príncipe	23.2	43.8	0.8	16.5	...
Senegal	22.8	24.9	1.0	21.0	59.5
Tanzania	8.4	17.2	0.1	7.6	55.2
Sub-Saharan Africa (avg)	26.0	27.0		12.4	77.4

Sources: Fitch's Bankscope database; and World Bank structural database.

1/ Credit of money deposit banks on the private sector.

2/ Assets of three largest banks as a share of assets of all commercial banks in the system in 2001.

3/ Two-bank concentration ratio for Cape Verde is for 2003.

II. OVERVIEW OF THE FINANCIAL SECTOR

4. **Cape Verde has a financially sound and well developed banking system, which has been growing steadily since 1999.** Net domestic assets and deposits have been growing on average by 13 percent a year over 1999–2004, and total credit to the economy by 12.2 percent over the same period. Average return on equity was almost 20 percent, and the ratio of deposits to GDP was 64.2 percent at end-2004 (see Table 2).

Table 2. Cape Verde: Aggregate Indicators of the Banking Sector, 2001–04

	2001	2002	2003	2004 1/
	(In billions of Cape Verde escudos, end of period)			
Total assets	50.0	57.2	62.8	68.9
Total loans	20.4	23.4	27.2	29.8
Total deposits	41.5	46.9	52.1	58.1
Nonperforming loans	1.9	1.74	2.0	2.2
	(In percent)			
Transformation rate 2/	49.1	49.2	52.1	51.3
NPL/Total assets	3.8	3.0	3.2	3.1
Cost to income ratio	65.4	70.9	66.6	65.6
Average cost of funds	3.8	4.1	3.8	3.4

Source: Bank of Cape Verde.

1/ Provisional data.

2/ Transformation rate is the ratio of total loans to total deposits.

5. **The banking system is mostly foreign-owned, small, and highly concentrated.** In December 2004, the financial sector comprised the central bank (Bank of Cape Verde, BCV), four commercial banks,²⁷ three off-shore banks, two insurance companies, and five non-banking financial institutions (two exchange bureaux, one society of risk capital, one venture capital company, and one credit card issuing and managing company). The banking sector is

²⁷ Four commercial banks include Banco Commercial do Atlântico (BCA), Caixa Economica de Cabo Verde (CECV), Banco Interatlântico (BIA), and Banco Totta de Cabo Verde (BTCV). They are all subsidiaries of Portuguese banks. Banking services are provided on all islands through 35 branches of commercial banks. The BTCV was acquired by a group of domestic private investors at the beginning of 2005, and became the first domestic private bank, Banco Caboverdeano de Negócios (BCN).

highly concentrated, with the largest bank, BCA, controlling 66.3 percent of the total deposits and total assets and 55.6 percent of the total loans of the commercial banks at end-2004 (see Table 3).

Table 3. Cape Verde: Shares of Market in the Banking Sector, 2004

(In percent)

	Total assets	Total deposits	Total loans
Banco Comercial do Atlantico	65.0	66.3	55.6
Caixa Economica de Cabo Verde	24.0	23.0	36.2
Banco Interatlantico	7.7	7.5	6.7
Banco Totta de Cabo Verde	3.3	3.2	1.5

Source: Bank of Cape Verde.

6. **The financial sector is highly liquid.** Broad money was 72.3 percent of GDP at end-2004, which is one of the highest in Sub-Saharan Africa. Net claims on the central government accounted for 24.5 percent of broad money, credit to the economy—for 50.1 percent, and currency in circulation—for about 11 percent. Demand for credit has been rising since 1998 with about 50 percent borrowed by the government (see Table 4). Credit to the private sector has risen on average by 11.4 percent in 1999–2004. As a result, the ratio of credit to the private sector to GDP has risen from 30 in 1999 to 38 in 2004. This rapid expansion of credit is attributable to strong demand for housing loans, especially by the emigrant community.

Table 4. Cape Verde: Total Credit of the Banking Sector, 2001–04

(In billions of Cape Verde escudos)

	2001	2002	2003	2004
Credit to the Economy	22.4	25.1	28.9	31.0
<i>of which:</i>				
BCV	1.2	1.2	1.2	1.2
BCA	12.6	14.1	15.6	15.8
CECV	7.0	8.0	9.9	11.3
BTA	0.5	0.4	0.4	0.4
BIA	1.1	1.5	1.9	2.3
Total commercial banks	21.2	23.9	27.7	29.8
Credit to government	22.2	25.1	28.9	28.1
Total credit	44.7	50.2	57.8	59.1

Source: Bank of Cape Verde.

III. MARKET INFRASTRUCTURE AND INTERMEDIATION SPREADS

7. **The market infrastructure in Cape Verde is still developing.** At present it consists of the payment system and the interbank market. The BCV has taken initiatives to strengthen institutional arrangements for financial infrastructure and legislation for banking, securities trading, and corporate governance. The BCV fostered the establishment of the stock exchange and the secondary market for Treasury bills. However, they have not yet become operational for a number of reasons, including the limited amount of available liquid financial instruments,²⁸ and other factors.²⁹

8. **In an effort to deepen the financial system and to strengthen financial infrastructure the BCV introduced a new payment system in 1997.** Following the improvements in the interbank payments, *A Comissão Interbancaria para o Sistema de Pagamentos* (CISP), created in June 1997, was transformed into *A Sociedade Interbancaria e Sistemas de Pagamentos* (SISP) in 1999. In 2001, another institution, *O Sistema Integrado de Compensação Interbancaria e Liquidação* (SICIL), was created to integrate three similar sub-systems: (i) compensation of checks and interbank transfers, and (ii) 24-hour processing operations.

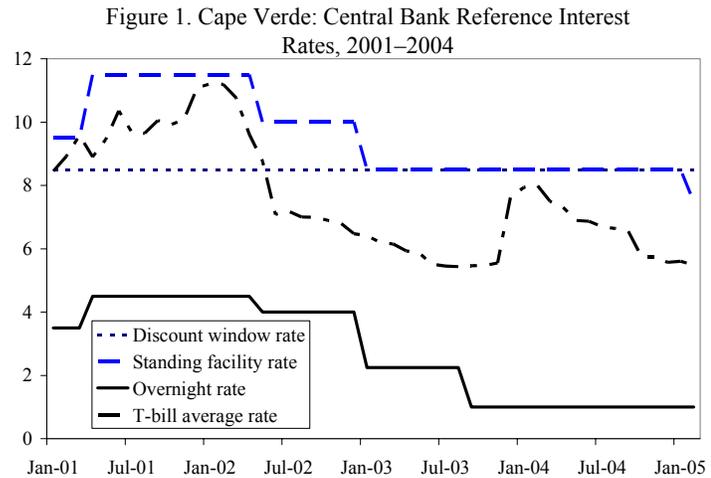
9. **The SISP entered into an agreement with VISA International to offer electronic VISA services** to further expand its role in the development of international financial markets in Cape Verde. This system supports tourism and provides business opportunities by attracting more foreign exchange to the country. The implementation of the system in some islands is still underway. To support the costs of further innovations, the SISP has acquired in-house expertise to produce customized cards, including VISA cards.

10. **The interbank market is still developing.** At present, the interbank market is marked by a limited number of participants, inelastic interest rates, dominance of two big banks, lack of interbank deposits, and temporary excess liquidity in the banking system. The Treasury bill market operates with bills of maturities up to one year. The BCV has the right to issue Certificates of Monetary Intervention (Títulos de Intervenção Monetária, TIM) and Certificates of Monetary Regulation (Títulos de Regulação Monetária, TRM) for the purpose of injecting liquidity into the market in the short term. However, the BCV has never used these facilities since July, 1999, because since that time, there was no shortage of liquidity in the banking sector.

²⁸ The only financial instruments available are treasury bills with the maturity up to one year. There are no corporate bonds and stocks on the market.

²⁹ First, elevated administrative costs made the stock exchange unlikely to become sustainable. Second, a withdrawal of a significant portion of treasury bills from the financial system, as a result of the domestic debt reduction, transformed these securities into the TCMFs.

11. **The BCV manages liquidity through open market operations.** The BCV has been given a mandate by the government to conduct Treasury bill auctions, as government agent. The BCV uses Treasury bills as policy instruments to absorb the excess liquidity from the banking system. Also, the BCV determines reference rates, including those for lending/borrowing facilities, and overnight deposit rate (see Figure 1).



12. **The government and corporate bond market does not exist at present.** The five-year government bonds have been swapped for the TCMFs.³⁰ The BCV is planning to introduce operations with medium and long term instruments to improve the dynamic of the financial system as well as foster better liquidity management. Corporate bonds do not exist either. Issuance of corporate bonds may become an attractive alternative to bank loans for attracting funding for big domestic enterprises, including the public utility company.

Intermediation spread

13. **Lending rates increased in the period 2000–02 to a peak of 14.1 percent (see Table 5), but they have declined slightly to 13.4 percent on average in 2004.** This evolution reflects the behavior of the standing lending facility rate of the BCV (with approximately a one-year lag). The reduction of lending rates continues in early 2005 following the reduction of the unremunerated reserve requirements and the standing lending facility rate of the BCV. The BCV decreased the standing lending facility rate from 8.5 to 7.5 percent in February, 2005. As a result, the two largest banks decreased all commercial lending rates by 1 percent. In general, the sensitivity of the volume of credit to the change in lending rates appears to be low, because when lending rates increased in the past, credit volumes to the private sector did not diminish. Between 2001 and 2004 real lending rates rose sharply in view of the drop in the inflation rate.

³⁰ See Box 1 for the description of the Trust Fund and the TCMFs.

Box 1. The Trust Fund and TCMFs

The International Support for Cabo Verde Stabilization Trust Fund (the Trust Fund) was established in 1998 to eliminate the debt overhang¹ through a privatization-cum-domestic-debt-reduction operation (DDRO), which represented a key element in the fiscal consolidation program supported by the 1998–99 Stand-By Arrangement. Specifically, the purpose was to mobilize foreign aid and resources from privatization to establish a Trust Fund placed abroad. The Trust Fund was to issue long-term bonds, *Titulos Consolidados de Mobilização Financeira* (TCMF), to be remunerated by returns on its investment, and these would be swapped for government bonds held by banks and other domestic investors. In this manner, the government budget would be relieved of the cost of servicing its domestic debt, thereby creating room for other expenditure.

This scheme was originally designed in 1998 with the purpose of retiring domestic government debt, which at that time amounted to US\$180 million.¹ In the event, resources from the aid and privatization, placed in the Trust Fund amounted by end-2004 to EUR 107 million, while the government debt increased after 1998. As a result, the Trust Fund bonds could replace only government bonds with maturity of more than one year, held outside the BCV (CVEsc 17.7 billion), and government domestic debt after this swap amounted by end-2004 to CVEsc 64.4 billion. The Trust Fund is managed by the Bank of Portugal under a management agreement signed in December, 1998. The invested portfolio generated annual interest from 3 to 5 percent during 1999–2004. For example, the interest paid on the TCMFs has been 2.89 percent in 2004.

The TCMFs are perpetual securities in CV escudos issued by the Republic of Cape Verde through the Treasury, converted from the Income Participation Units of the Trust Fund, denominated in dollars. During the first three years of their existence, TCMFs were nonnegotiable by entities other than credit institutions operating in Cape Verde. From the beginning of the fourth year of existence of TCMFs to the end of the seventh year, any credit institution may transfer TCMFs representing up to 25 percent of the total TCMF portfolio it holds. From the beginning of their eighth year of existence, TCMFs may be freely negotiable. The government of Cape Verde may acquire TCMFs at any time. TCMFs acquired by the government can be traded at their reference value.

The Trust Fund incomes are the net profits from managing its portfolio. The net profit is distributed in the following way: (i) 90 percent is delivered to the owners of the TCMFs proportionally, (ii) 5 percent is delivered to the BCV, and (iii) 5 percent is delivered to the Fund for Stabilization and Development (FEED).

¹ At end-1997, after years of running large bank-financed fiscal deficits, the stock of domestic debt stood at CVEsc 17.7 billion, equivalent to US\$180 million, or 40 percent of GDP.

14. **Between 2000 and 2004, the average deposit rate fell by one percentage point, while the average lending rate rose by 0.6 percentage points.** Thus, the bank intermediation spread—defined as the difference between the average rate charged on bank loans and that paid on deposits—widened from 7.1 percent in 2000 to 8.7 percent in 2004 (see

Figure 2. Cape Verde: Ratio of Credit to the Economy to Total Deposits and Intermediation Spread, 1996–2004

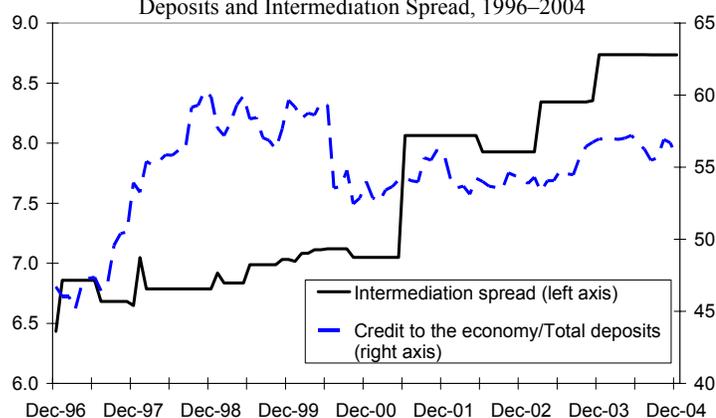


Figure 2). The widening spread is a result of several factors, such as high concentration of the banking sector, inadequate competition, high operational costs, relatively high share of nonperforming loans, high unremunerated reserve requirements, and risk premium against the private sector claims. In addition, the largest bank, BCA, holds a large amount of the low-yielding Trust Fund claims (TCMFs).³¹ Traditionally, in Cape Verde emigrant deposits have carried a higher interest rate than other time deposits, in order to attract emigrant savings. Up to 2003, the government provided an interest subsidy to banks on the emigrant time deposits. After the subsidy was abolished, banks continued to offer higher rates on emigrant deposits, because they constitute a key source of funding (40 percent of total deposits) for the banks. However, since 2002, rates on these deposits have declined in line with other rates.

15. **The widening intermediation spread hampers the transformation rate—the ratio of credit to the economy to total deposits.** The transformation rate has declined after 1999 and then was rising only insignificantly (see Figure 2). The transformation rate, which demonstrates the activity of banks on the loan markets, differed across commercial banks at end-2003—from 82 percent for CECV to 25 percent for BTCV.

Table 5. Cape Verde: Term Structure of Interest Rates, 2000–04

	2000	2001	2002	2003	2004
Refinance rate	8.5	11.0	10.5	8.5	8.5
Average T-bill rates	8.3	9.7	8.3	5.9	6.3
91 days	7.8	9.5	7.9	5.8	6.2
182 days	8.5	10.3	8.0	5.8	5.9
364 days	8.5	9.2	9.0	6.2	6.9
Lending rate (average)	12.8	13.8	14.1	13.4	13.4
Time deposit rate (average)	5.7	6.1	6.2	5.1	4.7
Intermediation spread	7.1	7.6	8.0	8.3	8.7
Emigrants time deposit rates					
From 30 to 180 days	6.1	6.8	7.9	6.2	5.5
From 181 days to one year	8.3	9.0	8.7	7.2	6.6
More than one year	9.5	9.8	9.6	8.1	7.9
Inflation rate (percentage change over the previous period)	-2.5	3.7	1.9	1.2	-1.9

Sources: Bank of Cape Verde; and staff estimates.

