EXECUTIVE BOARD MEETING

EBS/20/11

February 26, 2020

To: Members of the Executive Board

From: The Secretary

Subject: **Cabo Verde—First Review Under the Policy Coordination Instrument and Request for Modification of Targets**

Board Action:	Executive Directors' **consideration** (Formal)
Tentative Board Date:	**To be announced**
Proposed Decision:	Page 18
Publication:	Yes*
Questions:	Ms. Kabedi-Mbuyi, AFR (ext. 36387) Mr. Amo-Yartey, AFR (ext. 37713)
Document Transmittal in the Absence of an Objection and in accordance with Board policy:	After Board Consideration—African Development Bank, European Investment Bank, World Trade Organization

***The Secretary's Department has been notified by the authorities that their explicit consent is required prior to the publication of Board documents. At the time of circulation of this paper to the Board, the authorities have indicated that they consent to the Fund's publication of this paper.**

INTERNATIONAL MONETARY FUND

CABO VERDE

February 21, 2020

FIRST REVIEW UNDER THE POLICY COORDINATION INSTRUMENT AND REQUEST FOR MODIFICATION OF TARGETS

KEY ISSUES

Context. Cabo Verde's economic situation has been improving in recent years, with growth above historical trends, low inflation, strengthening fiscal and external positions, and declining public debt-to-GDP ratio. Inefficiencies in, and fiscal risks related to State-Owned Enterprises (SOEs) are being addressed through privatization and restructuring, consistent with the authorities' reform agenda under their Strategic Plan for Sustainable Development. However, vulnerabilities remain, hence sustained reform implementation is needed to improve the business environment, support broad-based growth and build resilience.

Outlook and risks. Economic prospects are positive. Growth is expected to remain strong, supported by the industry, services and transport sectors, as well as growth-enhancing structural reforms. The external position would improve further reflecting increased export receipts and remittances. This outlook is subject to risks. The most significant downside risks are weaker-than-projected economic conditions in the euro area, and rising protectionism and retreat from multilateralism. Domestically, downside risks include Cabo Verde's high vulnerability to weather-related shocks and delays in SOEs reforms. Upside risks include better-than-expected tourism activities and increased foreign direct investment.

Program implementation. Performance under the Policy Coordination Instrument-supported program has been strong. All end-September 2019 quantitative targets were met, except for the floor on tax revenue, missed by a narrow margin due to lower-than-projected taxes on international trade. All reform targets (RT) were met. A new RT was introduced on a strategy to operationalize the Sovereign Private Investment Guarantee Fund in line with the authorities' plan to adhere to best practice for the management of the fund.

Staff's views. Based on program performance and policies outlined in the authorities' updated Program Statement (PS), staff supports the completion of the first review under the program, and the modification of quantitative targets for the second and third reviews, consistent with the revised macroeconomic framework.

Approved By	
Annalisa Fedelino (AFR) and Johannes Weigand (SPR)	Discussions took place in Praia and Boa Vista island. The staff team comprised Ms. Kabedi-Mbuyi (Head), Messrs. Amo-Yartey and Abdychev, Mses. Parulian and Carvalho (all AFR). Mses. Mensah and Quartey and Mr. Treilly provided support from Headquarters; Mr. Fachada (OED) participated in some meetings. The team met with Deputy Prime Minister and Minister of Finance Olavo Correia, Central Bank Governor João Serra, other Cabinet members and senior government officials, the President of the Municipal Chamber of Boa Vista island Dr. José Luís Santos, non-government organizations, development partners, and the private sector.

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APPENDIX

RECENT ECONOMIC DEVELOPMENTS

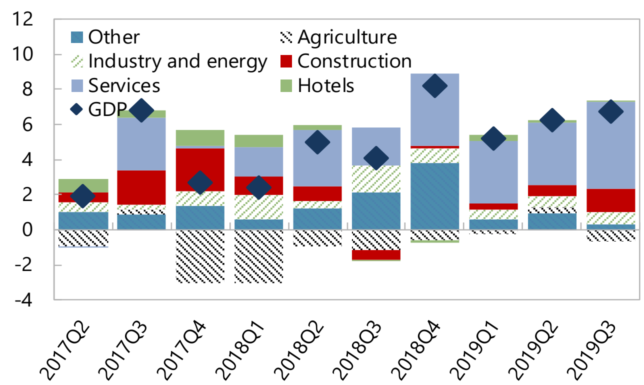
1. **Under the authorities' Strategic Plan for Sustainable Development (PEDS), macroeconomic performance has been marked by robust growth, low inflation, and strong external position** (Figure 1, Table 1).

- Real GDP expanded by 6.1 percent through end-September 2019 and is expected to reach 5.5 percent for the year. Key drivers include private consumption and exports on the demand side; and strong activity in services, construction and industry on the supply side (Text Figure 1).

- Inflation rose to 1.9 percent (y/y) in December 2019, up from 1 percent at end- 2018, reflecting mainly higher food prices.

Text Figure 1. Contributions to Growth

(Quarterly, year-on-year percent change)



Sources: Cabo Verdean Authorities.

- The external position improved during the first three quarters of 2019, thanks to increased exports receipts and remittances, as well as deceleration in imports. The current account deficit is expected to narrow to 3 percent of GDP in 2019 (5.3 percent of GDP in 2018), and international reserves are projected at 5.5 months of prospective imports of goods and services (Figure 2, Table 2).

- Credit to the economy rose only marginally at end-September 2019, consistent with banks' prudent lending practices and reduced exposure to SOEs resulting from reforms implemented in 2018-19, notably in the transport sector. The low credit extension, combined with strong growth in migrants' deposits contributed to increased excess reserves in the banking system (Figure 4, Table 4).

2. **The authorities' efforts to improve the fiscal position and put public debt on a sustained downward trajectory continued in 2019** (Text Table 1, Figure 3, Tables 3a, 3b), leading to the achievement of fiscal targets under the program.

- The primary surplus was well-above the program target at end-September, with revenue and expenditure lower than projected. Revenue performance was affected by shortfalls in: (i) taxes on international trade reflecting lower-than anticipated imports of goods; (ii) nontax revenue because receipts from property income were below projections; and (iii) delays in the disbursement of grants mainly due to a slower pace in the execution of capital outlays. On the expenditure side, under-execution of public investments, mainly due to lengthy procurement processes, particularly for externally-financed projects, was the main contributing factor. Preliminary estimates for the year show that, while increasing compared with 2018, both revenue and expenditure would be below program projections; the programmed primary surplus of 0.7 percent of GDP will be achieved and; the overall fiscal deficit will be slightly better than projected, and about 1 percentage point of GDP lower than in 2018.

- Net other liabilities (NOLs) were below the program target at end-September because of higher loan repayment by the airport management company (ASA) as well as slow execution of capitalization operations. Annual estimates show that NOLs will be lower than programmed, with capitalisation operations above projections, mainly due to two new operations completed in the fourth quarter: the recapitalization of the central bank, and the acquisition of 27 percent of shares in Caixa Economica (the second largest bank) from a foreign private investment group, to help preserve the bank's correspondent banking relationships.

- Resulting from the above developments, financing needs are estimated at 5 percent of GDP for 2019 (6.5 percent under the program). This notwithstanding, the central government debt-to-GDP ratio is projected at 123 percent, which, although in decline compared with 2018, (124 percent of GDP) is above the original forecast (121.4 percent of GDP) due to unfavourable exchange rates projections.

Text Table 1. Statement of Operations of the Central Government, 2018Q1–2019Q3[1]
(Millions of Cabo Verde Escudos)

	2018				2019				
	Q1	Q2	Q3	Q4	Q1	Q2		Q3	
	Act.	Act.	Act.	Act.	Act.	Proj.	Act.	Prog.	Act.
Revenue	11,768	23,628	36,153	52,097	11,891	25,951	25,094	41,562	37,803
Tax	9,076	18,908	29,056	40,657	9,518	19,965	20,219	31,362	30,652
of which: Taxes on international trade	1,686	3,562	5,571	7,733	1,735	3,833	3,663	6,090	5,655
Grants	825	1,085	1,284	2,575	357	1,326	928	2,401	1,225
Non-Tax	1,867	3,635	5,813	8,865	2,016	4,660	3,947	7,800	5,926
Expenditure	10,753	24,284	37,956	57,301	13,353	28,457	25,796	45,063	39,163
Current expenditure	10,399	22,950	34,491	49,162	12,772	25,372	24,119	38,930	36,492
Net acquisition of nonfinancial assets	354	1,334	3,466	8,140	581	3,084	1,676	6,133	2,671
Primary balance	1,917	1,735	1,751	-478	-280	456	1,880	841	2,510
Overall balance	1,015	-657	-1,803	-5,204	-1,462	-2,506	-701	-3,501	-1,360
Net other liabilities	-108	-62	-834	-1,903	8	-3,575	-2,674	-6,345	-1,657
Onlending to SOEs for investment purpose	0	0	-105	-1,541	0	-1,194	0	-2,332	-1,315
Other onlending (net)	6	127	1,729	3,606	6	-683	130	-1,315	1,603
Capitalization	-114	-189	-2,459	-3,968	0	-1,698	-2,806	-2,698	-1,944
Other	0	0	0	0	2	0	3	0	0
Financing needs	-907	719	2,638	7,107	1,454	6,081	3,375	9,846	3,017

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

3. The authorities created a Sovereign Private Investment Guarantee Fund (SPIGF) to be funded with the offshore trust fund (TF) set up in 1998 (Box 1). Resources in the TF were originally mobilized with donors' support and privatization receipts, in the context of financial sector reforms and a domestic debt reduction operation in the late 90s. The TF was backed by twenty-year bonds (*Titulos Consolidados de Mobilizacão Financeira* – TCMFs) issued to swap the stock of domestic debt totaling CVE 11.35 billion (equivalent to €103 million). At the end of the twenty-year period (August 2018), the authorities, in consultation with bond holders, decided to replace the largest bonds with new securities. Accordingly, through a law passed by parliament in June 2019, they created the SPIGF with an initial capital of €90 million, and an Emergency Fund totaling €10 million, intended to provide rapid first response to weather-related and other exogenous shocks. Since there are liabilities backed by resources in the offshore account, the creation of the SPIGF, as currently planned, would increase public gross debt by 5.7 percent of GDP and may raise debt service obligations, with implications for debt sustainability.[1] The authorities will prepare a strategy on the operationalization of the SPIGF, which is a new reform target, in consultation with staff (see below).