³¹ The return on the TCMFs has been around 3 percent, which is lower than the return on Treasury bills by 3 to 4 percent.

IV. REGULATION AND SUPERVISION

16. **The Bank of Cape Verde has responsibility for the regulation and supervision of commercial banks, offshore bank and non-bank financial institutions.** All commercial banks are subject to regulatory requirements (see Box 2), an annual on-site examination, and regular monthly reporting as a part of the off-site reporting system. The supervision department informs the Board of the BCV on a monthly basis on the situation of the individual banks and their compliance with prudential regulations.

17. **Regulations of the banking and financial sectors have improved over recent years.** The BCV has been implementing a number of measures designed to reinforce its operational and oversight responsibilities by training its staff and modernizing computer systems and internal control. A framework for internal controls for the commercial banks for anti-money laundering is becoming an integral part of on-site inspection.

18. **The authorities have addressed shortcomings in the enforcement of financial contracts.** There is an ongoing project to computerize the notary and registries as well as to link the islands into a single computer system. This initiative should reduce the time for registering collateral, as well as reducing the potential for fraud. Even with these efforts, delays in getting legal decisions may be greater than two years and while better trained, magistrates are not specialized in financial contracts. In addition, dispute resolution system could be introduced.

V. SAFETY NETS

19. **Under the new Central Bank Organic Law, the Central Bank may provide liquidity support for commercial banks.** The central bank may grant short-term credit to commercial banks with the collateral of marketable government securities. Furthermore, to bridge temporary liquidity shortages, the central bank may, if necessary, act as a lender of last resort; any lending of this type is limited, however, to three times the borrowing entity's capital and carries a penalty interest rate, determined on case by case basis. If necessary, the BCV can issues temporary emergency rules to govern the volume of credit and interest rates applicable to commercial banking operations, subject to approval by the Board. As subsidiaries of foreign banks, three banks in Cape Verde may receive liquidity support from their parent banks, which reduces the vulnerability of the banking sector.

VI. MACROECONOMIC RISKS AND VULNERABILITIES

20. **There exists a number of macroeconomic risks and vulnerabilities in the financial sector.** Credit risk remains the main risk in the banking sector. The concentration and operational risks are also important. Other risks stemming from the international economy are an increase of world interest rates, volatility of the euro-dollar exchange rate, and a slowdown of economic growth in the EU.

Box 2. Regulatory Requirements and Main Recent Legal Changes

In July 2002, the National Assembly approved a new Central Bank organic law (CBOL). This law was revised with close cooperation from the Fund and aimed to clarify the central bank's overriding policy objectives and bring the law in line with international best practices.

The new CBOL exhibits the following major changes: (i) Cash advances to the government may not exceed, at any time, five percent of the current revenue collected in the preceding year. Any overdraft account of this kind must be in balance at the end of each year; (ii) A new article has been added to specify the independence and accountability of the BCV; (iii) Admissible operations with domestic monetary policy instruments have been streamlined; and (iv) New best practice procedures for safeguarding the central bank's capital ("top-up" rules), determining net income, and distributing net profits, have been introduced.

In December 2002, the National Assembly approved the Anti-Money Laundering legislation (Lei no 17/IV/2002), and accompanying regulations were issued in February, 2003 (Annex to Circular Series A No. 108). The BCV incorporated 40 recommendations of FAFT/GAFI in its law and expects to incorporate the other eight operations imposed by GAFI.

The banks must comply with the following prudential regulations: (i) Equity stakes in firms not supervised by the BCV may not exceed certain maximum limit; (ii) Equity and loans exceeding 10 percent of the bank's capital are considered high risk. Exposure to any client may not exceed 25 percent of the institution's capital, and the total amount of high risks may not exceed eight times the amount of the bank's capital; (iii) The minimum capital of a bank in CV Escudos is 300 million and the risk-weighted capital adequacy ratio is 10 percent (the definitions of the various components of own capital and the criteria for weighting off-balance sheet assets and accounts follow closely the rules adopted by the EU); and (iv) Banks are obliged to set up provisions for overdue loans, general credit risks, retirement pensions, survivors' benefits, and capital losses on securities and other instruments (nonperforming loans are divided into the five groups—up to 3, 6, 12, 36, and more months—with nonperforming loans secured by collateral requiring lower provisioning).

21. **Credit risk is the main risk in the banking sector.** While the demand for credit has been steadily increasing, commercial banks have taken important measures to improve their credit analysis. As a result of these efforts, the quality of the banks' loan portfolio has been improving. Other contributing factors have been improved supervision of the BCV, and a better judicial enforcement of financial contracts. The banks are cautious to lend without collateral and/or an established credit history of the client.

22. **Concentration and operational risks are also important for the commercial banks.** Commercial banks in Cape Verde have high loan concentration in the housing sector and consumer loans (see Table 6 and Box 2 on the regulatory limits for sectoral concentration). There are no regulatory limits on sectoral concentration.³² Operational risk is not assessed and evaluated in an adequate way, because financial institutions lack conditions

³² For the regulatory limits on exposure, see Box 2.

and the capacity to do that.³³ The adoption of adequate models could be expensive and slow, because it requires extensive preparation.

Table 6. Cape Verde: Composition of Loans in two Largest Banks, 2002–03
(In percent of total loans)

	BCA		CECV		Average	
	2002	2003	2002	2003	2002	2003
Short-term loans (STL)	17.3	17.8	14.5	8.6	16.2	14.0
Medium- and long-term loans (MLTL)	82.7	82.2	80.4	86.8	81.8	84.1
Consumer loans	23.0	23.7	8.2	15.6	17.3	20.3
Housing loans	42.3	43.1	50.3	46.7	45.4	44.6
Non-performing loans	9.3	9.9	5.1	4.6	7.7	7.7
Ratio of short-term loans to medium- and long-term loans	20.9	21.7	18.0	9.9	19.8	16.6

Sources: Annual reports of BCA; and CECV.

23. **External shocks pose an important risk for the financial system in Cape Verde, as the country is highly dependent on external capital inflows.**³⁴ An increase in world interest rates could have an adverse effect on the banking system in Cape Verde: even if confidence in maintaining the country's peg to the Euro is supported by appropriate reserve coverage, declining margins between domestic and world interest rates could result in a sharp reduction of emigrant deposits inflows. In addition, rising world interest rates may push domestic lending rates up further, which may result in a deterioration of banks' loan portfolios and decrease the amount of loans to the private sector.

Financial soundness indicators

24. **The FSIs, with the exception of nonperforming loans (NPLs), are sound and compare well to international benchmarks.** The FSIs in Cape Verde are better than average in Africa. Three banks fully comply with prudential requirements, marking a determined efforts by the BCV to enforce and maintain full compliance. The smallest bank, BTCV, currently violating prudential norms, has performance contracts with the banking supervision department of the BCV with timetables within which it needs to return to full compliance.

³³ Old data are not computerized, thus, the time series are not long enough to apply advanced measurement methods.

³⁴ Detailed analysis of the accumulation of emigrant deposits is provided in the first Selected Issues Paper.

25. **The level of nonperforming loans has been steadily declining, although this remains one of the main concerns of the banking system.** The banking system (excluding the BTCV) has come a long way in reducing the NPLs as a percentage of total loans. The NPLs fell from about 30 percent in 1997 to 7.2 percent at end-2004. In 2004, three banks had share of NPLs of less than 10 percent of total gross loans, while one of the small banks, BTCV, had more than 28 percent of NPLs in its loan portfolio and experienced a loss of income (see Table 7).

Table 7. Cape Verde: Ratio of Nonperforming Loans to Total Gross Loans in Commercial Banks, 2001–04

(In percent)

	2001	2002	2003	2004
BCA	10.2	8.6	9.0	9
CECV	7.8	5.1	4.6	4.7
BTCV	19.3	27.7	25.3	28.3
BIA	3.5	3.9	4.9	4.4
Average	9.3	7.4	7.4	7.2

Source: Bank of Cape Verde.

26. **The current ratio of NPLs to total loans of 7.2 percent remains high by international norms.** This ratio is higher in Cape Verde compared to global and European samples, but it is much lower than average in Africa (see Table 8). The ratio of NPLs-net-of-provisions to capital, at 1.9 percent, is in fact lower than in the global and European samples. Although provisions as a percentage of NPLs, at 96.7 percent in 2004, are below global and European benchmarks, they are nonetheless substantial, especially compared to other developing countries, and African countries, in particular.

27. **Banks in Cape Verde appear to be generally profitable.** Return on assets has been stable at 1 percent on average over the last 4 years, higher than global and European benchmarks, but lower than in the African sample. The return on equity ratio, at 16.7 percent in 2004, is higher than global (9.2 percent) and European (13.7 percent) values, and above the African sample comparator (15.1 percent). The strong profitability in Cape Verde is not surprising, considering country risk, very high interest rate margins, and conservative strategies of the commercial banks. Intermediation spreads are high and continue to increase, as discussed above. Banks appear to be very liquid. Liquid assets account for more than 90 percent of total assets and more than 110 percent of short-term liabilities. All these factors compensate for relatively high overhead costs as a share of gross income (65.6 percent), which is higher than international benchmarks (63 percent).

Table 8. Cape Verde: Financial Soundness Indicators
(In percent, unless indicated otherwise)

	2001	2002	2003	2004 1/	International benchmarks (end-2002) 2/		
					Global sample	European sample	African sample
Capital adequacy							
Regulatory capital to risk-weighted assets	16.0	15.0	13.8	13.3			
Regulatory Tier I capital to risk weighted assets	17.8	16.5	15.2	14.6			
Asset quality							
Nonperforming loans to total gross loans	9.3	7.4	7.4	7.2	5.0	3.2	14.5
Nonperforming loans net of provisions to capital	-8.2	-7.9	-3.6	1.9	3.7	6.7	...
Provisions to nonperforming loans	113.5	114.9	106.3	96.7	139.0	129.0	91.9
Earnings and profitability							
Returns on assets (ROA)	1.0	1.1	1.1	0.9	0.7	0.6	2.9
Returns on equity (ROE)	15.5	18.7	19.8	16.7	9.2	13.7	15.1
Interest margin to gross income	66.5	66.7	68.5	66.0			
Non-interest expenses to gross income	63.2	67.6	66.6	65.6	63.0	62.0	...
Liquidity							
Liquid assets to total assets	93.2	93.9	93.9	94.1			
Liquid assets to short-term liabilities	112.9	112.1	111.7	111.4			

Sources: Bank of Cape Verde; Bankscope database; and author's estimates.

1/ Provisional data.

2/ Global sample consists of 108 commercial banks from Latin America (56), Europe (42), and the U.S. (10). African sample is based on 953 banks from Bankscope database.

VII. ENHANCING EFFICIENCY OF THE FINANCIAL SYSTEM

28. **Lack of competition in the banking sector and subsequent dominance of the BCA negatively influences the efficiency of financial intermediation.** Over the last several years, CECV has followed a more aggressive strategy in the lending and deposit markets, which resulted in an increase of its market shares from 6 to over 23 percent. This enhances competition, although it has led to an almost pure duopolistic system in the banking sector, especially in determining interest rates at the treasury bill auctions conducted by the BCV.

29. **The efficiency of the banking sector in Cape Verde needs to be further improved.** Efficiency may be improved by introducing new financial instruments on both the demand and the supply side and by increasing the rate of transformation. Efficient intermediation has been hampered by several factors: (i) lack of competition in the banking system does not encourage development of new instruments; (ii) high commercial lending rates further repress credit to the private sector, especially to small and medium enterprises; (iii) high unremunerated reserve requirements (recently reduced from 19 to 18 percent), which are, in fact, implicit taxes on commercial banks, have been draining liquidity out of the banking system; and (iv) shortages of foreign exchange have hampered funding for imports.

30. **Efficiency of the banking sector could be enhanced by supporting improvements in lending practices and providing credit information.** To facilitate a more accurate assessment of repayment probability and better allocation of credit, commercial banks participate in the central risk system (Central de Riscos), that was developed and is maintained by the BCV. This system contains credit information, provided to the BCV on a monthly basis, and the banks receive consolidated reports. At present, there is a one-month

lag before the information becomes available to the banking system, but on-line “real-time” system is being developed, which will facilitate faster access to the information.

VIII. CHALLENGES AHEAD

31. **The financial sector in Cape Verde needs to be further developed to function as an engine of growth.** Recent success at macroeconomic and financial sector stabilization is a prerequisite for the deepening of the financial markets. However, the financial sector in Cape Verde continues to be characterized by the high weight of the banking sector and poor diversification of activities and financial instruments, which constrains the development of financial intermediation. Additional measures are needed to improve the financial sector, including (i) further development of the liquidity market; (ii) strengthening of contract enforcement; (iii) development of domestic capital markets and new financial instruments, (iv) further development of microfinance initiatives; and (v) implementation of best international practices.

32. **Further development of the interbank market:** In addition to their function as collateral, government securities provide other crucial benefits to financial markets, by creating a yield curve as a reference rate for pricing credits by commercial banks, offering opportunities for investment diversification for financial and nonfinancial entities, including insurance companies and pension funds. The government may rationalize Treasury bills and develop a benchmark rate. Liquidity forecasting needs also to be improved. It would help to address issues of liquidity management and absorption of excess liquidity from the banking sector, since unless the BCV absorbs the excess liquidity, commercial banks have little incentive to trade with each other. Given the small size of the economy, it is difficult to establish a competitive money market. Cape Verde could consider the possibility of allowing entry of large corporations, insurance companies, and pension funds into the wholesale overnight market. Also, Cape Verde might consider the possibility of integrating its interbank money market with other African countries, whose local currency is pegged to the euro, such as Senegal.

33. **Strengthening of contract enforcement:** Credible credit enforcement could be achieved by accelerating the resolution of outstanding commercial banks' NPLs. The service of the office of centralization of credit risks has been improving. In 2005, the BCV will provide online access to this service for all credit institutions. This service would promote loan performance, facilitate risk analysis to be carried out upon request, and improve risk management. In addition, it would reduce the likelihood of loans being extended by any bank to current defaulters. With a credit risk system in place, loan classification regulations should be further tightened by requiring all banks to rate a client with the lowest classification assigned by any bank within the banking system. In this context other jurisdictional issues should be addressed, including bankruptcy law and regulations on seizing collaterals by banks.