Box 1. The Sovereign Private Investment Guarantee Fund – Background

Background. In the late 90's, Cabo Verde faced a domestic debt overhang. At end-1997, the stock of domestic debt stood at US$186 million (about 46 percent of GDP), reflecting excessive domestic financing of fiscal deficits, and contingent liabilities from restructured SOEs and banks. To reduce the public debt burden, the government put in place a debt reduction operation funded with donors' financial support and proceeds from privatization. The operation covered a stock of domestic debt totaling CVE 11.35 billion, held by the central bank, BCV (CVE 6.4 billion); a commercial bank, BCA (CVE 4.6 billion); the pension fund, INPS (CVE 328 million); and the insurance company, Garantia (CVE 22 million).

The offshore Trust Fund (TF). Although there was funding for the debt reduction operation, rather than repaying directly the creditors, the authorities decided to set up a scheme under which: (i) resources mobilized for the operation were placed in an offshore TF, created by law in August 1998, and managed by an European central bank and; (ii) an institution (Fiduciaria International) was created to swap the old stock of domestic debt with twenty-year bonds called *Titulos Consolidados de Mobilizacão Financeira- TCMFs*. Bonds holders earned dividends proportional to their shares, paid directly by the TF manager. The main reason for adopting this approach was to avoid a sudden and large injection of liquidity in the banking system through cash payments associated with the debt reduction.

The TCMFs were not repaid as planned. Under the 1998 law creating the TF, the TCMFs had to be repaid during the 20-year maturity period, using budgetary resources, as the fiscal position improved. However, the TCMFs were eventually not repaid as planned and they all matured in 2018. Consequently, in December 2018, the government issued a Decree calling for the repayment of TCMFs worth less than CVE 300 million, and the replacement of the remaining stock with new bonds to be repaid in 20 years in equal annual instalments, at an interest rate of up to 3 percent; or exchanged between bond holders on conditions to be agreed between parties. On this basis, TCMFs held by Garantia were redeemed in January 2019; and INPS repurchased BCA bonds. As a result, at end-December 2019, TCMFs totaled CVE 11.33 billion (equivalent to €102.7 million) and were held by the BCV (CVE 6.4 billion) and INPS (CVE 4.9 million).

The planned use of the Trust Fund. As of end-2019, the offshore account had €106 million; and the corresponding liabilities amounted to €102.7 million (5.7 percent of GDP). The authorities plan to use the resources in the offshore account to set up the SPIGF (€90 million) that will be invested and used to provide guarantees to capital-intensive private investment projects; and an Emergency Fund (€10 million) for rapid response to natural disasters. The balance would be allocated to the government budget (€6 million). Under this plan, the SPIGF will issue a bond to the Treasury, and the Treasury will issue bonds at 3 percent interest rate to replace the TCMFs, with debt service paid by the Treasury. The final modalities of the TCMFs replacement and parameters related to the new bonds will be clarified in the strategy currently under preparation. The authorities stressed that one important aspect in this regard would be to avoid a mismatch between assets and liabilities.

[1] The TCMFs were originally not included in the stock of domestic public debt, which would explain an increase in gross debt with the issuance of bonds replacing them.

PERFORMANCE UNDER THE PCI

4. Performance under the PCI-supported program has been strong (Program Statement (PS) Tables 1, 2, and ¶10-14).

- All, but one quantitative targets for the end-September 2019 test date were met, with the floor on international reserves exceeded by a wide margin. The target on tax revenue was narrowly missed due to a shortfall in taxes on international trade.
- All non-quantitative continuous targets were met.
- All reform targets have been completed either on or before the scheduled date. The two reform targets for the first review were met: (i) the compilation of financial information on cash flow performance of the six key SOEs for FY2019 and; (ii) the release of minutes of the Monetary Policy Committee meetings.
- In addition, the authorities met the following reform targets programmed for the period October-December 2019: (i) completion of the review report on tax exemptions; (ii) submission to parliament of the 2020 budget in line with commitments under the program; (iii) implementation of quarterly monitoring of actual performance of 6 key SOEs against their approved budgets, starting at end-December 2019; and (iv) reduction of the excessively wide overnight interest rate corridor.

OUTLOOK AND RISKS

5. The medium-term outlook remains favorable (Table 1). Real GDP growth is projected at 5 percent on the back of continued strong activity in the industry, services, and transport sectors, combined with the impact of planned large infrastructure projects and growth-enhancing reforms under the PEDS. These factors are expected to more than compensate the potential negative effects of economic downturn in the euro area, an important downside risk. Inflation would remain below 2 percent over the medium term, in line with forecasts for the euro area. The current account deficit is expected to widen in 2020 as imports demand accelerates, reflecting both a catching-up effect compared with the previous year and the impact of higher fuel prices. It is projected to improve thereafter, reaching 3 percent of GDP by 2024 thanks to strong export performance and increasing remittances. This, together with the projected private capital inflows would help maintain international reserves at 5.5 months of prospective imports of goods and services.

6. The balance of risks to the outlook is tilted to the downside (Box 2). Given Cabo Verde's high vulnerability to exogenous shocks, the most significant risks are external, and they include weaker-than-projected global economic conditions, a sharp rise in risk premia, large swings in energy prices, rising protectionism and retreat from multilateralism, and the coronavirus outbreak. Domestically, high vulnerability to climate-related shocks, faltering fiscal consolidation efforts, and delays in structural reforms, particularly in the SOEs sector are the most significant downside risks. Upside risks include better-than-projected tourism performance, increased foreign direct investment, notably related to the implementation of the PEDS, and broad-based structural reforms.

Box 2. Risk Assessment Matrix[1]
(Scale—high, medium, or low)

Source of Risks	Relative Likelihood[2]	Impact if Realized	Policy Response
Weaker-than-expected global growth: Europe.	**High** Weak foreign demand or an unanticipated Brexit outcome delays investment, reduces private consumption, and strains banks. With limited policy space, the region enters a prolonged period of anemic growth and low inflation.	**Medium/High** Prolonged downturn in the euro area would affect exports, remittances, and FDI, thus negatively impacting growth, as well as the external and fiscal positions.	Accelerate structural reforms to increase productivity, improve the business environment, and enhance resilience to shocks. Build external and fiscal buffers.
Large swings in energy prices.	**Medium** In the near term, uncertainty surrounding the shocks elevate price volatility, complicating economic management. As shocks materialize, they cause large and persistent price swings.	**Medium/High** Higher oil prices would harm growth, generate price pressures, and affect household and corporate incomes.	Build fiscal buffers and accelerate structural reforms to increase growth potential.
Sharp rise in risk premia that exposes financial vulnerabilities.	**High** Higher risk premia generate debt service and refinancing difficulties; stress on leveraged firms, households, and vulnerable sovereigns; and capital outflows, which could all depress growth.	**Medium** Higher interest rate, notably in the US and the Euro area may adversely affect the flow of migrant deposits to Cabo Verde, tourism and FDI.	Tighten monetary policy when needed. Accelerate growth-enhancing reforms.
Rising protectionism and retreat from multilateralism.	**High** In the near term, escalating and unpredictable protectionist action and an inoperative WTO dispute resolution framework imperil global trade. In the medium term, geopolitical competition, protracted tensions, and fraying consensus about the benefits of globalization lead to further fragmentation, with adverse effects on investment, productivity, growth and stability.	**Medium** A global downturn impacting investment, growth and stability would adversely affect FDI flows and Cabo Verde's external position as well as growth.	Build external buffers and accelerate growth-enhancing reforms.

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

[2] In case the baseline does not materialize.

Box 2. Risk Assessment Matrix (Concluded)			
Higher frequency and severity of natural disasters.	**Medium/Low** Higher frequency and severity of natural disasters cause severe economic damage to smaller economies susceptible to disruptions.	**Medium/High** Prolonged drought or other climate-related shocks would undermine agricultural production with negative impact on GDP growth and inflation.	Build resilience to weather-related shocks and accelerate growth-enhancing reforms.
Coronavirus outbreak.	**Medium** Coronavirus outbreak causes widespread and prolonged disruptions to economic activity and global spillovers through tourism, supply chains, containment costs, and confidence effects on financial markets and investments.	**Medium** Widespread and prolonged disruptions to economic activity resulting from the coronavirus could depress tourism with negative impact on economic growth and the external position.	Build resilience to shocks and accelerate growth-enhancing reforms.
Faltering fiscal consolidation efforts.	**Medium/High** Less ambitious and slower fiscal consolidation efforts and delayed SOEs reforms.	**High** Flickering fiscal consolidation efforts and SOEs reforms would undermine macroeconomic stability as well as medium-term fiscal and debt sustainability.	Advance revenue-enhancing reforms, improve capital expenditure management, reduce fiscal risks, notably linked to SOEs, and contain non-priority spending to build fiscal buffers.
Delays in implementing measures to increase productivity and restructure SOEs.	**Medium** Delays in structural reforms implementation, particularly in the public enterprises sector.	**Medium** Delays in advancing the structural reform agenda would hinder competitiveness, potential GDP growth and employment.	Accelerate structural reforms to improve the business environment, reduce the State's role in productive activities and enhance growth potential.

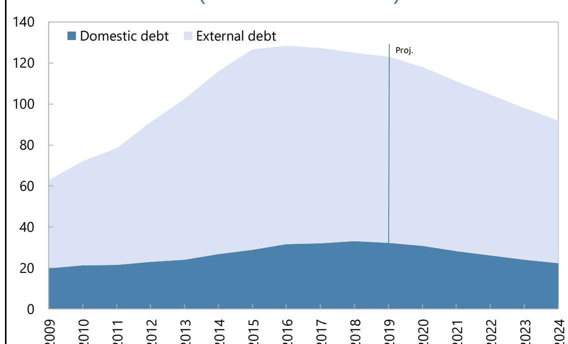
POLICY DISCUSSIONS

Discussions focused on the implementation of policies and reforms to support broad-based growth and secure medium-term fiscal and debt sustainability. Accordingly, priority was given to measures needed to: (i) enhance revenue mobilization and expenditure management; (ii) strengthen the banking system; (iii) accelerate structural reforms, particularly in the SOEs sector; and (iv) address issues related to the operationalization of the Sovereign Private Investment Guarantee Fund.

A. Fiscal Policy and Reforms

7. **The medium-term fiscal framework continues to focus on achieving primary surpluses to strengthen the fiscal position and reduce debt**. Tax and non-tax revenues are projected at around 28 to 29 percent of GDP during 2020-24, as measures are put in place to broaden the tax base, increase administrative efficiency, and rationalize exemptions. During the same period, expenditure is expected to decline to about 30 percent of GDP, with capital and social outlays at around 4 percent of GDP and 7 percent of GDP respectively. The primary surplus is therefore projected at 1.3 percent of GDP over the medium term. Staff stressed that, while the authorities have shown their ability to control spending in case of revenue shortfalls, the biggest challenge in meeting the medium-term fiscal targets rests on strengthening and securing revenue collection.

Text Figure 2. Domestic and External Debt
(Percent of GDP)



Sources: Cabo Verdean Authorities; and IMF estimates and projections.

8. **The projected financing needs support debt sustainability objectives** (Text figure 2). Under current assumptions, the overall fiscal deficit would narrow from 1.7 percent of GDP in 2020 to 0.6 percent of GDP in 2024 which, combine with the expected reduction in capitalization and onlending to SOEs, consistent with progress in structural reforms in the sector, would contribute to a sustained reduction in financing needs. As a result, the central government debt is projected to decline from an estimated 123 percent of GDP at end-2019 to 91.9 percent of GDP by end-2024, helping improve the country's rating under the Debt Sustainability Analysis (DSA). The 2019 joint IMF/World Bank DSA assessed that Cabo Verde's risk of external and total debt distress was high. Consistent with staff's revised medium-term projections, the country could graduate to moderate risk by 2023 (for external debt) and 2025 (for total public debt)[2] through sustained fiscal consolidation efforts, continued growth-enhancing structural reforms notably in the SOEs sector, and prudent borrowing policies, resting on concessional financing. However, the creation of the SPIGF, as envisaged, could have implications for these projections, which staff and the authorities plan to analyze at the time of the second program review.

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

9. The 2020 budget is consistent with program objectives (PS ¶18-24, Text Table 2). Although both revenue and expenditure are higher than projected under the original program, the budget seeks to achieve the programmed primary surplus of 1 percent of GDP. The overall balance (1.7 percent of GDP) is slightly above program projections, leading to financing needs of 3.9 percent of GDP—0.2 percentage points of GDP above the program level.

Text Table 2. Summary of Central Government Operations, 2018–21
(Percent of GDP)

	2018	2019		2020		2021
		Prog.	Proj.	Prog.	Budget	Proj.
Total revenue	28.2	31.7	29.4	30.4	32.5	31.2
Tax Revenue	22.0	21.8	21.3	21.9	22.9	22.6
Other revenue	4.8	7.1	5.5	6.5	6.8	6.4
Grants	1.4	2.8	2.6	1.9	2.8	2.2
Total expenditure	31.0	33.9	31.3	31.8	34.2	32.4
Current expenditure	26.6	28.8	27.5	27.5	29.7	28.7
Compensation of employees	10.7	11.7	10.5	11.2	11.4	11.1
Use of goods and services	4.0	4.7	4.0	4.6	6.4	5.7
Interest	2.6	2.8	2.5	2.4	2.7	2.3
Net acquisition of nonfinancial assets	4.4	5.1	3.7	4.3	4.6	3.6
Primary balance	-0.3	0.7	0.7	1.0	1.0	1.2
Overall balance	-2.8	-2.2	-1.9	-1.5	-1.7	-1.1
Net other liabilities	-1.0	-4.3	-3.1	-2.2	-2.2	-0.9
Onlending	1.1	-2.3	-1.1	-1.6	-1.6	-0.5
Capitalization	-2.1	-1.9	-2.1	-0.6	-0.7	-0.5
Financing needs	3.8	6.5	5.0	3.7	3.9	2.1

Sources: Cabo Verdean authorities and IMF staff projections.

- Revenue is budgeted at 32.5 percent of GDP, predicated on the projected strong economic activity, the full year impact of measures introduced in 2019, and new administrative measures. The latter focus on broadening the tax base, notably through an overhaul of the tax exemption system, improved compliance with tax obligations and digitalization of revenue administration covering collection, inspection and audit. The budgeted revenue to GDP ratio also reflects the following one-off measures with an estimated impact of 2 percent of GDP: (i) potential privatization receipts, projected conservatively; (ii) higher projects grants (0.9 percent of GDP); (iii) revenue from some public institutions now covered in central government statistics (hospitals, universities, the judiciary, and security agencies) in the context of the broadening of coverage for government finance statistics; (iii) higher collection of tax arrears and compensation of cross-liabilities between the Treasury and some companies, including SOEs (0.8 percent of GDP).

- Expenditure is projected at 34.2 percent of GDP (31.8 percent of GDP under the original program), mostly reflecting an upward revision in spending in goods and services due to the broadening of fiscal coverage and cross-liabilities compensation mentioned above. The significant increase in capital outlays projected for 2020 reflects the authorities' plan to improve public investments' execution rate, and the beginning of the water and sanitation project for Santiago island, originally planned for 2019.

10. Budget execution will benefit from planned public financial management and other fiscal reforms. Key measures for 2020 include the introduction of electronic billing, and the adoption of the plan for public acquisitions and E-procurement. The Medium-Term Fiscal Framework will also be enhanced with technical assistance from the World Bank. Staff welcomed the authorities' resolve to continue using the Treasury cashflow monitoring plan as well as the PAYLOG system as important tools to strengthen expenditure management and prevent accumulation of payment arrears. It encouraged them to maintain the past practice of mid-term review of budget execution to identify corrective measures needed to safeguard the achievement of fiscal targets.

11. Staff reached understandings with the authorities on the preparation of a comprehensive conceptual framework before the SPIGF becomes operational (PS ¶ 26-28, Box 1). During the discussions, the authorities explained that the use of resources from the offshore TF to set up a SPIGF and an emergency fund was driven by three main factors: (i) help facilitate access to finance for capital-intensive private investments; (ii) avoid flooding an already over-liquid banking system, with 5.7 percent of GDP if resources from the TF were to be used to repay immediately the TCMFs;[3] and (iii) improve the country's preparedness to respond to exogenous shocks that proportionately affect vulnerable groups. The authorities stressed that these resources present a unique opportunity for Cabo Verde to support private sector development and enhance growth prospects. Staff took the view that several aspects of the SPIGF raised concerns, particularly regarding potential quasi-fiscal risks if guarantees were to be called, uncertainties on yields from the fund in relation with the coverage of liabilities, and potential mismatch between assets and liabilities stemming from the allocation of resources from the TF. Consequently, staff called for a more comprehensive approach that would provide clarity on issues related to assets management and liabilities coverage. In this context, the authorities will prepare a Strategy Note (**new reform target**) addressing: (i) the issuance and repayment of bonds replacing the TCMFs; (ii) the statistical recording of assets and liabilities in public finance statistics and; (iii) key aspects of the legal framework that would govern the management and operations of the SPIGF as specified in the PS. The authorities indicated that a number of issues raised by staff were covered in the law creating the SPIGF. This notwithstanding, in consultation with staff, they will prepare the Strategy Note in time for the second PCI review.

B. Monetary Policy and Financial Sector Reforms

12. The BCV believes that the current monetary policy stance is appropriate (PS ¶ 29). In the current environment of low inflation, continued fiscal consolidation efforts, and adequate reserves, the BCV maintained the policy rate at 1.5 percent, while closely monitoring developments that may require a change in monetary policy stance. Staff supported the approach and encouraged the BCV to continue building precautionary reserves to enhance resilience to exogenous shocks and protect the peg.