34. **Development of domestic capital markets and new financial instruments:** The recent developments of pension schemes and insurance companies have highlighted the need

to develop the domestic capital market and new financial instruments, including bonds of medium and long-term maturities, that will cater to the new forms of savings. In particular, the pension funds generally invest a large proportion of funds in long-term instruments to match the risk, return, and maturity profiles of their liabilities. Those bonds could be issued by the government as well as corporates, including public enterprises and the utility company.³⁵ This would attract capital and create investment opportunities, because without access to a broad range of instruments in the domestic capital market, the market remains vulnerable to capital outflow, as investors seek profit opportunities overseas that match their needs.³⁶ Although there are ongoing efforts of the authorities to boost capital market activities, significant room remains for further improvement. The legal framework for a stock exchange, the Bolsa de Valores de Cabo Verde, was completed in 1999, although trading has yet to commence. The government recently appointed a new Board for the stock exchange, which is in the preparation to start trading. The corporate bond market and secondary market for government securities are established, but there are no transactions as of now.

35. **Microfinance development:** At present, CECV is the only commercial bank with a formal program in micro-finance. This micro-finance pilot project has been initiated by a U.S. NGO—CDI/VOCA—in 1997 within the context of the food aid program. It was transferred to CECV in 2001, and the bank has been managing the program since then. Micro credit has been gradually increasing because of favorable loan conditions. Loans are provided to solidarity groups, which solicit credit from the bank with a maximum time period of 8 months. Annual lending rates are on average 12 percent and the average maturity of loans is 8 months. The repayment rate of micro-finance loans was close 90 percent by end-2003. The amount of micro-credit has been gradually increasing, with the average level of loans reaching US\$5,395.8 by end-2003, which was 0.06 percent of total credit to the economy.

36. **Implementation of best international practices:** The authorities should follow best international practices in developing the legal framework for regulating the financial sector. Efforts to improve the legal framework for property rights, insolvency, creditor rights, and contract enforcement should also be included in the financial sector reform. The regulations and legislation for the offshore banking sector should follow best international practices from its early stages of development.

³⁵ Instead of borrowing from the banks in form of loans, big enterprises could issue paper and sell them in the domestic market, which has a number of advantages. Bonds of public utilities companies are popular instruments in a number of countries.

³⁶ The residents of Cape Verde are allowed to purchase shares, other securities, bonds, and other debt securities abroad; however, they must be effected through the stock market or authorized dealers. Insurance companies in Cape Verde are not allowed to invest abroad.

IX. CONCLUSIONS

37. **Cape Verde faces some typical issues of a small, open, and rapidly developing economy**, such as a shallow domestic capital market, a limited interbank market with few players, lack of available financial instruments, a tendency for institutions to be all either in surplus or shortage of funds at the same time, and a tendency for investors to hold securities until maturity because of lack of investment alternatives. The financial sector is important in the authorities' efforts to diversify the economy and boost economic growth. The authorities promote financial sector development by following best international practices, such as new financial services and legal regulations.

38. **Further efforts are needed to improve the money market and to expedite the development of the domestic capital market.** Interest rates in Cape Verde are high and do not necessarily accurately mirror liquidity conditions. Also, despite excess liquidity in the banking sector, intermediation spreads have been widening. Policies at promoting banking competition and attracting non-banking financial institutions could encourage better pricing of financial services and instruments.

39. **Insurance and pensions need to be promoted further.** In view of the weak social security system in the private sector, life insurance could play a supporting role as a social safety net.

40. **A financial system with a more active non-banking financial sector and domestic capital market will require a more comprehensive regulatory and supervisory framework to maintain its integrity.** Regulatory reform has played a crucial role in the recent economic growth. Financial supervision and regulations should be further strengthened to improve regulatory capacity and administrative arrangements. The regulatory framework needs to ensure that the business environment is appropriate, while protecting against any risk to reputation that may arise from weak regulation.

The Structure of the Financial System in Cape Verde

41. **Cape Verde's banking system has undergone a fundamental transition from a state-owned mono-banking system to a privatized two-tier banking system.** In 1993, the former mono-bank Banco de Cabo Verde (BCV) was effectively transformed into a central bank. Also in 1993, Banco Comercial do Atlântico (BCA) was created as a private commercial bank with public ownership, followed by Caixa Economica de Cabo Verde (CECV). In 1995, Banco Totta e Açores (BTA) from Portugal was allowed to operate branches in Cape Verde (Banco Totta de Cabo Verde, BTCV), and in 1997, Banco Interatlântico (BIA) was created by Portugal's Caixa Geral de Depositos and private Cape Verdean investors. In 1999, BCA and CECV were privatized, with the State of Cape Verde retaining a substantial minority share of 35.4 percent in BCA and 15.7 percent in CECV. In early 2005, BTCV was acquired by a group of private Cape Verdean investors and became the first domestic private bank, Banco Caboverdiano de Negócios (BCN).

42. **To strengthen the BCV's independence, the Cape Verdean authorities have revised the central bank organic law (CBOL).** The new CBOL³⁷ was approved by the National Assembly on July 15, 2002. The new CBOL has been designed to maximize the BCV's independence within the framework of the Constitution of Cape Verde. Article 92 of the Constitution stipulates that the "Bank of Cape Verde ... collaborates in the definition of the Government's monetary and foreign exchange policy, and implements these autonomously." Since this article does not allow for full and complete independence of the BCV, the new CBOL has been designed so as to commit the central bank to price stability as its primary objective in pursuing its tasks, making the most of the scope given by the Constitution.³⁸

43. **At present, financial assets in Cape Verde's economy represent almost 85 percent of GDP, of which more than 87 percent comes from the commercial banks.** By December 2004, the financial system in Cape Verde was comprised of a central bank (Bank of Cape Verde, BCV), four commercial banks,³⁹ three off-shore banks, two insurance companies, and five nonbanking financial institutions (two exchange bureaus, one society of risk capital, one venture company, and one credit card issuing and managing company).

³⁷ Lei no 10/IV/2002.

³⁸ Clearly, the revision of the Article 92 of the Constitution would be necessary to implement full independence of the BCV. In the short term, however, a change in the Constitution does not appear to be politically feasible.

³⁹ Four commercial banks include Banco Comercial do Atlântico (BCA), Caixa Economica de Cabo Verde (CECV), Banco Interatlântico (BIA), and Banco Totta de Cabo Verde (BTCV). Banking services are provided on all islands through 35 branches of commercial banks.

Three commercial banks in Cape Verde are subsidiaries of foreign banks.⁴⁰ The fourth bank, BTCV, was a branch of Portuguese bank, and was recently acquired by a group of private domestic investors, becoming the first private domestic bank. Off-shore banking is in its early stage of development in Cape Verde with two new off-shore banking institutions registered in 2004. A leasing company has been licensed but has not yet become operational. A stock exchange has been created but never become operational.

Table A1. Cape Verde: Financial System Structure (end of period)

	2003		2004 1/	
	Assets mln CVEsc	in percent of tot.assets	Assets mln CVEsc	in percent of tot.assets
Banks				
Foreign				
Banco Comercial do Atlântico (BCA)	40541.8	64.5	43277.6	62.8
Caixa Económica de Cabo Verde (CECV)	14866.4	23.7	17074.4	24.8
Banco Interatlântico (BIA)	5380.6	8.6	6597.0	9.6
Banco Totta Cabo Verde (BTCV)	2024.0	3.2	1974.1	2.9
Offshore banks				
Banco Fiduciário internacional (I.F.I.)	1493.4		36509.2	
Banco Insular (I.F.I)	14.7			
Nonbank institutions				
Investment companies				
Venture capital companies 2/				
Promotora - Sociedade de Capital de Risco	457.8			
Exchange bureau				
Cota Câmbios	32.2		21.1	
Others				
Sociedade Interbancária de Sist. Pagº. (SISP)	214.9		201.0	
Insurance companies				
Garantia	1313.0	58.9		
Impar	915.5	41.1		

Source: Bank of Cape Verde

1/ provisional data

2/ Promotora - Sociedade de Capital de Risco

⁴⁰ BCA and BIA are subsidiaries of the same state-owned bank in Portugal, Caixa Geral de Depositors. CECV is a subsidiary of two Portuguese banks, Caixa Economica Montapio Geral and Montepio Geral-Assoçiação Multulista.

44. **Insurance companies are a potential source of long-term funds.** However, the life insurance market in Cape Verde is limited, and life insurance is undeveloped. The major activity of insurance companies consists of providing mandatory automobile insurance, which operates with short-term financial horizons and provides little if any long-term capital to the market.

45. **There are two main pension schemes for formal sector workers covering one quarter of the formal labor force.** One of these schemes is a pay-as-you-go system and does not have large amount of long-term resources available for investment. The other pension scheme, Instituto Nacional de Previdencia Social (INPS), was created in 1983 as a defined benefit plan, and is very young demographically. In 2002, there were 18 contributors for each old-age-pension beneficiary and 10 for each pension recipient (including those on invalidity and survivors' benefits).⁴¹ The INPS has been running a surplus and has accumulated a substantial reserve of assets. Nonetheless, pension expenditures under the scheme face three pressures which will have a profound impact in the short- and medium-term: (i) the natural maturing of the INPS, (ii) demographic change (longer life expectancy) resulting in population "ageing," and (iii) exceptionally generous benefit promises.

⁴¹ Mature pension systems in Europe have only two to three contributors for each beneficiary.

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Table 1. Cape Verde: Selected Economic and Financial Indicators, 1999–2003

	1999	2000	2001	2002	2003
	(Annual percentage change)				
National income and prices					
Real GDP	8.9	7.3	6.2	5.0	5.3
Real GDP (per capita)	7.1	3.8	4.3	3.1	3.4
Consumer price index (annual average)	4.4	-2.4	3.8	1.8	1.2
Consumer price index (end of period)	-1.5	-1.0	4.6	3.0	-2.3
External sector					
Exports (in euros) 1/	16.4	28.7	17.5	10.5	8.9
Imports (in euros) 1/	21.5	7.6	9.2	13.8	5.1
Real effective exchange rate (annual average)	8.4	-7.4	0.2	2.6	3.4
Terms of trade (minus = deterioration)	-4.8	-5.1	0.5	-0.9	1.8
Government budget					
Total revenue (excluding grants)	22.3	3.5	12.1	12.3	5.1
Total expenditure	28.5	19.5	-25.4	12.2	-1.2
Recurrent expenditure	29.3	48.4	-31.2	3.0	6.4
Capital expenditure and net lending	8.9	-8.3	-9.6	27.8	-18.0
	(Annual change in percent of beginning-of-period broad money)				
Money and credit 2/					
Net domestic assets	7.3	15.5	4.0	10.5	10.3
<i>Of which:</i> net claims on the central government	-20.9	11.1	0.1	5.9	0.9
credit to the economy	7.6	1.6	7.1	5.9	7.3
Broad money	15.4	12.9	9.8	14.3	8.6
Income velocity (GDP/M2)	1.74	8.7	3.4	10.3	4.2
Discount rate 3/	8.5	1.64	1.59	1.49	1.46
	(In percent of GDP)				
Saving-investment balance					
Gross domestic investment	19.8	19.7	18.3	21.4	18.2
Public	7.4	6.3	5.2	6.2	4.7
Private	12.4	13.5	13.1	15.2	13.5
Gross national savings	6.9	8.5	8.4	10.4	9.0
<i>Of which:</i> public sector	1.8	-7.0	5.4	9.6	5.4
External current account (including official transfers)	-12.9	-11.2	-9.9	-11.0	-9.2
Government budget					
Total revenue (including grants)	27.8	20.5	21.0	22.1	21.3
Total grants	7.3	6.0	5.8	8.4	5.3
Total expenditure	40.8	46.1	31.4	33.0	29.9
Overall balance after grants	-13.0	-19.5	-4.6	-2.5	-3.2
Domestic bank financing	1.3	8.1	0.1	3.6	1.1
Domestic public debt, net 4/	20.1	91.1	91.2	84.5	73.7
External current account (excluding official transfers)	-17.3	-15.3	-13.6	-16.5	-14.5
Overall balance of payments	7.0	-7.3	2.7	3.6	-0.6
Total external public debt (end of year; including arrears and Fund credit)	53.8	59.5	62.4	54.4	44.9
	(In millions of U.S. dollars, unless otherwise specified)				
External current account (after grants)	-74.9	-65.7	-63.6	-75.4	-63.8
Gross international reserves (end of period)	43.5	30.4	47.5	76.1	74.1
Gross international reserves (in months					
of imports of goods and services)	1.5	1	1.5	2.0	1.9
External debt service (in percent of exports					
of goods and nonfactor services)	30.2	10.8	19.2	15.6	10.6
Memorandum items:					
Nominal GDP (in billions of Cape Verde escudos)	59.8	64.5	70.6	75.5	82.3
Exchange rate (Cape Verde escudos per U.S. dollar)					
Period average	102.7	119.7	123.2	117.2	97.7

Sources: Cape Verde authorities; and staff estimates.

1/ Exports and imports of goods and nonfactor services.

2/ Reflects revised presentation consistent with the Central Bank of Cape Verde.

3/ Central bank lending rate; in percent.

4/ Excluding the claims on the offshore Trust Fund.

Table 2. Cape Verde: Selected Social and Demographic Indicators, 1999–2003
(In units as indicated)

	1999	2000	2001	2002	2003
GDP per capita (in current U.S. dollars)	1379.3	1221.6	1282.8	1405.1	1768.3
GDP per capita (constant 1995 U. S. dollar)	1482.0	1537.9	1574.3	1600.4	1638.7
GDP per capita, PPP (constant 1995 international dollar)	4348.2	4540.1	4603.1	4710.7	4826.0
Population					
Total (thousand)	423	435	446	458	470
Growth rate (percent a year)	2.6	2.8	2.5	2.7	2.6
Urban population (percent of total)	52.4	53.3	54.2	55.0	55.9
Life expectancy at birth, total (years)	..	68.8	..	69.1	..
Male	..	66.0	..	66.3	..
Female	..	71.7	..	72.0	..
Mortality rate, infant (per 1,000 live births)	..	30	..	29	..
Death rate, crude (per 1,000 people)	..	5.7	..	5.2	..
Birth rate, crude (per 1,000 people)	..	33.6	..	30.1	..
Fertility rate, total (births per woman)	..	3.7	..	3.5	..
Health					
Physicians (per 1,000 people)	4274	..	..	..	..
Hospital beds (per 1,000 people)	631	..	..	..	..
Immunization rate (percent of children ages 12–23 months)					
DPT	69	86	78	94	..
Measles	61	80	72	85	..
Improved water source (percent of population with access)	..	74	..	..	..
Rural (percent of rural population with access)	..	89	..	..	..
Urban (percent of urban population with access)	..	64	..	..	..
Education					
Literacy rate, adult total (percent of people ages 15 and above)	72.9	73.8	74.9	75.7	..
Male	83.2	84.5	84.9	85.4	..
Female	64.9	65.7	67.0	68.0	..
School enrollment, primary (percent net)	99.7	99.4	99.4	..	..
Pupil-teacher ratio, primary	28.7	28.2	28.8	..	..
Labor force, total (thousand)	172.3	179.0	185.4	192.4	199.4
Labor force, female (percent of total labor force)	38.9	38.9	38.9	38.8	38.8

Source: World Development Indicators; and Cape Verde authorities.