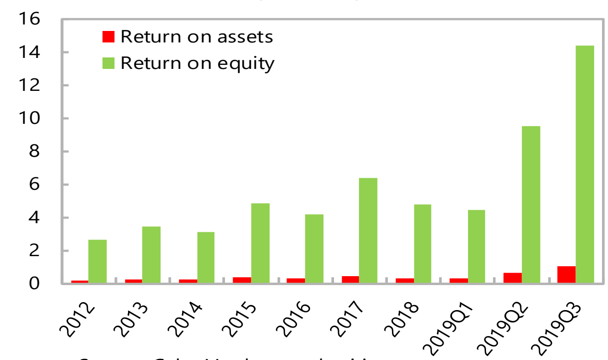
13. Staff welcomed measures introduced to improve monetary policy transmission mechanism (PS ¶ 30). In June 2019, the BCV reduced the overnight interest rate corridor to 150 basis points and established a symmetric interest rate corridor with overnight rates linked directly to the policy rate. The BCV noted that, thanks to this measure and increased competition in the market, there was some decline in banks' lending rates (about 0.4 percent) during June-September 2019. To enhance communication on monetary policy orientation, the BCV started publishing in July, the minutes of the Monetary Policy Committee meetings.

[3] At end-September 2019, excess liquidity in the banking system stood at 15 percent of deposits, equivalent to 13.9 percent of GDP. Injecting another 5.7 percent of GDP through the full repayment of TCMFs could be destabilizing. It is worth noting that in this high liquidity environment, investment opportunities for banks are limited as demand for credit from good borrowers is low, and the government has been reducing domestic borrowing in the securities market where banks are the main investors.

14. The authorities have decided to recapitalize the BCV (PS ¶ 31). At end-2018, the BCV's equity position was negative (CVE -2.7 billion). Contributing factors have been unfavorable income, and revaluation of assets in US dollars. In recent years, income opportunities declined, partly because the banking system is over-liquid. The authorities are planning to recapitalize the BCV with CVE 2.1 billion during 2019–21. While welcoming this measure, staff called for more resources to be committed if the recapitalization is to deliver the expected results and given the widening negative equity gap.[4] A safeguards assessment of the BCV is expected before the end of the year.

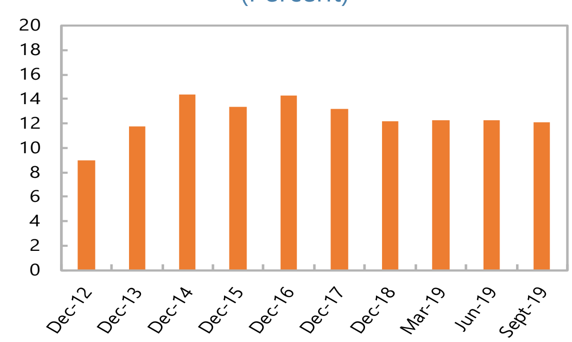
15. Financial stability indicators continue to improve (Text Figures 3, 4; Table 5, PS ¶ 32). Banks are well-capitalized, and their profitability has been improving. The regulatory capital to risk-weighted assets has increased in recent years, standing at 17 percent at end-September 2019, well-above the regulatory minimum of 12 percent. The reduction in funding costs has contributed to higher return on assets and on equity. However, assets quality remains weak with non-performing loans (NPLs) reaching 12 percent of total loans at end-September 2019. Staff reiterated the need for the BCV to continue working with banks to reduce the stock of legacy loans (70 percent of total NPLs) to foster credit growth. The BCV noted that some banks had written-off some legacy loans, and that compliance with foreclosure regulations is being monitored.

Text Figure 3. Earnings and Profitability of Commercial Banks
(Percent)



Source: Cabo Verdean authorities.

Text Figure 4. Total Non- Performing Loans
(Percent)



Source: Cabo Verdean authorities.

16. Staff welcomed the authorities' continued resolve to accelerate financial sector reforms (PS ¶ 33). It noted that the focus on deepening financial intermediation, enhancing risk-based supervision and facilitating access to finance was appropriate. Key actions planned for 2020 include: (i) operationalizing the credit registry and information system (**Reform Target**); (ii) setting up a functional central registry of mobile collateral (**Reform Target**); (iii) developing a centralized official balance sheets database for the corporate sector, to facilitate banks' risk assessment and; (iv) establishing the National Commission for the development of the financial system. In addition, the authorities reaffirmed their plan to sell the shares acquired in Caixa

[4] BCV's capital level of CVE 200 million remains low; more resources for recapitalization would need to be planned even if BCV's profitability improves.

Economica in 2019 (PS ¶ 7). They indicated that discussions are ongoing with a potential investor, and that selling these shares through the Stock Exchange was also being considered.

17. Cabo Verde has been able to maintain correspondent banking relationships (CBRs). Loss of CBRs in recent years has been marginal and mostly related to US dollars transactions. Nonetheless, given the economy's dependence on migrant deposits and remittances, staff stressed the importance of continued implementation of the AML/CFT framework in line with FATF requirements to avoid loss of CBRs. In this context, staff welcomed the authorities' plan to establish a national commission by end-2020, to evaluate AMF/CFT risks.

C. Structural Reforms

18. Advancing structural reforms, particularly in the SOEs sector remains an important priority to enhance growth prospects and build resilience to shocks (PS ¶ 34,35).

- *Building on recent progress*. Staff encouraged the authorities to build on progress made in 2019 to press ahead with SOEs reforms. It noted in particular the case of the airline company (Cabo Verde Airline – CVA) which, since privatization in March 2019, has established its hub in Sal island as anticipated, and opened new routes in Africa as well as North and South America. Staff stressed that measures taken so far, including improved oversight mechanism to monitor the financial performance of key SOEs, and compilation of financial information on their cash flow performance provide an important platform to detect inefficiencies in SOEs and take corrective measures to continue reducing fiscal risks.

- *Completing the 2020 agenda*. Although the timeline has been updated, the 2020 reform agenda for SOEs covers the privatization of four companies in the following sectors: energy (ELECTRA), health (INPHARMA, EMPROFAC), and transport (CV Handling); and the granting of concessions for port (ENAPOR) and airport (ASA) services. Other than ELECTRA for which cost cutting measures are being implemented to prepare the company for privatization, the other SOEs have positive income positions and are expected to generate some privatization revenue. While determined to complete these reforms by end-2020, the authorities have cautioned that market-related factors beyond their control may generate delays.

- *Advancing broader structural reforms.* Key actions under the PEDs aim to improve the business environment, contribute to skills building through reforms in the education system and increased vocational training, and to support small and medium-sized enterprises (SME). The authorities put in place in 2019, a financial ecosystem comprising three institutions that seek to facilitate access to finance for SMEs through loan guarantees (*Pro Garante)*; venture capital (*Pro Capita)* and capacity building (*Pro Empressa*). The three institutions are expected to become fully operational in 2020.

PROGRAM MODALITIES

19. Modification of quantitative targets. Based on updated projections for 2020, staff revised the quantitative targets for the second review (end-March 2020) and the third review (end-September 2020) on tax revenue, primary balance, net other liabilities, new concessional external debt of the central government, and net international reserves. The modification is supported by:

- The disbursement of a loan financing a water and sanitation project for Santiago island, delayed from 2019 to early 2020, which affects two targets: the floor on the primary balance and the ceiling on the nominal level of new concessional external debt of the central government.
- The updated level of capitalization and onlending operations, which affects the target on net other liabilities at end-March.
- A better targeting of quarterly revenue collection, which leads to a lower-than originally programmed floor on tax revenue for end-September.
- Revised projections for the external position, which will support a higher level of reserve accumulation at end-September.

20. New reform target (RT). As explained above, a new RT is proposed for end-April 2020, on the preparation of a Strategy Note related to the operationalization of the Sovereign Private Investment Guarantee Fund in line with best practice. Staff continues close discussions with the authorities and stands ready to provide technical advice on this matter as needed.

21. Other program issues:

- The 2020 program is fully financed with loans from the World Bank and the African Development Bank, and government securities issued in the domestic market in line with the country's regulation that caps total issuance to 3 percent of GDP.
- Cabo Verde does not face present, potential or prospective balance of payments needs, and the authorities are not seeking IMF financial support.
- Risks to the economic outlook discussed above are also relevant for program performance.

STAFF APPRAISAL

22. The authorities deserve credit for maintaining the reform momentum as well as efforts to enhance macroeconomic stability. The implementation of the authorities' PEDS is proceeding well and reforms are being undertaken. All reform targets for the first program review were met and all, but one, quantitative targets at end-September 2019 were achieved. The economy continues to perform well with strong growth, low inflation and improving external position. Although there are important downside risks, medium-term prospects are positive. Expected sustained activity in tourism, industry, and services, combined with planned infrastructure projects and structural reforms underpin the favorable growth projections. Staff encouraged the authorities to remain vigilant and stand ready to take needed mitigating measures should identified downside risks materialize.

23. The continued improvement in the fiscal position is welcome. Budget execution has been in line with the programmed fiscal primary surplus that is needed to contain debt accumulation. Staff urged the authorities to advance decisively with revenue-enhancing measures, calling in particular for increased efficiency gains in tax administration, strengthened monitoring of fiscal risks, increased compliance with tax obligations, and streamlined exemptions. Meeting medium-term fiscal objectives also requires continued restrain on current expenditures and improved management for capital outlays. In this context, staff emphasized the need to strengthen procurement procedures to increase public investments execution rate and efficiency.

24. Reducing the public debt-to-GDP ratio remains a key objective for the medium term. Continued strong growth prospects, sustained fiscal consolidation, successful SOEs reforms, and continued reliance on concessional financing are essential to help bring the debt-to-GDP ratio below 100 percent over the medium term, and contribute to a reduction in Cabo Verde's risk of debt distress, as highlighted in the 2019 IMF/World Bank debt sustainability analysis. However, the creation of the SPIGF could impact progress in this regard.

25. Staff welcomed the authorities' plan to prepare a Strategy Note ahead of the operationalization of the Sovereign Private Investment Guarantee Fund and urged its swift preparation. The Note is essential to ensure that critical aspects of assets management and liabilities coverage related to the use of the offshore trust fund set up in 1998 will be thoroughly addressed. Of particular importance will be sound governance and safeguards mechanisms needed to support the efficient functioning of the SPIGF, and the repayment plan for bonds backed by resources in the offshore account.

26. The monetary policy stance remains appropriate and recent measures to improve the monetary policy transmission mechanism are welcome. Staff concurred with the BCV that in the current environment of low inflation and adequate level of reserves, a change in the monetary policy stance was not warranted. As in the past, the BCV should continue to closely monitor developments in the euro area and stand ready to tighten monetary policy if pressures on reserves and prices emerge. The recent narrowing of the overnight interest rates corridor has contributed to some lowering of lending rates, a welcome development given the tepid credit expansion.

27. Maintaining correspondent banking relationships is important given Cabo Verde's dependence on remittances and migrant deposits. It is therefore encouraging that the country has been able to maintain CBRs in recent years. Staff stressed that it was essential to continue the implementation of the AML/CFT framework in line with FATF requirements to prevent loss of CBRs.

28. Staff welcomed progress in structural reforms. Decisive actions taken in 2019 to privatize and restructure SOEs, particularly for air and maritime transportation, and to enhance monitoring of their financial situation have had encouraging results. They should serve as a stepping stone to advance the remaining reform agenda. Staff encouraged the authorities to advance broad-based reforms to support private sector development, particularly small and medium-sized enterprises, to enhance growth prospects.

29. Staff supports the completion of the first review under the PCI and the modification of quantitative targets. At end-September 2019, all quantitative targets were met except for the floor on tax revenue. The nonobservance was minor and caused by lower-than-projected taxes on international trade. All reform targets were met. In view of this performance and the authorities' commitment to policies and reforms needed to foster macroeconomic stability, presented in their revised Program Statement, staff supports the completion of the first PCI review and the modification of quantitative targets for the second and third reviews.

Proposed Decision

The following decision, which may be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

1. Pursuant to paragraph 7 of Decision No. 16230-(17/62), adopted July 14, 2017, and paragraph 1 of the Policy Coordination Instrument for Cabo Verde ("PCI") EBS/19/68, Sup. 4, the Fund has conducted a review to assess program implementation.

2. The Program Statement dated February 20, 2020 (the "February 2020 Program Statement") and its attached Technical Memorandum of Understanding ("February 2020 TMU") shall be attached to the PCI, and the Program Statement dated June 21, 2019, together with all of its attachments, shall be read as supplemented and modified by the February 2020 Program Statement and the February 2020 TMU.

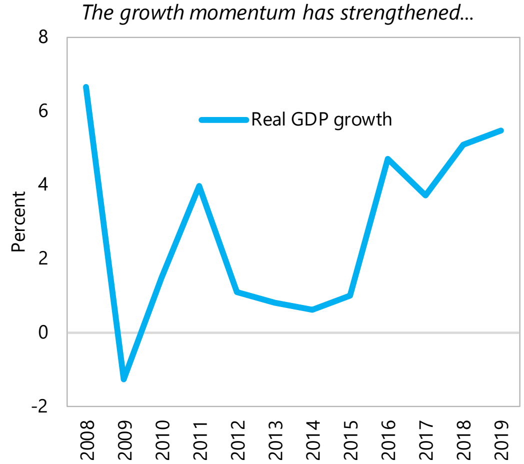
3. Accordingly, the end-March 2020 and end-September 2020 quantitative targets, the standard continuous targets, and the reform targets under the PCI shall be as specified in Table 1 and Table 2 attached to the February 2020 Program Statement and as further specified in the February 2020 TMU.

4. In paragraph 3 of the PCI the references to "Program Statement" and "TMU" shall be replaced with "February 2020 Program Statement" and "February 2020 TMU", respectively.

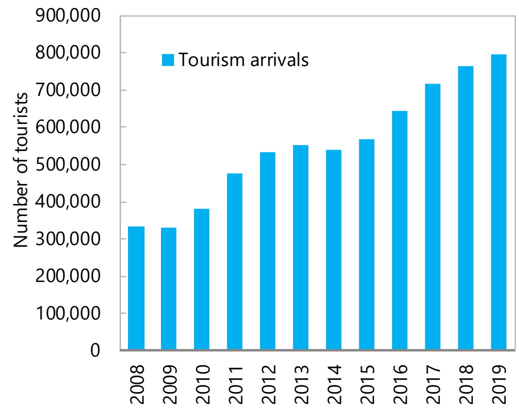
5. The Fund completes the first review specified in paragraph 1 of the PCI on the condition that the information provided by Cabo Verde on its performance under the Quantitative Targets and Standard Continuous Targets related to this review is accurate.

Figure 1. Cabo Verde: Recent Economic Developments

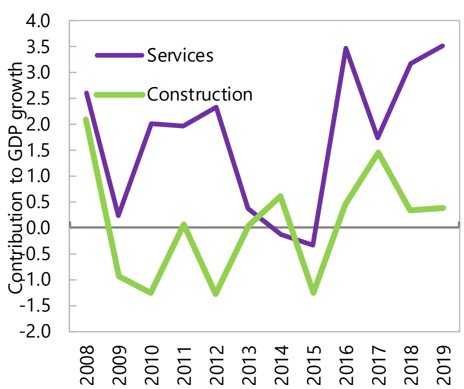
The growth momentum has strengthened...



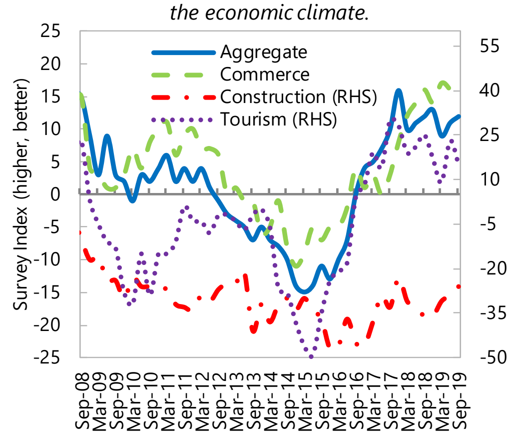
...thanks to strong performance in tourism...



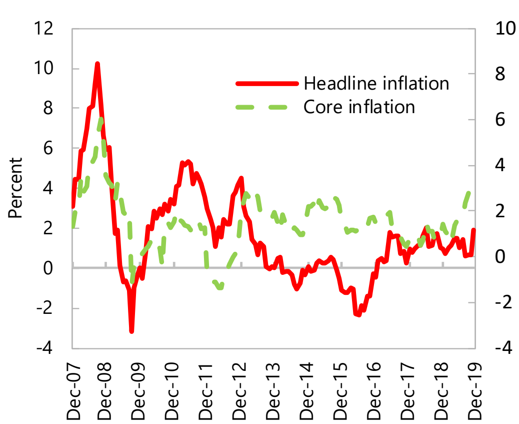
... and in services and construction.



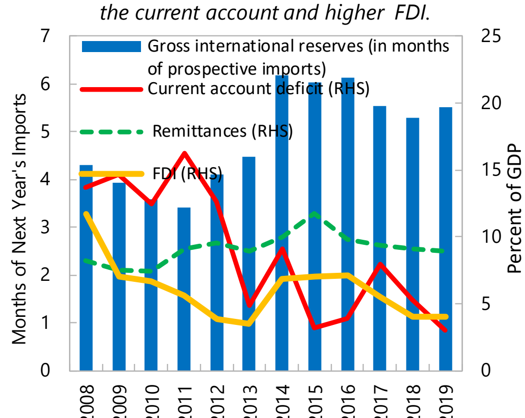
Confidence indicators point to improvement in the economic climate.



Headline inflation has increased reflecting mainly higher food prices.



Reserves have increased reflecting the improvement in the current account and higher FDI.



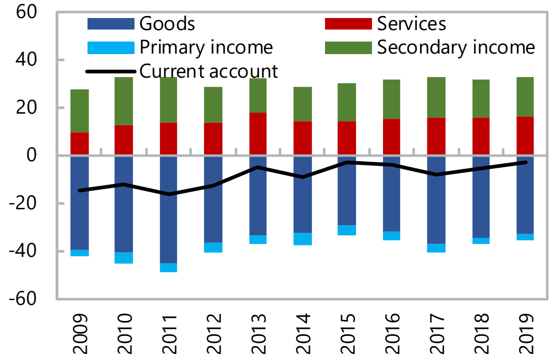
Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 2. Cabo Verde: External Sector Developments

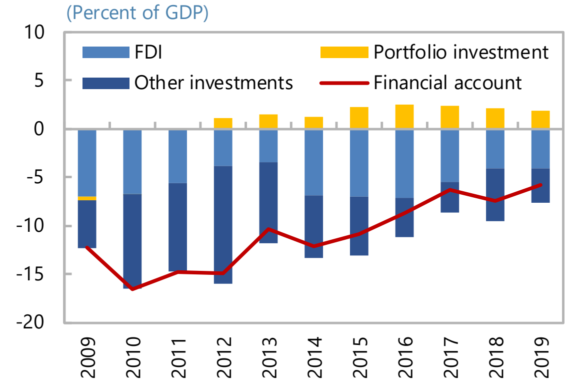
Current account deficit has narrowed owing to an increase in exports and a deceleration in imports.

… the deficit has been financed mainly by foreign direct investment and other investments.