Table 3. Cape Verde: Sources and Uses of Resources, 1999–2003

	1999	2000	2001	2002	2003
(In millions of Cape Verde escudos; unless otherwise indicated)					
Gross domestic product (<i>Y</i>)	61,774	64,539	69,380	72,953	79,911
Percentage change	19.7	4.5	7.5	5.1	9.5
Current account (<i>CA</i>)	-7,680	-7,246	-7,016	-8,314	-7,539
Current account, excluding official transfers	-12,709	-9,859	-9,617	-12,473	-12,315
Resource balance (<i>X - M</i>)	-23,178	-22,047	-22,645	-26,431	-26,911
Exports of goods and nonfactor services	13,595	17,503	20,557	22,717	24,728
Imports of goods and nonfactor services	-36,773	-39,550	-43,203	-49,148	-51,640
Net factor income	-867	-1,366	-753	-1,364	-1,134
Public sector	-385.9	-558.5	-568.0	-556.8	-514.4
Private sector	-481	-807	-185	-808	-620
Unrequired transfers	16,366	16,167	16,382	19,482	20,507
Public sector	5,028.4	2,613.6	2,600.7	4,158.9	4,776.2
Private sector	11,337	13,554	13,781	15,323	15,730
Gross national product	60,906	63,173	68,627	71,588	78,777
Gross national income	77,272	79,340	85,009	91,070	99,283
Public sector					
Current revenue	12,794	13,238	14,542	16,437	16,972
Current expenditure 1/	16,054	21,627	14,863	15,530	17,038
Capital expenditure 1/	8,827	8,098	7,322	9,360	7,674
Gross domestic investment (<i>I</i>)	18,835	18,647	19,394	23,491	22,912
Fixed capital formation	18,835	18,647	19,394	23,491	22,912
Public sector 1/	4,414	4,049	3,661	4,680	3,837
Private sector	14,421	14,598	15,733	18,810	19,075
Change in stocks	...	...	...	...	...
Domestic consumption (<i>C</i>)	66,118	67,939	72,632	75,893	83,911
Public sector 1/	20,468	25,676	18,524	20,210	20,875
Private sector	45,650	42,262	54,108	55,683	63,035
Domestic saving (<i>Sd</i>)	-4,344	-3,400	-3,252	-2,941	-4,000
Public sector	-2,874	-7,830	246	1,463	448
Private sector	-1,470	4,430	-3,498	-4,404	-4,447
National saving	11,154	11,402	12,377	15,177	15,373
Public sector	1,090	-4,485	3,788	7,225	4,334
Of which: total external grants	4,350	3,903	4,110	6,319	4,400
Private sector	10,065	15,887	8,589	7,951	11,039

Table 3. Cape Verde: Sources and Uses of Resources, 1999–2003 (concluded)

	1999	2000	2001	2002	2003
	(In percent of GDP)				
Gross domestic product (<i>Y</i>)	100.0	100.0	100.0	100.0	100.0
Current account (<i>CA</i>)	-12.4	-11.2	-10.1	-11.4	-9.4
Current account, excluding official transfers	-20.6	-15.3	-13.9	-17.1	-15.4
Resource balance (<i>X - M</i>)	-37.5	-34.2	-32.6	-36.2	-33.7
Exports of goods and nonfactor services	22.0	27.1	29.6	31.1	30.9
Imports of goods and nonfactor services	-59.5	-61.3	-62.3	-67.4	-64.6
Net factor income	-1.4	-2.1	-1.1	-1.9	-1.4
Public sector	-0.6	-0.9	-0.8	-0.8	-0.6
Private sector	-0.8	-1.3	-0.3	-1.1	-0.8
Unrequired transfers	26.5	25.1	23.6	26.7	25.7
Public sector	8.1	4.0	3.7	5.7	6.0
Private sector	18.4	21.0	19.9	21.0	19.7
Gross national product	98.6	97.9	98.9	98.1	98.6
Gross national income	125.1	122.9	122.5	124.8	124.2
Public sector					
Current revenue	20.7	20.5	21.0	22.5	21.2
Current expenditure 1/	26.0	33.5	21.4	21.3	21.3
Capital expenditure 1/	14.3	12.5	10.6	12.8	9.6
Gross domestic investment (<i>I</i>)	30.5	28.9	28.0	32.2	28.7
Fixed capital formation	30.5	28.9	28.0	32.2	28.7
Public sector 1/	7.1	6.3	5.3	6.4	4.8
Private sector	23.3	22.6	22.7	25.8	23.9
Change in stocks	...	...	...	...	...
Domestic consumption (<i>C</i>)	107.0	105.3	104.7	104.0	105.0
Public sector 1/	33.1	39.8	26.7	27.7	26.1
Private sector	73.9	65.5	78.0	76.3	78.9
Domestic saving (<i>Sd</i>)	-7.0	-5.3	-4.7	-4.0	-5.0
Public sector	-4.7	-12.1	0.4	2.0	0.6
Private sector	-2.4	6.9	-5.0	-6.0	-5.6
National saving	18.1	17.7	17.8	20.8	19.2
Public sector	1.8	-7.0	5.5	9.9	5.4
<i>Of which:</i> total external grants	7.0	6.0	5.9	8.7	5.5
Private sector	16.3	24.6	12.4	10.9	13.8

Sources: National Institute of Statistics (INE); and staff estimates and projections.

1/ Assuming that 50 percent of capital expenditure, as classified by the treasury, is indeed current expenditures.

Table 4. Cape Verde: Gross Domestic Product at Current Prices, 1999–2003

	1999	2000	2001	2002	2003
Agriculture, forestry, and livestock	6,975	6,897	6,754	6,593	7,497
Fishing	1,412	1,432	1,184	940	1,212
Industry and energy	5,355	4,950	4,443	5,064	5,307
Construction	4,816	4,940	5,143	5,888	6,713
Commerce	10,958	11,495	12,018	13,554	15,683
Hotels	1,224	1,471	1,695	1,583	2,104
Transport and communications	11,741	12,820	15,977	14,902	14,844
Banks and insurance	3,043	2,542	3,054	3,262	3,473
House renting	3,281	3,369	3,726	4,062	4,214
Public service	8,269	8,717	8,761	9,237	10,306
Other services	1,345	1,450	1,518	1,526	1,649
Intermediary banking services 1/	-2,111	-1,766	-1,907	-2,209	-2,450
Sum of value added 2/	56,309	58,316	62,366	64,403	70,550
Taxes on imports	5,465	6,223	7,014	8,550	9,361
Gross domestic product at market prices	61,774	64,539	69,380	72,953	79,911
	(In percent of GDP)				
Agriculture, forestry, and livestock	11.3	10.7	9.7	9.0	9.4
Fishing	2.3	2.2	1.7	1.3	1.5
Industry and energy	8.7	7.7	6.4	6.9	6.6
Construction	7.8	7.7	7.4	8.1	8.4
Commerce	17.7	17.8	17.3	18.6	19.6
Hotels	2.0	2.3	2.4	2.2	2.6
Transport and communications	19.0	19.9	23.0	20.4	18.6
Banks and insurance	4.9	3.9	4.4	4.5	4.3
House renting	5.3	5.2	5.4	5.6	5.3
Public service	13.4	13.5	12.6	12.7	12.9
Other services 3/	7.6	9.2	9.5	10.8	10.7
Gross domestic product	100.0	100.0	100.0	100.0	100.0
	(Annual percentage change)				
Agriculture, forestry, and livestock	48.0	-1.1	-2.1	-2.4	13.7
Fishing	55.1	1.4	-17.3	-20.6	28.9
Industry and energy	7.5	-7.6	-10.2	14.0	4.8
Construction	13.6	2.6	4.1	14.5	14.0
Commerce	23.0	4.9	4.6	12.8	15.7
Hotels	5.2	20.2	15.2	-6.6	32.9
Transport and communications	15.8	9.2	24.6	-6.7	-0.4
Banks and insurance	-1.7	-16.5	20.1	6.8	6.4
House renting	16.3	2.7	10.6	9.0	3.7
Public service	13.7	5.4	0.5	5.4	11.6
Other services 3/	18.6	7.8	4.7	0.5	8.0
Intermediary banking services 1/	-12.3	-16.3	8.0	15.9	10.9
Sum of value added 2/	19.9	3.6	6.9	3.3	9.5
Taxes on imports	18.3	13.9	12.7	21.9	9.5
Gross domestic product at market prices	19.7	4.5	7.5	5.1	9.5
Memorandum items:					
Change in CPI	3.9	-2.4	3.8	1.8	1.2
Change in GDP deflator	10.9	-2.5	3.5	-0.8	4.5
Real GDP growth	8.8	7.0	4.0	5.9	5.0

Sources: National Institute of Statistics; and staff estimates.

1/ This amount represents the value of intermediary banking services used by other economic sectors; it has been globally netted out from the total value added, because it was not possible to do it for each sector. The amount is estimated by the interest received by the banking sector for the period.

2/ Includes indirect taxes, net of subsidies, with the exception of taxes on imports.

3/ Includes "Intermediary banking services" and "Taxes and duties on imports."

Table 5. Cape Verde: Gross Domestic Product by Major Sector at Constant 1980 Prices, 1999–2003

	1999	2000	2001	2002	2003
Agriculture, forestry, and livestock	1,744	1,759	1,759	1,723	1,758
Fishing	202	179	172	179	196
Industry and energy	1,463	1,604	1,684	1,785	1,887
Construction	1,583	1,500	1,455	1,521	1,607
Commerce	2,670	2,731	2,786	2,925	3,057
Hotels	927	1,158	1,250	1,307	1,437
Transport and communications	2,911	3,193	3,369	3,588	3,824
Banks and insurance	808	928	1,002	1,042	1,094
House renting	1,049	1,088	1,122	1,157	1,192
Public service	1,864	1,994	2,045	2,078	2,103
Other services 1/	432	496	506	516	557
Intermediary banking services 2/	-628	-720	-738	-760	-798
Sum of value added 3/	15,025	15,909	16,411	17,061	17,915
Taxes on imports	1,496	1,755	1,969	2,225	2,343
Gross domestic product at market prices	16,521	17,663	18,380	19,286	20,258
Agriculture, forestry, and livestock	10.6	10.0	9.6	8.9	9.8
Fishing	1.2	1.0	0.9	0.9	1.1
Industry and energy	8.9	9.1	9.2	9.3	10.5
Construction	9.6	8.5	7.9	7.9	9.0
Commerce	16.2	15.5	15.2	15.2	17.1
Hotels	5.6	6.6	6.8	6.8	8.0
Transport and communications	17.6	18.1	18.3	18.6	21.3
Banks and insurance	4.9	5.3	5.5	5.4	6.1
House renting	6.4	6.2	6.1	6.0	6.7
Public service	11.3	11.3	11.1	10.8	11.7
Other services 1/	7.9	8.7	9.4	10.3	-1.3
Gross domestic product at market prices	100.0	100.0	100.0	100.0	100.0
Agriculture, forestry, and livestock	12.8	0.9	0.0	-2.0	2.0
Fishing	-2.9	-11.3	-4.0	4.0	10.0
Industry and energy	3.3	9.6	5.0	6.0	5.7
Construction	7.3	-5.3	-3.0	4.6	5.6
Commerce	8.7	2.3	2.0	5.0	4.5
Hotels	17.5	25.0	8.0	4.5	10.0
Transport and communications	9.0	9.7	5.5	6.5	6.6
Banks and insurance	0.4	14.8	8.0	4.0	5.0
House renting	24.5	3.7	3.1	3.1	3.1
Public service	2.8	6.9	2.6	1.6	1.2
Other services 1/	4.9	14.7	2.0	2.0	8.0
Intermediary banking services 2/	2.0	14.7	2.5	3.0	5.0
Sum of value added 3/	8.7	5.9	3.2	4.0	5.0
Taxes on imports	10.0	17.3	12.2	13.0	5.3
Gross domestic product at market prices	8.8	6.9	4.1	4.9	5.0

Sources: National Institute of Statistics; and staff estimates.

1/ Includes "Intermediary banking services" and "Taxes and duties on imports."

2/ This amount represents the value of intermediary banking services used by other economic sectors; it has been globally netted out from the total value added, because it was not possible to do it for each sector. The amount is estimated by the interest received by the banking sector for the period.

3/ Includes indirect taxes, net of subsidies, with the exception of taxes on imports.

Table 6. Cape Verde: Consumer Prices, 1999–2003

	1999	2000	2001	2002	2003
	(Index: 1990 = 100)				
January	181.4	176.6	173.8	183.0	189.5
February	183.2	175.9	174.1	182.8	190.8
March	180.5	173.9	179.6	183.8	189.9
April	179.5	175.4	181.9	184.1	188.9
May	180.4	175.7	182.6	186.0	188.6
June	180.7	175.8	182.1	185.6	188.9
July	183.2	175.5	184.3	185.9	189.4
August	183.8	180.7	188.7	187.3	189.1
September	184.1	179.6	189.7	188.9	188.9
October	181.9	179.0	187.5	188.3	186.4
November	178.9	177.5	185.0	189.3	185.4
December	179.5	177.6	185.0	190.5	186.2
Average	181.4	176.9	182.8	186.3	188.5
	(Monthly percentage changes)				
January	-0.5	-1.6	-2.2	-1.1	-0.5
February	1.0	-0.4	0.2	-0.1	0.7
March	-1.5	-1.1	3.2	0.5	-0.5
April	-0.5	0.9	1.3	0.2	-0.5
May	0.5	0.2	0.4	1.0	-0.2
June	0.2	0.1	-0.2	-0.2	0.1
July	1.4	-0.2	1.2	0.2	0.3
August	0.3	3.0	2.4	0.7	-0.2
September	0.2	-0.6	0.5	0.9	-0.1
October	-1.2	-0.4	-1.1	-0.3	-1.3
November	-1.6	-0.8	-1.3	0.5	-0.6
December	0.3	0.1	0.0	0.7	0.4
Average	-0.1	-0.1	0.4	0.2	-0.2
	(Annual percentage changes)				
January	7.0	-2.7	-1.2	5.3	3.6
February	8.1	-4.0	-0.6	5.0	4.4
March	7.5	-3.6	3.3	1.7	3.4
April	6.2	-2.3	4.1	1.2	2.6
May	4.9	-2.6	4.3	1.9	1.4
June	5.3	-3.0	4.0	1.9	1.8
July	6.4	-4.2	5.2	0.9	1.9
August	4.5	-1.7	4.5	-0.7	0.9
September	3.1	-2.4	5.8	-0.4	0.0
October	1.6	-1.6	5.3	0.4	-1.0
November	-0.1	-0.8	4.6	2.3	-2.1
December	-1.6	-1.0	4.6	3.0	-2.3
Average	4.4	-2.5	3.7	1.9	1.2

Sources: National Institute of Statistics (INE).