Current Account Balance
(Percent of GDP)



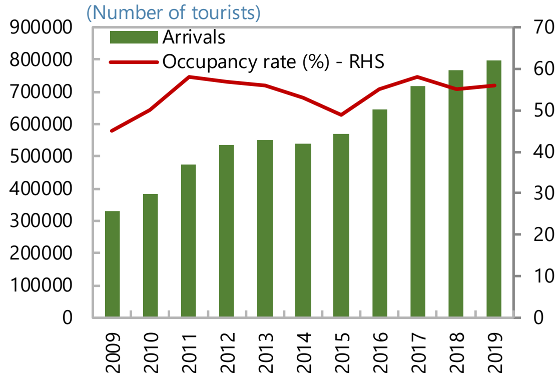
Financial Account Composition
(Percent of GDP)



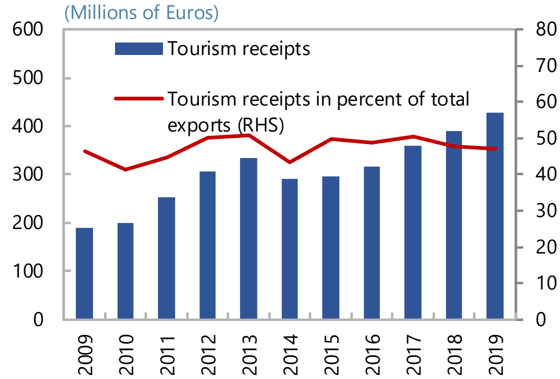
Tourism arrivals steadily improved in recent years …

… as a result tourism receipts continue to be a significant contributor to export performance.

Tourism Arrivals and Occupancy Rate
(Number of tourists)



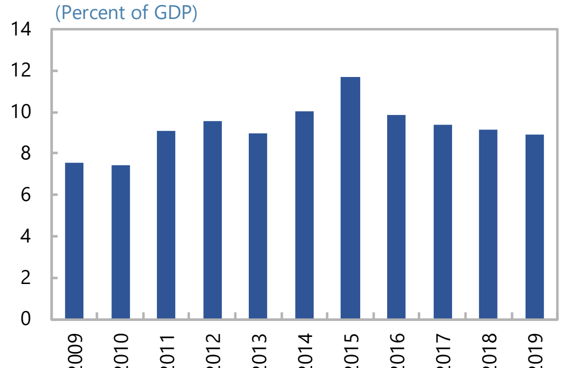
Tourism Receipts
(Millions of Euros)



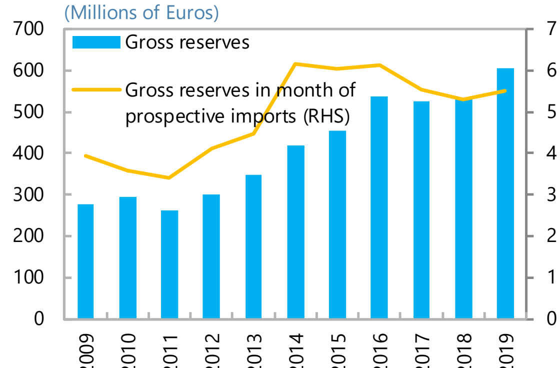
Remittances remain an important source of foreign currency …

… supporting the country's strong reserve position.

Remittances
(Percent of GDP)



Reserves
(Millions of Euros)

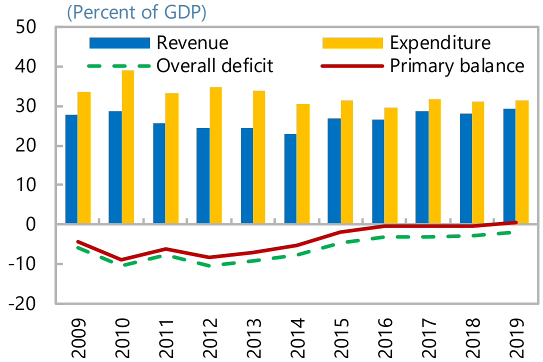


Sources: Cabo Verdean authorities; and IMF estimates.

Figure 3. Cabo Verde: Fiscal Sector Developments

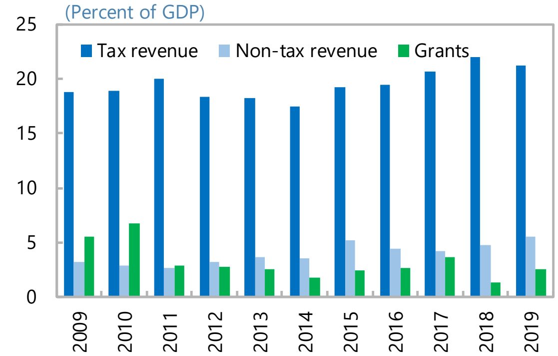
Fiscal perfomance has continously improved in recent years....

Fiscal Performance
(Percent of GDP)



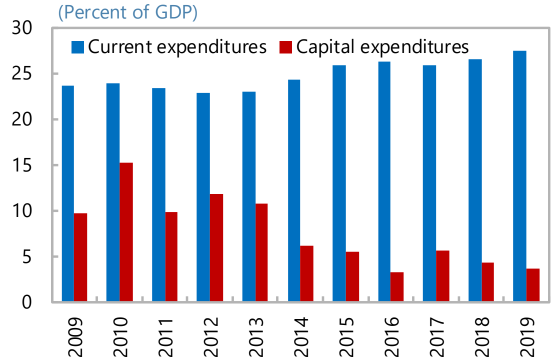
... owing to strong performance in tax revenue that compensated for the decline in grants...

Revenue Composition
(Percent of GDP)



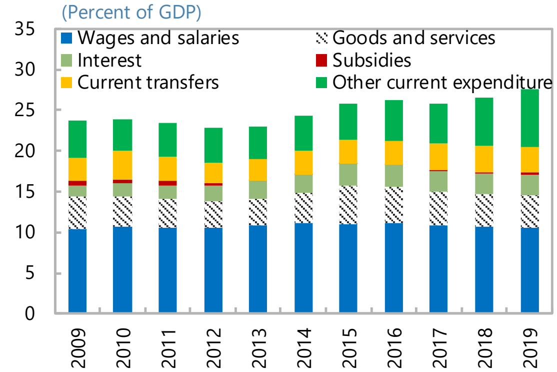
... and a decline in capital expenditures.

Expenditure
(Percent of GDP)



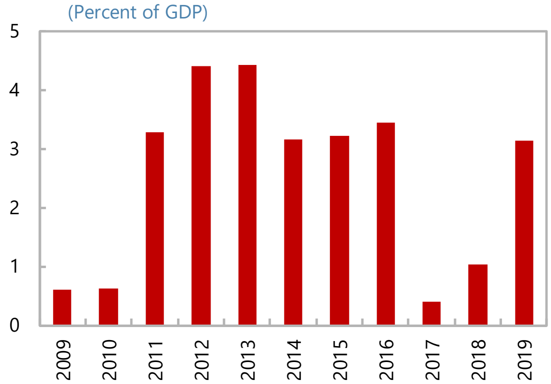
Wages and salaries remain the largest component of current expenditures.

Current Expenditure Composition
(Percent of GDP)



Net other liabilities increased in 2019 mainly reflecting support to SOEs and municipalities...

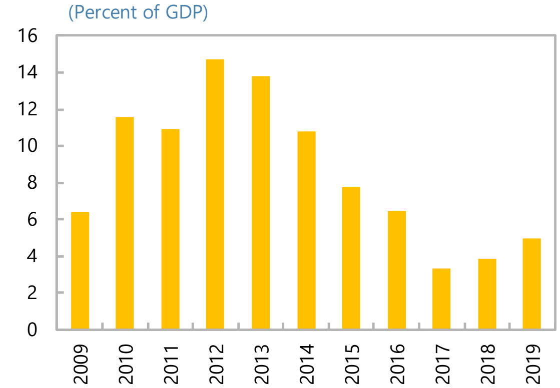
Support from the Budget to SOEs[1/]
(Percent of GDP)



[1/]Includes onlending and capitalization.

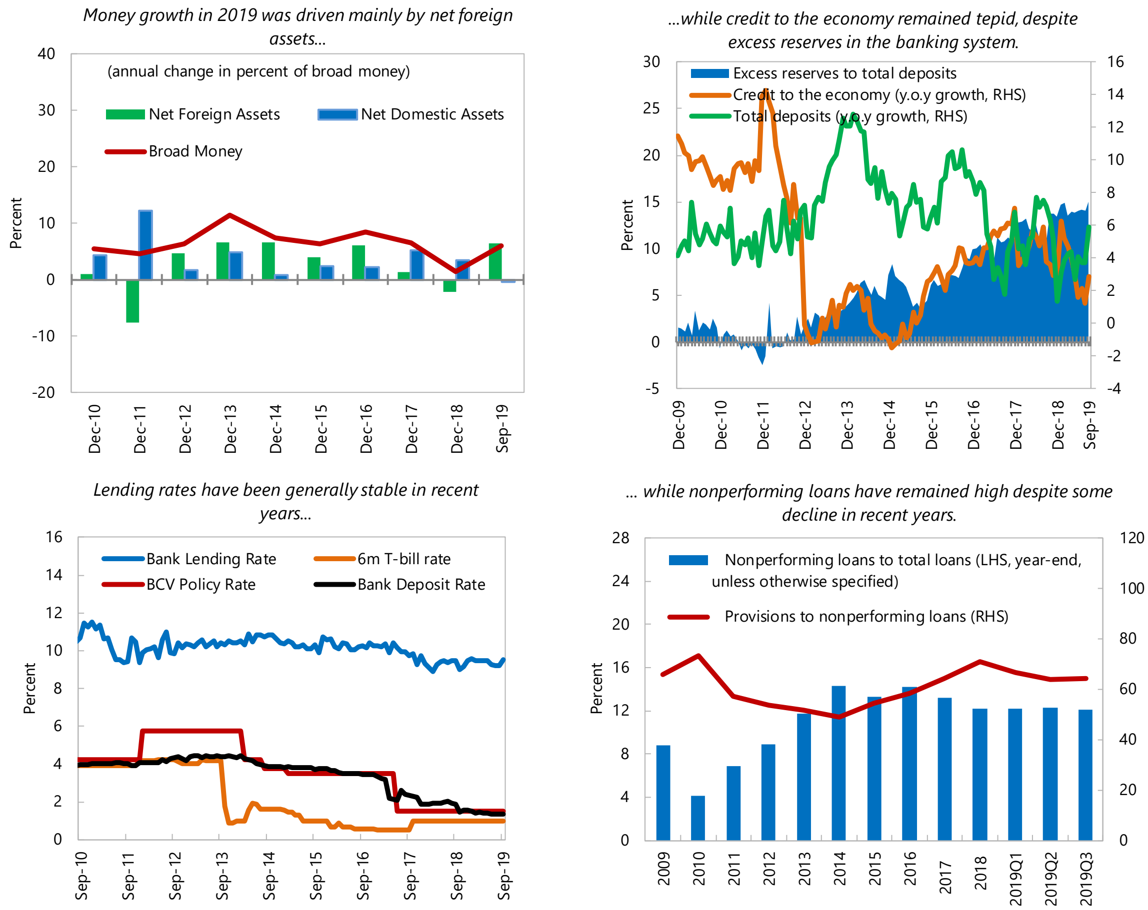
... contributing to an increase in financing needs.