Table 7. Cape Verde: Fiscal Operations of the Central Government, 1999–2003

	1999	2000	2001	2002	2003
(In billions of Cape Verde escudos)					
Revenue, grants, and net lending	17.1	17.1	18.9	23.0	21.9
Domestic revenue	12.8	13.2	14.8	16.7	17.5
Tax revenue	10.4	11.8	13.0	14.7	15.5
Income and profit taxes	3.2	3.9	4.8	5.1	5.3
Consumption taxes	1.8	1.9	2.1	2.5	2.5
International trade taxes	4.2	4.8	5.3	6.1	6.8
Other taxes	1.2	1.2	0.8	0.9	0.9
Nontax revenue	2.4	1.5	1.5	1.8	1.5
Fees and penalties	0.4	0.4	0.3	0.3	0.4
Other nontax revenues	1.4	1.1	0.6	0.6	0.9
Profit transfers	0.6	0.0	0.6	0.8	0.3
Domestic capital participation	0.0	0.0	0.0	0.0	0.0
External grants	4.3	3.9	4.1	6.3	4.4
Capital grants	4.3	3.9	4.1	5.2	3.6
Budget support	0.0	0.0	0.0	1.2	0.8
Net lending	0.0	0.0	0.3	0.2	0.0
Total expenditure	24.9	29.7	22.2	24.9	24.7
Recurrent expenditure	14.6	17.2	14.9	15.3	16.4
Primary current expenditure	13.8	15.8	13.4	13.3	14.4
Wages and salaries	6.0	6.4	6.6	7.1	9.4
Goods and services	0.7	0.5	0.6	0.6	1.3
Transfers and subsidies 1/	3.5	6.8	5.7	4.9	3.0
Other expenditures	3.6	2.1	0.5	0.7	0.8
Domestic interest payments	0.4	0.8	0.9	1.4	1.5
External interest payments	0.4	0.6	0.6	0.6	0.5
Extraordinary expenditures	1.5	4.5	0.0	0.2	0.6
Social emergency measures	1.5	0.0	0.0	0.0	0.0
Restructuring costs	0.0	4.4	0.0	0.2	0.6
Capital expenditure	8.8	8.1	7.3	9.4	7.7
Foreign financed	7.9	6.8	6.2	8.6	6.9
Domestically financed	1.0	1.3	1.1	0.7	0.8
Overall balance, including grants 2/	-7.7	-12.6	-3.2	-1.9	-2.8
Financing	8.3	13.0	3.0	1.9	3.0
Foreign (net)	3.6	3.4	2.1	1.1	2.0
Total drawings	7.3	2.4	7.6	4.1	4.1
Balance of payments, budget	2.3	0.0	5.1	1.3	1.3
Borrowings	0.7	0.0	1.8	0.0	0.0
Credit facility (FAC)	1.7	0.0	0.6	0.6	0.6
Other	0.0	0.0	2.7	0.8	0.8
Project loans	5.0	2.4	2.5	2.8	2.8
Amortization	-3.7	-1.3	-5.4	-3.0	-2.1
Bridge loans and Portuguese credit facility	-1.7	0.0	-2.3	-0.6	-1.1
Other	-2.1	-1.3	-3.2	-2.4	-1.0
Change in arrears	-0.8	2.3	-1.9	-0.8	0.0
Refinancing and rescheduling of arrears	0.8	0.0	1.9	0.8	0.0
Debt relief	0.0	0.0	0.0	0.0	0.0
Domestic (net)	4.7	9.6	0.9	0.8	1.0
Banking system 3/	0.1	5.2	0.1	2.7	0.9
Nonbanks	3.7	2.1	1.3	2.0	0.7
Domestic arrears	0.8	2.3	-0.5	-3.9	-0.6
Net errors and omissions	-0.6	-0.4	0.2	0.0	-0.2
Financing gap	0.0	0.0	0.0	0.0	0.0
Memorandum items:					
Overall balance, excluding grants 4/	-12.1	-16.5	-7.4	-8.2	-7.2
Primary current balance 5/	-1.0	-2.5	1.5	3.3	3.1
Primary balance 6/	-3.4	-8.3	0.3	2.4	1.7
Domestic balance 7/	-3.8	-9.2	-0.6	1.0	0.2

Table 7. Cape Verde: Fiscal Operations of the Central Government, 1999–2003 (concluded)

	1999	2000	2001	2002	2003
	(In percent of GDP)				
Revenue, grants, and net lending	27.8	26.6	27.3	31.5	27.4
Domestic revenue	20.7	20.5	21.4	22.8	21.9
Tax revenue	16.8	18.2	18.7	20.1	19.3
Income and profit taxes	5.2	6.1	6.9	7.0	6.6
Consumption taxes	2.9	2.9	3.0	3.4	3.1
International trade taxes	6.8	7.5	7.7	8.4	8.5
Other taxes	1.9	1.8	1.1	1.3	1.1
Nontax revenue	3.9	2.3	2.2	2.4	1.9
Fees and penalties	0.7	0.6	0.5	0.4	0.4
Other nontax revenues	2.2	1.7	0.8	0.8	1.1
Profit transfers	1.0	0.0	0.9	1.1	0.4
Domestic capital participation	0.0	0.0	0.0	0.0	0.0
External grants	7.0	6.0	5.9	8.7	5.5
Capital grants	7.0	6.0	5.9	7.1	4.5
Budget support	0.0	0.0	0.0	1.6	1.0
Net lending	0.0	0.0	0.4	0.3	0.0
Total expenditure	40.3	46.1	32.0	34.1	30.9
Recurrent expenditure	23.6	26.6	21.4	21.0	20.5
Primary current expenditure	22.3	24.5	19.3	18.2	18.0
Wages and salaries	9.7	9.9	9.5	9.7	11.7
Goods and services	1.1	0.7	0.8	0.8	1.7
Transfers and subsidies 1/	5.7	10.6	8.2	6.7	3.7
Other expenditures	5.8	3.2	0.7	1.0	1.0
Domestic interest payments	0.6	1.3	1.4	2.0	1.9
External interest payments	0.6	0.9	0.8	0.8	0.6
Extraordinary expenditures	2.4	6.9	0.0	0.3	0.8
Social emergency measures	2.4	0.0	0.0	0.0	0.0
Restructuring costs	0.0	6.9	0.0	0.3	0.8
Capital expenditure	14.3	12.5	10.6	12.8	9.6
Foreign financed	12.7	10.5	8.9	11.8	8.6
Domestically financed	1.6	2.0	1.6	1.0	1.0
Overall balance, including grants 2/	-12.5	-19.5	-4.7	-2.6	-3.5
Financing	13.4	20.1	4.3	2.6	3.8
Foreign (net)	5.9	5.2	3.0	1.6	2.5
Total drawings	11.9	3.8	10.9	5.7	5.1
Balance of payments, budget	3.8	0.0	7.3	1.8	1.7
Project loans	8.1	3.8	3.6	3.8	3.5
Amortization	-6.0	-2.1	-7.8	-4.1	-2.6
Bridge loans and Portuguese credit facility	-2.7	0.0	-3.3	-0.8	-1.4
Other	-3.3	-2.1	-4.6	-3.4	-1.3
Change in arrears	-1.3	3.5	-2.7	-1.1	0.0
Domestic (net)	7.6	14.8	1.3	1.0	1.3
Banking system	0.2	8.1	0.1	3.7	1.2
Nonbanks	6.1	3.2	1.9	2.7	0.9
Domestic arrears	1.3	3.5	-0.7	-5.4	-0.7
Net errors and omissions	-0.9	-0.6	0.4	0.0	-0.3
Financing gap	0.0	0.0	0.0	0.0	0.0
Memorandum items:					
Overall balance, excluding grants 4/	-19.6	-25.5	-10.6	-11.3	-9.0
Primary current balance 5/	-1.6	-3.9	2.1	4.6	3.9
Primary balance 6/	-5.6	-12.9	0.5	3.3	2.1
Domestic balance 7/	-6.2	-14.2	-0.9	1.3	0.3

Sources: Ministry of Finance and Planning; Bank of Cape Verde; and staff estimates.

1/ Includes student scholarships.

2/ Overall balance, incl. grants = revenue, incl. grants - total expenditure.

3/ Due to TCMF operations, bank financing in 1999 and 2000 does not match change in banking systems' net credit to central government.

4/ Overall balance, excl. grants = revenue, excl. grants - total expenditure.

5/ Primary current balance = domestic revenue - primary current expenditure.

6/ Primary balance = domestic revenue - total expenditure + domestic and external interest payments.

7/ Domestic balance = domestic revenue - recurrent expenditure + external interest payments - extraordinary expenditures - domestically financed capital expenditure.

Table 8. Cape Verde: Central Government Revenue, 1999–2003

(In millions of Cape Verde escudos, unless otherwise indicated)

	1999	2000	2001	2002	2003
Tax revenue	10,384	11,761	12,988	14,678	15,457
Direct taxes	3,203	3,908	4,788	5,132	5,304
Unified tax on income and profits	3,203	3,908	4,788	5,132	5,304
Other direct taxes	0	0	0	0	0
Indirect taxes	7,181	7,853	8,199	9,546	10,153
Taxes on international trade	4,175	4,808	5,341	6,127	6,755
Import duties	2,838	3,255	3,705	4,042	4,330
Customs services fee	1,301	1,440	1,624	2,072	2,412
Other taxes	37	113	11	13	13
Consumption taxes	1,805	1,889	2,099	2,470	2,500
Domestic goods and services	112	164	63	108	100
International goods and services 1/	1,348	1,527	1,712	1,798	1,934
Tax on petroleum products	175	28	122	315	218
Liquor tax	106	110	105	125	126
Tourism tax	64	60	98	124	122
Municipal taxes 2/	117	136	68	113	83
Ecological tax	40	47	68	113	83
Other municipal taxes	78	89	0	0	0
Other indirect taxes	1,084	1,020	691	836	815
Stamp tax	579	583	591	723	678
Other	505	437	100	114	137
Nontax revenue	2,410	1,477	1,543	1,759	1,514
Fees and penalties	409	369	339	320	355
Property income	636	10	645	832	294
Transfers	647	587	384	294	436
Sales of fixed assets and services	198	201	153	154	149
Autonomous revenues 3/	502	300	0	0	0
Other revenues	18	11	22	158	281
Total budgetary revenue 4/	12,794	13,238	14,834	16,658	17,509
Annual percent change	26.8	3.5	12.1	12.3	5.1

Source: Ministry of Finance and Planning.

1/ Collected by the customs department on imports.

2/ In 1998, municipal taxes were collected by the central government and directly passed on to the municipalities.

3/ These are called *contas de ordem*, which are revenue as budgeted from the direct provision of services by government agencies, offset by the same amounts of current expenditure for each of these agencies.

4/ Excludes revenue from domestic capital participation and net lending.

Table 9. Cape Verde: Selected Indicators of Central Government Revenue, 1999–2003

	1999	2000	2001	2002	2003
(In millions of Cape Verde escudos)					
Tax revenue	10,384	11,761	12,988	14,678	15,457
<i>Of which:</i> taxes on income and profits	3,203	3,908	4,788	5,132	5,304
taxes on international trade	4,175	4,808	5,341	6,127	6,755
consumption taxes	1,805	1,889	2,099	2,470	2,500
Nontax revenue	2,410	1,477	1,543	1,759	1,514
<i>Of which:</i> property income	636	10	645	832	294
transfers	647	587	384	294	436
sale of fixed assets	198	201	153	154	149
(As percent of budgetary revenue)					
Tax revenue	81.2	88.8	87.6	88.1	88.3
<i>Of which:</i> taxes on income and profits	25.0	29.5	32.3	30.8	30.3
taxes on international trade	32.6	36.3	36.0	36.8	38.6
consumption taxes	14.1	14.3	14.2	14.8	14.3
Nontax revenue	18.8	11.2	10.4	10.6	8.6
<i>Of which:</i> property income	5.0	0.1	4.4	5.0	1.7
transfers	5.1	4.4	2.6	1.8	2.5
sale of fixed assets	1.6	1.5	1.0	0.9	0.8
(Annual percentage change)					
Tax revenue	22.3	13.3	10.4	13.0	5.3
<i>Of which:</i> taxes on income and profits	12.9	22.0	22.5	7.2	3.4
taxes on international trade	20.7	15.2	11.1	14.7	10.3
consumption taxes	7.8	4.7	11.1	17.7	1.2
Nontax revenue	50.4	-38.7	4.4	14.0	-13.9
<i>Of which:</i> property income	48.5	-98.4	6,120.6	28.9	-64.7
transfers	149.5	-9.3	-34.6	-23.4	48.1
sale of fixed assets	-29.2	1.2	-23.8	1.0	-3.7
(In percent of GDP)					
Tax revenue	16.8	18.2	18.7	20.1	19.3
<i>Of which:</i> taxes on income and profits	5.2	6.1	6.9	7.0	6.6
taxes on international trade	6.8	7.5	7.7	8.4	8.5
consumption taxes	2.9	2.9	3.0	3.4	3.1
Nontax revenue	3.9	2.3	2.2	2.4	1.9
<i>Of which:</i> property income	1.0	0.0	0.9	1.1	0.4
transfers	1.0	0.9	0.6	0.4	0.5
sale of fixed assets	0.3	0.3	0.2	0.2	0.2

Sources: Ministry of Finance and Planning; and staff estimates.

1/ In 1993 the tax on the fuel distributor's profits and capital distributions was replaced by the tax on petroleum products.

2/ Collected by the customs departments on imports.

3/ On government-guaranteed external borrowing.

4/ These are the so called *contas de ordem*, which are revenue as budgeted from the direct provision of services by government agencies offset by the same amounts of current expenditure for each of these agencies.

5/ As of 1998, municipal taxes were collected by the central government and directly passed on to the municipalities. Therefore, they are not considered in the "tax revenue" row.

Table 10. Cape Verde: Economic Classification of Central Government Expenditure, 1999–2003

	1999	2000	2001	2002	2003
(In millions of Cape Verde escudos)					
Total expenditure	29,726	22,185	24,890	24,890	24,712
Recurrent expenditure	17,167	14,863	15,305	15,305	16,408
Wages and salaries	6,412	6,577	7,092	7,092	1,951
Goods and services	474	566	604	604	202
Interest on public debt	1,383	1,505	1,994	1,994	1,995
Domestic 1/	824	937	1,437	1,437	1,480
External 2/	558	568	557	557	514
Subsidies and transfers	6,837	5,717	4,889	4,889	2,969
Public enterprises	0	0	0	0	0
Public sector	3,864	4,041	4,199	4,199	2,334
Other entities	2,973	1,677	690	690	634
Other current expenditure	2,061	498	726	726	765
<i>Of which: autonomous expenditure 3/</i>	300	300	0	0	0
Capital expenditure 4/	8,098	7,322	9,360	9,360	7,674
Foreign financing	6,777	6,189	8,638	8,638	6,912
Grants	3,903	4,110	6,319	6,319	4,400
Loans	2,873	2,080	2,319	2,319	2,512
Domestic resources	1,322	1,132	723	723	762
(In percent of recurrent expenditure)					
Recurrent expenditure	100.0	100.0	100.0	100.0	100.0
Wages and salaries	37.4	44.3	46.3	46.3	11.9
Goods and services	2.8	3.8	3.9	3.9	1.2
Interest on public debt	8.1	10.1	13.0	13.0	12.2
Domestic 1/	4.8	6.3	9.4	9.4	9.0
External 2/	3.3	3.8	3.6	3.6	3.1
Subsidies and transfers	39.8	38.5	31.9	31.9	18.1
Public enterprises	0.0	0.0	0.0	0.0	0.0
Public sector	22.5	27.2	27.4	27.4	14.2
Other entities	17.3	11.3	4.5	4.5	3.9
Other current expenditure	12.0	3.4	4.7	4.7	4.7
<i>Of which: autonomous expenditure 3/</i>	1.7	2.0	0.0	0.0	0.0
(In percent of GDP)					
Recurrent expenditure	100.0	100.0	100.0	100.0	100.0
Wages and salaries	37.4	44.3	46.3	46.3	11.9
Goods and services	2.8	3.8	3.9	3.9	1.2
Interest on public debt	8.1	10.1	13.0	13.0	12.2
Domestic 1/	4.8	6.3	9.4	9.4	9.0
External 2/	3.3	3.8	3.6	3.6	3.1
Subsidies and transfers	39.8	38.5	31.9	31.9	18.1
Public enterprises	0.0	0.0	0.0	0.0	0.0
Public sector	22.5	27.2	27.4	27.4	14.2
Other entities	17.3	11.3	4.5	4.5	3.9
Other current expenditure	12.0	3.4	4.7	4.7	4.7
<i>Of which: autonomous expenditure 3/</i>	1.7	2.0	0.0	0.0	0.0

Sources: Ministry of Finance and Planning; and staff estimates.

1/ Including the debt service to the central bank and the Instituto Nacional de Previdencia Social (INPS).

2/ Including central government and public enterprises' debt guaranteed by the central government.

3/ These are called *contas de ordem*, which are revenue as budgeted from the direct provision of services by government agencies, offset by the same amounts of current expenditure for each of these agencies.

4/ In 1999, capital expenditures include social emergency expenditures.

Table 11. Cape Verde: Public Domestic Debt of Central Government, 1999–2003

(In millions of Cape Verde escudos)

	1999	2000	2001	2002	2003
Stock of domestic debt, incl. claims on Trust Fund (TCMFs)	24,714	31,555	31,653	34,616	34,959
TCMFs	11,188	11,188	11,188	11,188	11,188
Stock of domestic public debt	13,526	20,366	20,465	23,428	23,771
Banking sector	9,038	12,973	13,268	16,422	15,903
Bank of Cape Verde	5,865	5,043	4,547	5,590	4,776
Banco Comercial do Atlântico	894	4,597	5,131	6,521	7,253
Caixa Económica de Cabo Verde	1,166	2,039	2,200	1,981	1,331
Banco Totta e Açores	376	275	460	963	887
Caixa Geral de Depositos	738	1,020	930	1,368	1,656
Nonbanking sector	2,990	3,618	3,936	5,933	6,342
INPS 1/	2,085	2,431	2,584	5,295	5,571
Garantia	182	170	125	128	145
Other	723	1,017	1,227	511	626

Sources: Ministry of Finance and Planning; Bank of Cape Verde; and staff estimates.

1/ Instituto Nacional de Previdencia Social (INPS).

Table 12. Cape Verde: Monetary Survey, 1999–2003

	1999	2000	2001	2002	2003
(In millions Cape Verdean Escudos, unless otherwise indicated)					
Net foreign assets	8,110	7,139	10,002	11,331	10,456
Foreign assets	9,899	9,244	11,934	13,841	13,434
<i>Of which:</i> foreign reserves	4,678	3,349	5,684	8,391	8,173
Foreign liabilities	-1,789	-2,104	-1,932	-2,511	-2,978
Net domestic assets	28,740	34,561	35,823	41,027	46,428
Net domestic credit	32,885	41,184	44,119	49,914	54,503
Net claims on general government	13,978	21,702	21,692	24,790	25,561
Claims on the Trust Fund (TCFMs) 1/	6,803	10,600	10,600	10,600	11,038
Net claims on the central government	6,775	10,678	10,589	13,922	14,858
Credit to central government	8,906	12,973	13,139	16,546	17,097
Deposits of central government	-2,132	-2,295	-2,550	-2,624	-2,239
<i>Of which:</i> project deposits	-410	-211	-331	-397	-393
Net claims on local government	81	-57	3	8	67
Net claims on other government agencies (INPS)	-422	-466	-614	-186	-402
Credit to the economy	18,888	19,317	22,258	25,120	28,906
Credit to public enterprises	512	115	215	230	180
Credit to private sector	18,377	19,202	22,043	24,890	28,726
Claims on nonbank financial institutions	0	0	7	6	37
Other items (net)	-4,244	-6,539	-8,093	-8,889	-8,075
Broad money (M2)	36,629	41,483	45,604	52,357	56,884
Narrow money (M1)	18,307	20,131	20,759	22,620	22,989
Currency in circulation	6,026	6,458	6,703	6,459	6,516
Demand deposits	12,281	13,673	14,056	16,161	16,474
Quasi money	18,322	21,352	24,844	29,737	33,895
Time deposits	17,691	20,793	24,026	28,119	32,414
Other quasi-monetary deposits	631	559	819	1,618	1,480
Foreign currency deposits	2,110	2,198	2,106	2,101	2,232
(Change in percent of broad money 12 months earlier)					
Net foreign assets	7.9	-2.6	5.8	3.9	-1.7
Net domestic assets	7.6	15.5	4.0	10.5	10.3
Net domestic credit	10.4	22.5	7.0	12.7	8.8
Net claims on the central government	-20.9	11.1	0.1	5.9	0.9
Credit to the economy	7.6	1.6	7.1	5.9	7.3
Credit to public enterprises	1.5	-1.0	0.1	0.0	-0.1
Credit to private sector	6.1	2.5	6.9	5.9	7.3
Valuation	0.0	0.0	0.0	0.0	0.0
Other items (net)	-2.8	-7.0	-2.9	-2.3	1.6
Broad money	15.4	12.9	9.8	14.3	8.6
Narrow money	9.2	4.7	1.5	4.1	0.7
Currency outside banks	3.0	1.2	0.6	-0.5	0.1
Demand deposits	6.2	3.5	0.9	4.6	0.6
Time and savings deposits	5.0	7.4	8.9	8.9	7.9
Foreign currency deposits	1.5	0.2	-0.2	0.0	0.3
(In units as indicated)					
Selected monetary indicators					
Reserve ratio	0.18	0.18	0.18	0.18	0.19
Excess reserves/total deposits	-0.01	-0.004	-0.004	0.005	0.001
Vault cash/total deposits	0.02	0.02	0.02	0.02	0.02
Global FX coverage of potential FX liabilities	0.42	0.25	0.32	0.42	0.35
Money multiplier (broad money/reserve money)	3.16	3.08	3.14	3.22	3.29

Sources: Bank of Cape Verde; and staff estimates.

1/ Títulos Consolidados de Mobilização Financeira.

Table 13. Cape Verde: Summary Accounts of the Bank of Cape Verde, 1999–2003

	1999	2000	2001	2002	2003
(In millions of Cape Verdean Escudos, unless otherwise indicated)					
Net foreign assets	6,476	4,053	5,945	8,632	8,088
<i>Of which:</i> net international reserves	4,590	3,221	5,100	7,984	7,528
Foreign assets	6,596	4,212	6,115	9,135	8,818
International reserves	4,678	3,349	5,238	8,391	8,173
Non reserve assets	1,918	864	877	744	645
Foreign liabilities	-120	-160	-170	-503	-730
Short-term foreign liabilities	-88	-128	-138	-407	-645
Medium- and long-term foreign liabilities	-32	-32	-32	-96	-85
Net domestic assets	5,225	9,499	8,635	7,605	9,201
Net domestic credit	6,552	10,867	9,976	9,728	10,651
TCMFs 1/	0	4,167	4,167	4,167	4,605
Net claims on central government	5,027	4,444	4,183	4,103	4,424
Credit to central government	5,865	5,043	4,857	5,302	5,373
Deposits of central government	-838	-598	-675	-1,199	-948
<i>Of which:</i> project account	-410	-211	-331	-397	-393
foreign currency deposits	-291	-272	-256	-330	-456
Claims on local government	0	0	0	0	0
Credit to the economy	1,193	1,157	1,189	1,184	1,212
Credit to public enterprises	87	82	82	72	72
Credit to private sector	1,101	1,075	1,106	1,112	1,107
Claims on nonbank financial institutions	6	0	0	0	33
Credit to commercial banks	331	1,099	438	275	410
Valuation	0	0	0	0	0
Other items (net)	-1,326	-1,368	-1,341	-2,123	-1,451
Assets	2,194	2,276	2,616	2,345	2,396
Liabilities	3,520	3,644	3,957	4,468	3,847
Reserve money	11,701	13,552	14,581	16,237	17,289
Currency outside banks	6,026	6,458	6,703	6,459	6,516
Cash in vaults	630	597	650	1,013	808
Deposits of commercial banks	4,955	6,496	7,227	8,764	9,964
Deposits of private sector	0	0	0	0.0	0.0
Deposits of other financial institutions	90	1	1	1	0
Deposits of public sector (local govt. and PSE)	0.0	0.0	0.0	0.0	0.0
(12-month percentage change)					
Reserve money	6.7	15.8	7.6	11.36	6.5
Net foreign assets	27.2	-20.7	14.0	18.43	-3.4
Net domestic assets	-20.5	36.5	-6.4	-7.07	9.8
Net domestic credit	0.3	36.9	-6.6	-1.70	5.7
Claims on the govt.	0.2	-5.0	-1.9	-0.55	2.0
Credit to the economy	0.4	-0.3	0.2	-0.03	0.2
Credit to banks	-0.3	6.6	-4.9	-1.12	0.8
Other items (net)	-20.8	-0.4	0.2	-5.37	4.1

Sources: Bank of Cape Verde; and staff estimates.

1/ Titulos Consolidados de Mobilização Financeira.

Table 14. Cape Verde: Summary Accounts of the Commercial Banks, 1999–2003

(In millions of Cape Verde escudos, unless otherwise specified)

	1999	2000	2001	2002	2003
Net foreign assets	1,634	3,086	3,612	2,699	2,368
Foreign assets	3,304	5,031	5,374	4,706	4,616
Foreign liabilities	-1,670	-1,945	-1,762	-2,007	-2,248
Net domestic assets	29,106	32,155	35,511	43,198	48,000
Net domestic credit	31,919	37,410	42,021	49,962	54,625
Net claims on general government	8,951	13,091	13,343	16,519	16,531
TCMFs 1/	6,803	6,433	6,433	6,433	6,433
Other government deposits: INPS 2/	-422	-466	-614	-186	-402
Net claims on central government	2,489	3,714	7,523	10,265	10,433
Loans and overdrafts	1,085	1,590	5,513	6,704	7,302
Holding of government securities	2,148	2,983	3,015	4,540	4,423
Deposits of central government	-744	-859	-1,005	-979	-1,291
Net claims on local government	81	-57	3	8	67
Claims on local government	238	289	261	266	239
Deposits of local government	-158	-347	-258	-259	-172
Credit to the economy	17,715	18,326	21,239	23,941	27,731
Credit to public enterprises	425	73	133	158	108
Credit to private sector	17,289	18,252	21,099	23,778	27,619
Claims on nonbank financial institutions	0	0	7	6	4
Net claims on the Bank of Cape Verde	5,254	5,994	7,438	9,502	10,363
Total reserves	5,585	7,093	7,877	9,777	10,772
Vault cash	630	597	650	1,013	808
Deposits with central bank	4,955	6,496	7,227	8,764	9,964
Required reserves	4,970	5,784	6,493	7,825	8,529
Excess reserves	-14	712	734	939	1,435
Credit from the Bank of Cape Verde	-331	-1,099	-438	-275	-410
Other items (net)	-2,813	-5,256	-6,510	-6,765	-6,625
Deposit liabilities to nonbank residents	30,740	35,241	39,122	45,896	50,367
Local currency deposits	28,629	33,043	37,017	43,795	48,135
Demand deposits	12,191	13,672	14,056	16,159	16,473
Of which: emigrant deposits	1,055	1,387	1,765	2,133	2,202
Quasi-money	16,439	19,371	22,961	27,636	31,662
Time deposits	15,349	18,081	21,802	25,857	29,983
Of which: emigrant deposits	8,002	10,015	12,672	15,817	18,918
Other quasi-monetary deposits	1,090	1,290	1,160	1,779	1,480
Foreign currency deposits	2,110	2,198	2,106	2,101	2,232
Of which: emigrant deposits	1,002	1,075	1,148	1,092	1,033
Memorandum item:					
Emigrant deposits (as share of total deposits)	0.27	0.30	0.34	0.36	0.39
Other deposits (in percent of total deposits)	0.73	0.70	0.66	0.64	0.61
Composition of emigrant deposits	1.00	1.00	1.00	1.00	1.00
Local currency	0.90	0.91	0.93	0.94	0.95
Demand	0.10	0.11	0.11	0.11	0.10
Time	0.80	0.80	0.81	0.83	0.85
Foreign currency	0.10	0.09	0.07	0.06	0.05
Memo item: Emigrant deposits	12,477	15,585	15,585	19,042	22,153

Sources: Bank of Cape Verde; and staff estimates.

1/ Títulos Consolidados de Mobilização Financeira.

2/ INPS=Instituto Nacional de Previdência Social.

Table 15. Cape Verde: Interest Rate Structure, 1999–2003
(Annual average, in percent)

	1999	2000	2001	2002	2003
Refinance rate	9.2	8.5	11.0	10.5	8.5
Average T-bill rates	7.2	8.3	9.7	8.3	5.9
91 days	6.2	7.8	9.5	7.9	5.8
182 days	7.2	8.5	10.3	8.0	5.8
364 days	8.1	8.8	9.2	6.6	6.2
Lending rates (average)	13.0	12.8	13.8	14.1	12.6
Up to 90 days	12.0	11.9	12.8	13.2	12.7
From 91 to 180 days	12.4	12.4	13.3	13.5	13.1
From 181 days to one year	12.7	12.7	13.6	13.5	13.3
From one to two years	13.7	13.5	14.4	14.9	14.3
From two to five years	13.5	13.1	14.2	14.7	13.6
More than five years	13.6	13.2	14.3	14.5	13.6
Time deposit rates					
Up to 60 days	4.1	4.2	4.3	4.6	4.1
From 61 to 90 days	4.8	4.3	4.7	4.9	3.9
From 91 to 180 days	6.2	5.6	6.1	6.2	5.2
From 181 days to one year	7.7	6.9	7.5	7.5	6.2
More than one year	7.6	7.6	8.1	7.6	6.3
Emigrants time deposit rates					
From 30 to 180 days	6.9	4.7	7.3	6.6	5.0
From 181 days to one year	9.1	8.3	9.0	8.7	7.2
More than one year	9.5	9.5	9.8	9.6	8.1

Source: Bank of Cape Verde.