Financing Needs
(Percent of GDP)



Sources: Cabo Verdean authorities; and IMF staff estimates.

Figure 4. Cabo Verde: Monetary Developments



Sources: Cabo Verdean authorities; IMF staff estimates.

Table 1. Cabo Verde: Selected Economic Indicators, 2017–24

	2017	2018	2019		2020		2021	2022	2023	2024
		Prel.	Prog.	Proj.	Prog.	Proj.		Proj.		
					(Annual percent change)					
National accounts and prices 1/										
Real GDP	3.7	5.1	5.0	5.5	5.0	5.0	5.0	5.0	5.0	5.0
GDP deflator	0.7	1.5	1.5	1.4	1.6	1.4	1.6	1.8	1.8	1.9
Consumer price index (annual average)	0.8	1.3	1.2	1.1	1.6	1.3	1.4	1.8	1.8	1.8
Consumer price index (end of period)	0.3	1.0	1.0	1.9	1.6	1.3	1.4	1.8	1.8	1.8
External sector										
Exports of goods and services	9.5	15.0	8.9	11.3	10.0	9.2	9.8	9.8	9.9	9.9
Of which: tourism	13.0	8.8	8.1	9.9	9.8	9.5	11.3	12.2	10.0	8.4
Imports of goods and services	16.7	8.4	8.7	6.4	8.7	9.1	7.5	7.9	7.3	7.2
					(Change in percent of broad money, 12 months earlier)					
Money and credit										
Net foreign assets	1.3	-2.1	2.0	3.4	2.8	2.5	1.9	1.9	2.5	2.5
Net domestic assets	5.2	3.5	5.0	3.6	3.5	3.7	4.0	4.1	3.7	3.5
Net claims on the central government	1.5	4.3	0.6	0.4	0.2	0.2	0.0	0.2	0.0	0.0
Credit to the economy	4.4	1.9	3.0	2.1	3.3	2.5	2.9	3.0	3.0	3.0
Broad money (M2)	6.5	1.4	7.0	7.0	6.3	6.2	5.9	6.0	6.2	6.1
					(Percent of GDP, unless otherwise indicated)					
Savings and investment										
Domestic savings	30.2	31.0	32.7	32.7	32.8	31.3	31.3	31.8	32.8	33.4
Government	0.9	1.8	2.3	1.4	2.3	1.7	2.1	2.6	3.4	4.0
Private	29.2	29.2	30.5	31.3	30.6	29.5	29.2	29.2	29.4	29.4
National investment	38.1	36.3	36.9	35.7	36.9	35.2	35.0	35.2	35.9	36.3
Government	5.7	4.4	5.1	3.7	4.3	4.6	3.6	3.9	3.9	4.2
Private	32.4	31.9	31.8	32.0	32.6	30.6	31.3	31.3	32.0	32.1
Savings-investment balance	-7.9	-5.3	-4.2	-3.0	-4.1	-3.9	-3.7	-3.4	-3.1	-2.9
Government	-4.8	-2.6	-2.8	-2.3	-2.0	-2.8	-1.6	-1.3	-0.4	-0.2
Private	-3.2	-2.7	-1.3	-0.7	-2.0	-1.1	-2.1	-2.1	-2.7	-2.7
External sector										
External current account (including official transfers)	-7.9	-5.3	-4.2	-3.0	-4.1	-3.9	-3.7	-3.4	-3.1	-2.9
External current account (excluding official transfers)	-11.4	-8.1	-7.5	-6.1	-7.1	-7.2	-6.3	-5.8	-4.8	-4.3
Overall balance of payments	-0.7	0.5	3.6	4.1	2.6	2.4	2.4	2.3	2.4	2.4
Gross international reserves (months of prospective imports of goods and services)	5.5	5.3	5.3	5.5	5.3	5.5	5.5	5.5	5.5	5.5
Government finance										
Revenue	28.6	28.2	31.7	29.4	30.4	32.5	31.2	30.0	29.1	29.0
Tax and nontax revenue	24.9	26.8	28.9	26.8	28.5	29.7	29.0	28.3	28.1	28.1
Grants	3.7	1.4	2.8	2.6	1.9	2.8	2.2	1.7	1.0	0.9
Expenditure	31.6	31.0	33.9	31.3	31.8	34.2	32.4	31.0	29.9	29.6
Primary balance	-0.4	-0.3	0.7	0.7	1.0	1.0	1.2	1.2	1.3	1.3
Overall balance (incl. grants)	-3.0	-2.8	-2.2	-1.9	-1.5	-1.7	-1.1	-1.0	-0.8	-0.6
Net other liabilities (incl. onlending)	-0.4	-1.0	-4.3	-3.1	-2.2	-2.2	-0.9	-0.7	-0.2	-0.1
Total financing (incl. onlending and capitalization)	4.0	3.8	6.5	5.0	3.7	3.9	2.1	1.7	1.0	0.7
Net domestic credit	0.2	1.4	1.0	0.8	0.4	0.4	0.1	0.4	0.0	0.1
Net external financing	4.0	1.5	5.5	4.2	3.3	3.6	2.0	1.3	1.0	0.7
Public debt stock and service										
Total nominal government debt	125.9	124.0	121.4	123.0	116.8	118.1	111.1	104.5	98.1	91.9
External government debt	93.8	91.0	89.3	90.6	86.3	87.2	82.8	78.3	73.9	69.4
Domestic government debt	32.2	33.1	32.1	32.4	30.5	30.9	28.3	26.1	24.2	22.5
External debt service (percent of exports of goods and services)	6.4	5.9	7.6	7.4	6.8	6.8	7.4	8.0	7.6	7.0
Present value of PPG external debt										
Percent of GDP (risk threshold: 55%)	...	60.6	64.0	62.9	62.4	62.1	59.5	56.7	53.8	50.9
Percent of exports (risk threshold: 240%)	...	123.8	128.2	123.6	121.4	118.8	110.7	102.6	94.9	87.4
Present value of total debt										
Percent of GDP (benchmark: 70%)	...	96.0	95.8	95.8	92.7	92.7	87.7	82.7	77.9	73.3
Memorandum items:										
Nominal GDP (billions of Cabo Verde escudos)	173.1	184.7	197.8	197.4	211.1	210.3	224.3	239.8	256.4	274.3
Gross international reserves (€ millions, end of period)	525.4	533.7	596.6	606.6	645.8	651.7	700.1	750.7	805.8	864.4

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

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

Table 2. Cabo Verde: Balance of Payments, 2017–24

(Millions of Euros; unless otherwise indicated)