Table 16. Cape Verde: Balance of Payments, 1999–2003
(In millions of Cape Verde escudos, unless otherwise indicated)

	1999	2000	2001	2002	2003
Current account	-7,680	-7,246	-7,016	-8,314	-7,539
Excluding official current transfers	-12,709	-9,859	-9,617	-12,473	-11,940
Trade balance	-22,096	-22,938	-23,958	-27,673	-28,253
Exports, f.o.b.	2,697	4,598	4,577	4,909	5,150
Imports, f.o.b.	-24,793	-27,536	-28,535	-32,583	-33,403
Services (net)	-1,082	890	1,312	1,242	1,342
Credit	10,898	12,904	15,981	17,808	19,578
<i>Of which:</i> tourism	2,901	4,821	6,539	7,509	8,152
Debit	-11,980	-12,014	-14,668	-16,565	-18,236
Factor income (net)	-867	-1,366	-753	-1,364	-1,134
<i>Of which:</i> Government interest payments	-386	-558	-568	-557	-514
Current transfers (net)	16,366	16,167	16,382	19,482	20,507
Official	5,028	2,614	2,601	4,159	4,401
Private	11,337	13,554	13,781	15,323	16,106
Capital and financial account (net)	10,831	4,819	9,545	11,329	6,278
Capital transfers	916	1,342	3,004	1,058	2,071
Direct investment (net)	5,432	3,888	983	1,718	1,350
Net official flows	2,982	1,106	2,113	1,150	1,998
<i>Of which:</i> Amortization	-945	-1,325	-5,444	-2,995	-2,101
Trust fund investments (net)	-1,940	-2,384	0	0	1,006
Other capital	3,148	881	3,265	7,404	-147
Commercial banks	-104	-1,227	-115	1,082	3,261
Emigrants' deposits flows	2,044	2,417	3,108	3,457	3,111
Commercial credit (net)	1,441	-576	663	2,577	-171
Other	-233	268	-391	288	-6,348
Net errors and omissions	377	-2,274	-636	-328	760
Overall balance	3,528	-4,701	1,892	2,687	-500
Financing	-3,528	4,701	-1,892	-2,687	500
Arrears (+ = increase)	-548	2,277	-1,855	-811	0
Rescheduling/cancellation of arrears	0	0	1,855	811	0
Remaining financing gap	0	0	0	0	0
Memorandum items:					
Current account, including official transfers 1/	-12.9	-11.2	-9.9	-11.0	-9.1
Current account, excluding official transfers 1/	-21.3	-15.3	-13.6	-16.5	-14.5
Overall balance 1/	7.0	-8.5	2.7	3.5	-0.6
Gross international reserves	4,678	3,349	5,238	8,391	8,173
In months of imports of goods and services	1.5	1.0	1.5	2.0	1.9
Scheduled debt service 2/	30.2	10.8	29.2	15.6	10.6
External debt (excluding arrears) 1/	53.2	59.5	62.3	54.2	44.8
Exchange rate per U.S. dollar (average)	103.5	119.7	123.2	117.2	97.7

Sources: Bank of Cape Verde; and staff estimates.

1/ In percent of GDP.

2/ In percent of exports of goods and nonfactor services.

Table 17. Cape Verde: Merchandise Exports, 1999–2003
(In millions of Cape Verde escudos)

	1999	2000	2001	2002	2003
Agricultural products	3.7	0.0	10.9	0.0	3.4
Fish and crustaceans	184.6	90.1	37.7	58.8	48.2
Fish (including tuna)	135.9	61.2	27.0	20.1	8.9
Canned	0.1	4.0	9.2	4.0	6.6
Frozen	120.4	42.8	17.3	12.9	0.9
Fresh	15.4	14.4	0.5	3.2	1.4
Shellfish and lobster	48.7	28.9	10.7	38.7	39.3
Hides and skin	4.3	1.2	2.9	57.0	1.6
Shoes and shoe parts	670.8	658.7	511.2	445.4	381.8
Miscellaneous	1496.5	1348.4	1456.8	645.7	801.1
Clothing	236.4	447.0	606.5	574.5	674.1
Electronic components	43.7	29.9	26.4	11.3	0.0
Other	41.1	45.1	12.3	59.9	127.0
Total national exports	1184.6	1272.0	1207.8	1234.7	1236.0
Total reexports	1136.7	2939.4	2955.1	3315.4	3619.8
Total exports	2321.3	4211.4	4162.9	4550.1	4855.8

Sources: Bank of Cape Verde; Directorate of Customs; National Statistics Institute; and staff estimates.

Table 18. Cape Verde: Merchandise Imports, c.i.f., 1999–2003

(In millions of Cape Verde escudos, unless otherwise indicated)

	1999	2000	2001	2002	2003
Consumer goods	10,600	11,148	12,571	12,732	13,403
Primary food products	1,734	1,344	1,356	1,809	1,847
Intermediate food products	5,443	6,079	7,132	6,565	7,006
Transport materials	1,094	1,160	1,418	1,167	1,269
Other durable goods	672	771	753	1,008	1,024
Other semidurable goods	741	668	775	919	906
Other nondurable goods	916	1,127	1,137	1,265	1,353
Intermediary goods	5,799	6,509	6,027	7,535	7,137
Primary food products	180	204	195	208	198
Intermediate food products	106	156	89	134	127
Other primary products	105	110	111	81	92
Agricultural products	9	5	16	11	18
Finished food products	159	158	124	134	135
Shoe products	99	154	103	142	97
Other industrial products	233	250	235	293	301
Construction materials	2,349	2,739	2,326	3,025	3,069
<i>Of which:</i> cement	919	992	976	1,164	1,315
metal	1,430	920	714	1,034	1,170
Wood products	766	705	783	676	964
Electrical materials	743	680	659	1,401	614
Other intermediate products	943	1,196	1,205	1,253	1,418
Parts and accessories for transport materials	105	151	181	178	104
Capital goods	4,319	4,537	4,560	6,220	4,647
Machines	2,364	2,681	2,589	2,944	2,218
Transportation	1,468	1,394	1,349	2,112	2,006
Engines	487	462	623	1,164	424
Petroleum imports	1,328	1,533	1,520	1,635	4,329
<i>Of which:</i> fuel oil	90	367	274	192	515
diesel oil	565	613	882	950	2,355
gasoline	108	173	154	319	268
kerosene	64	11	0	11	0
Other imports	3,036	5,832	5,297	4,147	4,697
Total merchandise imports, c.i.f.	25,082	29,559	29,974	32,269	34,213
Total merchandise imports, f.o.b.	24,806	28,139	28,535	32,583	33,403
Ratio of imports c.i.f. to imports f.o.b. (in percent)	101	105	105	99	102

Source: Cape Verde authorities.

1/ In percent.

Table 19. Cape Verde: International Trade in Services, 1999–2003

(In millions of Cape Verde escudos)

	1999	2000	2001	2002	2003
Total services (net)	-1,081.9	876.2	1,312.4	1,471.9	1,342.0
Credit	10,898.0	12,904.5	15,980.7	18,588.3	19,578.4
Tourism	2,900.9	4,826.2	6,539.1	6,985.5	8,152.0
Nontourism	7,997.1	8,078.3	9,441.6	11,602.8	11,426.4
Transport	4,528.5	5,319.5	6,244.0	8,662.1	8,105.4
Sea	385.1	351.6	399.0	205.1	191.6
Air	4,143.4	4,967.8	5,844.9	8,457.0	7,913.8
Travel	2,960.7	4,871.0	6,621.5	7,112.2	8,299.8
Business	59.8	44.8	82.4	126.7	147.8
Personal (tourism)	2,900.9	4,826.2	6,539.1	6,985.5	8,152.0
Embassies and other officials	993.5	838.9	1,148.3	995.8	1,251.1
Construction	758.9	113.2	19.9	7.4	8.0
Communications	567.4	1,252.0	1,334.3	1,418.8	1,425.3
Information services	15.3	9.4	11.4	3.3	4.2
Financial services	55.2	1.2	4.4	7.7	14.2
Insurance	259.5	124.7	304.1	36.2	115.4
Other	759.0	374.6	292.8	344.8	355.0
Debit	-11,979.9	-12,014.1	-14,668.3	-17,116.3	-18,236.4
Transport	-4,680.5	-5,337.1	-6,183.8	-7,982.1	-8,787.4
Sea	-2,940.5	-2,902.4	-3,090.7	-3,216.3	-3,092.6
Air	-1,740.0	-2,434.8	-3,093.1	-4,765.8	-5,694.8
Travel	-4,202.1	-4,347.5	-5,818.7	-6,614.5	-6,928.1
Business	-553.7	-534.3	-529.9	-726.6	-705.2
Personal	-3,648.5	-3,813.3	-5,288.8	-5,887.8	-6,222.9
Embassies and other officials	-444.3	-406.9	-688.5	-522.6	-543.2
Construction	-52.8	-1.7	0.0	-0.2	0.0
Communications	-269.8	-478.4	-524.7	-533.3	-337.8
Information services	-481.6	-381.2	-240.1	-277.1	-289.1
Financial services	-315.3	-18.9	-342.4	-86.1	-185.6
Insurance	-340.8	-370.6	-455.0	-524.0	-510.1
Other	-1,192.7	-671.8	-415.1	-576.4	-655.1

Source: Cape Verde authorities.

Table 20. Cape Verde: Direction of Trade, 1999–2003

(In percent of total)

	1999	2000	2001	2002	2003
Exports	100.0	100.0	100.0	100.0	100.0
Angola	0.0	0.3	0.1	0.0	0.8
France	0.4	0.1	0.2	0.1	0.1
Germany	0.0	2.3	0.7	1.6	1.1
Guinea-Bissau	2.1	0.4	0.0	0.4	0.0
Netherlands	0.8	0.3	0.2	0.2	0.4
Portugal	89.7	80.1	90.7	88.4	70.8
Spain	2.9	3.5	0.2	0.8	0.0
United States	0.0	11.4	6.3	4.4	22.5
Other	4.1	1.7	1.6	4.0	4.2
Imports	100.0	100.0	100.0	100.0	100.0
Brazil	0.0	0.0	2.3	3.5	2.7
Côte d'Ivoire	0.0	0.0	0.8	0.6	2.6
France	2.4	4.4	3.2	2.1	3.1
Germany	2.0	1.5	0.6	3.9	1.0
Italy	0.0	0.0	3.2	3.1	2.2
Netherlands	17.8	13.0	22.0	18.1	20.3
Portugal	52.7	52.4	52.1	55.3	48.4
Senegal	0.0	0.0	0.5	1.0	1.3
Spain	2.4	2.5	3.6	3.8	2.6
Sweden	0.1	0.0	0.6	0.1	0.1
United Kingdom	2.9	1.8	1.6	0.4	0.9
United States	3.4	3.6	2.3	3.3	3.4
Other	16.3	20.8	7.1	4.8	11.3

Source: Direcção Geral das Alfândegas.

Table 21. External Trade with CEDEAO Countries, 1999–2003
(in Millions of Cape Verde escudos)

	1999		2000		2001		2002		2003	
	Import	Export	Import	Export	Import	Export	Import	Export	Import	Export
Total	432.9	24.9	344.9	8.2	409.0	14.3	556.7	46.6	1,436.7	17.0
Benin	0.0	0.0	0.0	0.0	0.0	0.0	31.3	0.0	0.0	0.0
Côte d'Ivoire	212.3	0.0	162.8	0.0	243.8	0.0	201.1	0.0	907.0	0.0
Ghana	0.0	0.0	0.0	0.0	3.0	0.0	0.5	0.0	47.1	0.0
Gambia, The	3.5	0.0	4.4	0.0	5.3	0.0	2.2	0.0	1.3	0.0
Guinea-Bissau	0.2	24.9	1.0	4.9	5.3	0.0	6.1	5.3	2.5	0.5
Guinea Conakry	9.3	0.0	0.0	0.0	0.0	0.0	1.0	2.0	0.0	0.0
Liberia	34.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	50.2	0.0
Mali	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0
Mauritania	0.0	0.0	0.0	0.0	0.0	7.0	0.0	24.4	0.0	11.9
Nigeria	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Senegal	173.3	0.0	176.7	3.3	151.6	7.3	314.6	14.9	428.6	4.6
Sierra Leone	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Togo	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total external trade	25,483.9	1,184.8	27,516.5	1,271.4	28,803.0	1,210.8	32,269.4	1,234.7	34,235.2	1,236.1
Share of external trade with CEDEAO countries in the total external trade (in percent)	1.7	2.1	1.3	0.6	1.4	1.2	1.7	3.8	4.2	1.4

Source: Direcção Geral das Alfândegas.

Table 22. Cape Verde: Factor Income, 1999–2003

(In millions of Cape Verde escudos)

	1999	2000	2001	2002	2003
Total factor income (net)	-860.2	-1,365.8	-662.9	-1,641.4	-1,134.3
Credit	202.0	607.3	830.2	819.9	1,515.6
Investment income	74.7	459.3	684.0	774.1	1,499.2
<i>Of which:</i> Trust Fund	...	99.6	402.5	503.4	508.4
Compensation of employees	127.3	148.1	146.2	45.8	16.5
Other	0.0	0.0	0.0	0.0	0.0
Debit	1,062.2	1,973.2	1,493.2	2,461.3	-2,649.9
Investment income	-1,013.3	-1,927.1	-1,458.5	-2,430.3	-2,596.2
Scheduled interest	-385.9	-558.5	-478.1	-719.3	-514.4
Government	-385.9	-558.5	-478.1	-719.3	-514.4
Public enterprises	0.0	0.0	0.0	0.0	0.0
Other investment income	-627.4	-1,368.6	-980.4	-1,711.0	-2,081.9
Compensation of employees	-48.9	-46.1	-34.6	-31.0	-53.7
Other	0.0	0.0	0.0	0.0	0.0

Source: Bank of Cape Verde.

Table 23. Cape Verde: Private and Public Transfers, 1999–2003

(In millions of Cape Verde escudos)

	1999	2000	2001	2002	2003
Current transfers (net)	16,365.5	16,167.5	16,381.7	19,549.8	20,506.6
Private (net)	11,337.1	13,553.9	13,781.0	15,390.9	15,730.4
Credit	12,105.6	14,473.7	16,478.5	17,166.0	17,520.4
Emigrant remittances	8,070.8	10,241.3	9,826.9	9,912.0	9,032.4
Other	4,034.8	4,232.4	6,651.6	7,254.0	8,488.0
Debit	-768.5	-919.8	-2,697.4	-1,775.1	-1,790.0
Remittances	0.0	-9.7	0.0	-153.3	-22.3
Other	-768.5	-910.1	-2,697.4	-1,621.8	-1,767.7
Official (net)	5,028.4	2,613.6	2,600.7	4,158.9	4,776.2
Credit	5,199.0	3,105.6	2,684.0	4,209.7	4,877.8
Foreign exchange	3,733.8	1,830.1	1,947.1	2,138.6	3,104.2
Food	874.6	709.5	391.9	925.4	867.0
Debit	-170.6	-492.0	-83.3	-50.8	-101.6
Capital transfers (net)	916.4	1,341.6	3,004.0	1,579.9	2,071.5

Source: Bank of Cape Verde.

Table 24. Cape Verde: External Public Debt Outstanding, 1999–2003

(In millions of U.S. dollars, unless otherwise indicated; end of period)

	1999	2000	2001	2002	2003
Multilateral	210.8	226.9	252.2	288.4	351.0
AfDF 1/	71.6	77.9	86.2	85.5	108.4
IDA	86.8	101.9	110.1	143.4	176.3
IMF	0.0	0.0	0.0	3.3	7.6
BADEA 1/	14.9	12.5	20.6	20.6	22.1
AfDB 1/	6.8	1.3	1.3	0.6	0.0
EIB 1/	10.4	9.0	8.1	7.0	9.4
OPEC 1/	4.7	7.3	7.7	10.7	6.6
IFAD 1/	10.1	10.2	8.9	9.1	10.9
Saudi Fund 1/	0.7	0.0	0.3	0.0	0.0
NDF 1/	2.3	2.3	2.9	2.7	3.3
NTF 1/	2.7	4.5	6.2	5.4	6.5
Bilateral	84.6	74.4	77.2	82.2	120.8
Government	61.6	55.5	56.0	67.7	87.5
China	13.4	13.4	0.0	0.0	7.6
Kuwait	9.1	2.5	4.4	2.9	2.8
Portugal	18.4	24.2	41.3	44.1	48.3
South Africa	7.2	3.8	0.0	0.0	...
Abu Dhabi	0.2	0.2	0.2	0.1	0.0
Germany	13.4	11.4	10.1	20.6	11.0
Russia	...	...	...	...	17.8
Export credit agencies	23.0	18.9	21.2	14.5	33.3
Caisse Générale des Dépôts	4.7	3.9	4.7	7.0	16.6
ICO (Spain)	6.8	6.7	7.9	1.2	12.7
CACEX (Brazil)	2.7	2.2	2.4	2.4	0.0
SOMEK (Portugal)	8.7	6.2	6.3	3.9	4.0
Private companies	...	...	8.2	12.4	3.9
Banco Espirito Santo	...	...	7.5	11.8	3.9
MSF (Portugal)	...	...	0.7	0.7	...
Total (excluding arrears) 2/	295.4	301.3	337.6	383.0	475.7
As percent of GDP	52.5	55.3	60.9	55.2	52.0
Stock of external debt arrears	3.8	22.8	14.5	7.5	0.0
Total (including arrears)	299.2	324.1	352.1	390.5	475.7
As percent of GDP	53.2	59.5	63.5	56.3	52.0
Total (including arrears and financing gap)	299.2	324.1	352.1	390.5	475.7
As percent of GDP	53.2	59.5	63.5	56.3	52.0
In millions of Cape Verde escudos	32,837	38,412	44,052	41,064	41,536

Source: Cape Verde authorities.

1/ AfDF = African Development Fund; BADEA = Arab Bank for Economic Development for Africa;

AfDB = African Development Bank; EIB = European Investment Bank;

OPEC = Organization of Petroleum Exporting Countries; IFAD = International Fund for Agricultural Development;

Saudi Fund = Saudi Fund for Development; NDF = Nordic Development Fund; and NTF = Nigeria Trust Fund.

2/ Total debt (excluding arrears) for 2003 now includes rescheduled debt to ICO, which was formerly included in debt arrears.

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
<p>1. Single income tax (Imposto Único sobre Rendimentos or, IUR; Decree-Law 1/96 of 1/15/96; Law 1/V/96 of 6/20/96; Law 16/V/96 of 12/30/96; and, Law 1116/V/99 of 12/20/99).</p>	<p>Taxpayers</p> <p>The IUR applies to the following:</p> <ul style="list-style-type: none"> • all national or foreign companies, whether commercial or civil in commercial form, partnerships, joint-stock companies, cooperatives, public enterprises, and corporate persons under public or private law, with headquarters or actual management on Cape Verdean territory; • individuals engaged in import or export activities with turnover exceeding CVEsc 5 million a year; • unincorporated entities resident in Cape Verde (e.g., unsettled estates, legal entities declared invalid, unincorporated civil companies, commercial companies, or civil companies in commercial form); and • individuals or corporations not resident in Cape Verde, as long as they produce or earn any income in Cape Verde. 	<p>Exemptions</p> <p>The following exemptions apply:</p> <ul style="list-style-type: none"> • The state, municipalities, and any of their services or establishments are exempt, even if identified as individual taxpayers, provided that they do not engage in commercial, industrial, agricultural, fishing, or service-providing activities. • Social welfare institutions and labor unions or associations are exempt regarding the activities for which they were legally established, and provided that they do not engage in commercial, industrial, agricultural, service-providing, or capital investment activities. • The Bank of Cape Verde is exempt from payment on the income earned from operations that it carries out as General Cashier of the Treasury and related activities. • Also exempt are associations legally established to perform cultural, recreational, or sporting activities and which meet all the following conditions: there are no distributed profits; and no member of their corporate bodies has a direct or indirect interest in their operating profit. <p>Interest from emigrants' term deposits and TCMFs are exempt.</p> <ul style="list-style-type: none"> • The income of (a legally established) 	<p>The following rates apply:</p> <ul style="list-style-type: none"> • 20 percent for enterprises subject to pre-assessment; • 30 percent for enterprises subject to direct assessment (except for financial institutions, for which a rate of 30 percent applies); • 20 percent on interest from term deposits; • 15 percent on other capital income (dividends, profit sharing, advances on profits, and gambling profits); and • 20 percent on profits earned by nonresidents (on billing volume). <p>Note: The rates will be published in the State Budget Law.</p>

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
		<p>agricultural, fishing, housing, education, or handicraft production cooperative is exempt, provided that at least three-fourths of its workers are members and none owns more than 10 percent of the cooperative's equity capital, and that turnover does not exceed CVEsc 10 million.</p> <ul style="list-style-type: none"> • Fishing, artisanal, or industrial activities are exempt, provided that annual turnover does not exceed CVEsc 3 million. • Income from treasury securities is exempt. 	
	<p>Personal tax base</p> <p>Insofar as it applies to individual income, the IUR is chargeable on overall annual income in the following categories:</p> <ul style="list-style-type: none"> • Category A comprises income from property; • Category B covers commercial and industrial income, including capital gains, provision of services, and agricultural and fishing income; • Category C constitutes capital income and other income such as that from gaming, lotteries, and mutual betting; and 	<p>The following are also exempt</p> <ul style="list-style-type: none"> • annual income of CVEsc 150,000 or less; • staff of diplomatic or consular missions; • foreign staff of foreign organizations; • clerics, when exercising their spiritual mission; • salaries or other income paid to employees and workers on leave for treatment abroad; • family allowances granted under law; • cost allowances up to the limits set by law; 	

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
	<ul style="list-style-type: none"> Category D comprises wage and salary income, including reserve and retirement pensions, alimony, and fixed-term, life, or other kinds of annuities. 	<ul style="list-style-type: none"> cash shortage allowances up to 10 percent of monthly salary; 	
	<p>Assessment methods</p>	<ul style="list-style-type: none"> occasional medical or hospital allowances, and retirement pensions up to CVEsc 960,000 a year; and 	<p>IUR Annual Calculation Schedule (Individuals)</p>
	<p>Three assessment methods are used:</p>	<ul style="list-style-type: none"> severance payments arising from contract rescission or extinction of public employment, if agreed between the employer and the worker. 	<p>Overall annual income (In Cape Verde escudos)</p> <p>Marginal Rate (In percent)</p> <p>Average Rate</p>
	<ul style="list-style-type: none"> Under self-assessment (<i>método declarativo</i>), a return is submitted by the taxpayer or, in cases of tax substitution, by the entity legally required to do so. 		<p>Less than 300,000 15.0</p> <p>300,001 – 630,000 20.0</p> <p>630,001 – 1,260,000 27.5</p> <p>1,260,001 – 1,890,000 35.0</p> <p>More than 1,890,000 45.0</p> <p>...</p>
	<ul style="list-style-type: none"> Pre-assessment (<i>método de estimativa</i>) is applied to all individuals not considered to be companies for tax purposes as envisioned in the industry schedule (<i>Tabela Geral das Indústrias</i>). The taxable base is determined on a presumptive basis, taking into account the turnover and kind of business, or normal production and market conditions if returns are not filed. 	<p>Deductions</p>	
	<ul style="list-style-type: none"> Under direct assessment (<i>método de verificação</i>), the taxable base is based on the taxpayer's filed return, which derives from the accounting data. 	<p>The following deductions apply: up to CVEsc 160,000 for single, widowed, or divorced individuals; CVEsc 210,000 for single-income married couples; CVEsc 330,000 for married couples with two or more incomes; CVEsc 80,000 for individuals resident abroad; CVEsc 25,000 for each child, up to a maximum of CVEsc 100,000; and 80 percent of receipts from housing rental, up to a maximum of CVEsc 144,000.</p> <p>Also deductible are interest and charges on home purchase or improvement loans, up to a maximum of CVEsc 144,000; pension allowances that the taxpayer is required to pay, up to a maximum of CVEsc 240,000; 40 percent of income from liberal professions, up to a maximum of CVEsc 80,000; mandatory social security or union contributions paid by industrial or commercial workers; life, health, or accident</p>	
	<p>The tax due in accordance with these methods is paid in two installments.</p>		

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
		<p>insurance premiums, up to a maximum of CVEsc 30,000; and grants to schools, homes for the aged and childcare centers, up to a maximum of CVEsc 240,000.</p>	
		<p>50 percent of health expenses, CVEsc 50,000 every two years for purchase of computer equipment, and interest on loans for payment of health expenditures are deductible.</p>	
		<p>Wages and salaries subject to IUR; rents subject to real estate tax; fees paid to perform any activity; contributions to unions and union funds; and insurance premiums and trade association fees are deductible.</p>	
		<p>There is a 10 percent abatement of tax payable by eligible companies that used Cape Verdean merchant ships to carry at least 50 percent of their imports during the base year; and an amount equal to the discount rate plus 2 percent is applied to tax obligations settled in advance.</p>	
<p>2. Value Added Tax (Imposto Sobre o Valor Acrescentado, IVA; Law 14/VI/2002 of 09/19/2002, Law 21/VI/2003 of 07/14/03, Law 33/VI/03 of 09/15/03)</p>	<p>Levied on value added, using the invoice-credit method: VAT is levied on domestic sales of goods and services and on imports, with deductions for VAT paid on inputs to production of taxable goods.</p> <p>A special regime is in place for VAT applied to administered prices (electricity, water, telecommunication, transports and combustibles).</p> <p>Threshold of 180 thousand per year.</p>	<p>Zero rated: exports of taxable goods and services.</p> <p>Exemptions</p> <p>Animal, agricultural, fishing products and forestry (e.g. meat, fish, milk, cheese, eggs, vegetables, fruit, cereals); medical services; education and training; social protection; sports and recreation; scientific and cultural activities (e.g. courses, conferences, seminars, theater, music, film, arts etc); postal services;</p>	<p>15 percent except for lodging, restaurants and hotel establishment services where the tax rate is 6 percent.</p>

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
		intellectual property; newspapers and books; political, religious, humanitarian and patriotic activities; pharmaceutical products including veterinary for therapeutic purpose and prophylaxis; financial service such as insurance; postal stamps; gambling; real estate subject to the Real Estate Tax; rental of property; funerary services; trash removal; public radio and television.	
3. Special Consumption Tax (Imposto sobre Consumos Especiais, ICE; Law 14/VI/2002 of 09/19/2002; Law 48/VI/2004 of 07/26/2004)	Ad valorem excise duty applied to consumption and imports. Tax is applied to tobacco, alcoholic beverages, beauty and luxury products, fuel, old vehicles, arts.	Exemptions Products related to diplomatic and consular relations and to international organizations; exports and raw materials used as a basis for production of medical, sanitary, scientific and laboratory products; goods subject to customs regulation.	10 percent except for alcoholic beverages where 30 percent is levied and Vehicles older than: 4 years - 30 percent 6 years - 60 percent 10 years - 150 percent
4. Customs Duties (Direitos de Importação, DI; Law 14/VI/2002)	Duties are levied on most imported goods, generally ad valorem on the c.i.f value, except for		Tractors older than: 4 years – 10 percent 6 years – 20 percent 10 years – 60 percent 5, 10, 20, 30, 40 and 50 percent
5. Real estate tax (Law 1543/63, amended by Law 61/IV/92 of 12/30/92; and Law 94/IV/93 of 12/31/93).	Charged on rural and urban property, whether rented or owner occupied. It is based on the rent charged or on the annual rental value established by the permanent valuation committee. The tax due is paid in one or two equal installments.	Exemptions Government buildings, including those occupied by economic coordination agencies; buildings belonging to local and administrative institutions that do not produce rent or ground rent; buildings occupied by hospitals, shelters, or other social welfare institutions; buildings used for religious services; public interest institutions; rent-exempt schools; facilities of sports associations; diplomatic or consular buildings; private secondary school buildings worth more than	A rate of 3 percent is applied to both rural and urban buildings.

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates
		<p>CVEsc 1 million if situated in Praia or Mindelo or those worth more than CVEsc 500,000 elsewhere in the country, for 15 years; finished buildings, for 6 years (rental) or 10 years (owner occupied), from the completion of construction; nonproductive rural properties; rural properties used for certain crops, for 10-20 years from the start of cultivation; and rural buildings with yearly rent below CVEsc 5,000 and urban buildings with yearly rent below CVEsc 100,000.</p>	
		<p>Deductions</p>	
		<p>For urban properties, 15 percent of rental value is deductible as maintenance expense.</p>	
		<p>For rural properties, normal expenses with cultivation, maintenance, and sale of products. Also deductible are improvements to rural buildings, construction of and improvements to rural buildings, and administration, fertilizer, seeds, wages, and some inputs. Taxable income shall be no less than 40 percent of the gross income obtained from agricultural activity.</p>	

Table 25. Cape Verde: Summary of the Tax System
(As of end-2004)

Tax	Nature of Tax	Exemptions and Deductions	Rates																																
6. Municipal vehicle tax (Law 61/IV/92 of 12/30/92; and Ministerial Order 1/93 of 1/20/93).	Levied yearly on motor vehicles.	All exemptions have been abolished.	<table border="0"> <tr> <td>Displacement (Cubic centi- meters)</td> <td>Up to 5 yrs (Cape Verde escudos)</td> <td>5-10 yrs</td> <td>>10 yrs</td> </tr> <tr> <td></td> <td>Automobiles</td> <td></td> <td></td> </tr> <tr> <td>Up to 1,000</td> <td>900</td> <td>500</td> <td>300</td> </tr> <tr> <td>1,001 - 1,300</td> <td>1,200</td> <td>800</td> <td>400</td> </tr> <tr> <td>1,301 - 1,750</td> <td>1,600</td> <td>1,100</td> <td>500</td> </tr> <tr> <td>1,751 - 2,600</td> <td>3,800</td> <td>1,800</td> <td>900</td> </tr> <tr> <td>2,601 - 3,500</td> <td>5,400</td> <td>2,700</td> <td>1,400</td> </tr> <tr> <td>Over 3,500</td> <td>8,400</td> <td>4,200</td> <td>2,100</td> </tr> </table>	Displacement (Cubic centi- meters)	Up to 5 yrs (Cape Verde escudos)	5-10 yrs	>10 yrs		Automobiles			Up to 1,000	900	500	300	1,001 - 1,300	1,200	800	400	1,301 - 1,750	1,600	1,100	500	1,751 - 2,600	3,800	1,800	900	2,601 - 3,500	5,400	2,700	1,400	Over 3,500	8,400	4,200	2,100
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