	2017	2018	2019		2020		2021	2022	2023	2024
		Prel.	Prog.	Proj.	Prog.	Proj.	Proj.			
Current account	-125	-89	-75	-54	-78	-75	-75	-74	-72	-72
Trade balance	-583	-582	-636	-594	-696	-649	-705	-775	-830	-879
Exports, f.o.b.	167	232	253	277	276	309	336	352	381	422
Imports, f.o.b.	750	814	889	871	972	958	1041	1127	1211	1301
Consumer goods	270	278	303	314	327	337	359	386	417	451
Intermediate goods	156	158	176	161	192	178	198	212	228	247
Capital goods	131	99	111	103	123	115	127	138	150	163
Others (including fuel)	192	279	299	293	329	327	357	390	416	439
Fuel	69	82	77	76	80	82	83	84	87	86
Services (net)	245	263	293	295	335	323	378	441	503	564
Receipt	546	588	642	635	709	687	758	848	938	1028
Of which: tourism	359	390	407	429	447	470	523	587	645	699
Payment	301	325	349	340	374	364	380	407	435	464
Primary Income (net)	-54	-40	-54	-42	-65	-54	-52	-53	-55	-77
Of which: interest on public debt	-16	-17	-18	-18	-18	-18	-19	-20	-20	-21
Secondary Income (net)	267	270	322	287	348	305	305	312	310	321
General Government	54	46	60	55	58	64	53	53	38	34
Other Sectors	214	223	262	232	290	242	251	260	272	286
Of which: remittances	147	153	187	159	212	166	172	177	186	197
Capital account	16	13	22	22	9	17	20	13	13	14
Of which: Grants	13	11	20	20	7	14	18	10	10	12
Financial account 1/	-109	-115	-53	-32	-69	-58	-55	-61	-60	-58
Foreign direct investment	-87	-68	-72	-73	-105	-92	-116	-158	-167	-176
Portfolio investment	37	36	39	33	37	32	33	33	33	33
Other investment	-48	-93	-86	-65	-51	-42	-20	13	20	26
Net acquisition of financial assets	53	-70	-27	-36	-9	-15	-17	2	4	4
Net incurrence of liabilities	102	23	58	29	43	28	3	-10	-16	-22
Monetary authority	2	0	0	13	0	0	0	0	0	0
Central government	63	25	87	63	62	61	34	29	23	17
Disbursements	92	56	137	113	111	110	97	106	104	98
Amortization	-29	-32	-51	-50	-49	-49	-62	-77	-80	-82
Exceptional financing	0	0	0	0	0	0	0	0	0	0
Commercial banks	-4	4	5	5	4	4	5	5	5	5
Non-bank flows	41	-5	-34	-52	-23	-37	-37	-44	-44	-44
Reserve assets (+ accumulation)	-11	8	65	73	49	45	48	51	55	59
Errors and omissions 2/	0	-39	0	0	0	0	0	0	0	0
Overall balance	-11	8	65	73	49	45	48	51	55	59
Memorandum items:										
Current account (incl. official transfers, percent of GDP)	-7.9	-5.3	-4.2	-3.0	-4.1	-3.9	-3.7	-3.4	-3.1	-2.9
Current account (excl. official transfers, percent of GDP)	-11.4	-8.1	-7.5	-6.1	-7.1	-7.2	-6.3	-5.8	-4.8	-4.3
Overall balance (percent of GDP)	-0.7	0.5	3.6	4.1	2.6	2.4	2.4	2.3	2.4	2.4
Gross international reserves	525	534	597	607	646	652	700	751	806	864
Months of current year's imports of goods and services	6.0	5.6	5.8	6.0	5.8	5.9	5.9	5.9	5.9	5.9
Months of next year's imports of goods and services	5.5	5.3	5.3	5.5	5.3	5.5	5.5	5.5	5.5	5.5
External public debt	1492	1538	1602	1622	1653	1663	1684	1704	1718	1726
External aid (grants and loans, percent of GDP)	10.1	6.8	12.1	10.5	9.2	9.9	8.3	7.8	6.5	5.8
Nominal GDP	1570	1675	1794	1791	1914	1907	2034	2175	2325	2487

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

1/ Including international reserves and exceptional financing.

2/ Including banks' delays on trade credit reporting.

Table 3a. Cabo Verde: Statement of Operations of the Central Government, 2017–24[1]

(Millions of Cabo Verde Escudos)

	2017	2018	2019		2020		2021	2022	2023	2024
		Prel.	Prog.	Proj.	Prog.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	49,505	52,097	62,650	58,048	64,133	68,395	70,071	71,926	74,599	79,629
Tax	35,842	40,657	43,126	42,022	46,298	48,066	50,780	54,912	59,190	64,113
Taxes on income and profit	11,292	12,253	13,169	12,821	13,656	14,448	15,092	16,187	17,627	19,097
Taxes on goods and services	16,777	19,887	20,660	20,468	22,576	23,759	24,838	27,123	29,240	31,541
Taxes on international trade	7,224	7,733	8,466	7,984	9,199	8,972	9,904	10,600	11,255	12,333
Other taxes	549	784	830	749	867	887	946	1,002	1,067	1,141
Grants	6,389	2,575	5,479	5,127	4,070	5,959	5,041	4,110	2,488	2,490
Other revenue	7,273	8,865	14,045	10,899	13,765	14,370	14,250	12,904	12,921	13,026
Fees and penalties	498	433	297	388	295	375	388	400	400	407
Property Income	976	1,828	4,808	2,973	4,508	4,632	4,261	2,339	2,339	2,339
Sale of Goods and Services	5,189	5,732	7,896	6,777	7,956	8,256	8,577	9,114	9,155	9,237
Other (inc. social contributions)	610	873	1,045	761	1,005	1,108	1,023	1,051	1,026	1,043
Expenditure	54,650	57,301	66,972	61,717	67,197	71,965	72,626	74,346	76,581	81,283
Current expenditure	44,760	49,162	56,874	54,330	58,083	62,386	64,454	64,892	66,642	69,783
Compensation of employees	18,891	19,741	23,207	20,793	23,680	24,000	24,928	25,285	26,189	26,599
Use of goods and services	6,961	7,415	9,217	7,923	9,775	13,375	12,771	12,524	12,869	13,083
Interest	4,523	4,726	5,637	4,994	5,158	5,662	5,253	5,223	5,203	5,236
Domestic	2,684	2,811	3,406	3,056	3,025	3,337	3,054	2,964	2,889	2,873
External	1,790	1,822	2,128	1,849	2,036	2,229	2,103	2,162	2,218	2,266
Other Charges	50	93	102	89	97	96	97	97	97	97
Subsidies	124	153	579	579	588	729	691	716	726	746
Current transfers	6,001	6,283	5,682	6,040	6,964	6,477	7,481	7,070	7,728	8,534
Social benefits	5,541	6,237	6,963	7,443	7,429	7,486	7,717	8,165	8,777	9,393
Other expense (incl. capital transfer)	2,718	4,606	5,589	6,558	4,488	4,658	5,614	5,909	5,150	6,192
Net acquisition of nonfinancial assets	9,890	8,140	10,098	7,387	9,114	9,579	8,172	9,454	9,939	11,500
Purchase of assets	10,059	8,194	11,094	7,487	10,066	10,803	8,910	9,919	10,410	11,971
Sales of assets (-)	-168	-54	-996	-100	-952	-1,224	-738	-465	-471	-471
Primary balance	-622	-478	1,315	1,324	2,093	2,093	2,698	2,803	3,221	3,582
Overall balance	-5,145	-5,204	-4,322	-3,669	-3,065	-3,569	-2,555	-2,420	-1,982	-1,654
Net other liabilities	-615	-1,903	-8,511	-6,204	-4,674	-4,718	-2,061	-1,633	-499	-399
Onlending to SOEs for investment purpose	-4,098	-1,541	-2,992	-1,672	-2,152	-2,101	-1,197	-252	-643	-543
Other onlending (net)	4,565	3,606	-1,872	-454	-1,293	-1,294	144	-1,392	144	144
Disbursement	0	0	-2,057	-2,057	-1,437	-1,437	0	-1,536	0	0
Repayment	4,565	3,606	185	1,603	145	144	144	144	144	144
Capitalization	-1,157	-3,968	-3,667	-4,078	-1,229	-1,448	-1,056	0	0	0
Other	75	0	20	0	0	125	49	11	0	0
Financing needs	5,760	7,107	12,833	9,873	7,738	8,288	4,616	4,053	2,481	2,053
Total financing	7,197	5,239	12,833	9,873	7,738	8,288	4,616	4,053	2,481	2,053
Net domestic financing	273	2,517	2,029	1,521	851	797	127	870	-65	216
Net external financing	6,924	2,723	10,804	8,352	6,888	7,491	4,489	3,183	2,546	1,837
Disbursement	10,137	6,202	15,135	12,483	12,280	12,137	10,677	11,678	11,416	10,832
Budget Loans	2,205	2,205	6,085	6,148	3,116	3,136	3,320	3,124	3,124	3,124
Project and Program Loans	3,834	2,456	6,058	4,662	7,012	6,899	6,160	8,302	7,649	7,165
Loans to on lend to SOEs 2/	4,098	1,541	2,992	1,672	2,152	2,101	1,197	252	643	543
Amortization	3,213	3,479	4,331	4,131	5,392	4,645	6,188	8,495	8,870	8,995
Net errors and omissions (+ overfinancing)	1,437	-1,868	0	0	0	0	0	0	0	0
Memorandum items:										
Social Spending 3/	14,151	14,008	14,423	14,198	15,391	15,122	16,129	17,246	18,437	19,723
Total Public Investment	14,156	9,735	14,086	9,160	12,218	12,905	10,107	10,172	11,053	12,514
of which: public investment done by SOEs	4,098	1,541	2,992	1,672	2,152	2,101	1,197	252	643	543

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

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

2/ On lend to SOEs for public investment execution.

3/ Covering health, education, and social protection sectors, excluding compensation of employees.

Table 3b. Cabo Verde: Statement of Operations of the Central Government, 2017–24[1]

(Percent of GDP)

	2017	2018	2019		2020		2021	2022	2023	2024
		Prel.	Prog.	Proj.	Prog.	Proj.	Proj.	Proj.	Proj.	Proj.
Revenue	28.6	28.2	31.7	29.4	30.4	32.5	31.2	30.0	29.1	29.0
Taxes	20.7	22.0	21.8	21.3	21.9	22.9	22.6	22.9	23.1	23.4
Taxes on income and profit	6.5	6.6	6.7	6.5	6.5	6.9	6.7	6.7	6.9	7.0
Taxes on goods and services	9.7	10.8	10.4	10.4	10.7	11.3	11.1	11.3	11.4	11.5
Taxes on international trade	4.2	4.2	4.3	4.0	4.4	4.3	4.4	4.4	4.4	4.5
Other taxes	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Grants	3.7	1.4	2.8	2.6	1.9	2.8	2.2	1.7	1.0	0.9
Other revenue	4.2	4.8	7.1	5.5	6.5	6.8	6.4	5.4	5.0	4.7
Fees and penalties	0.3	0.2	0.2	0.2	0.1	0.2	0.2	0.2	0.2	0.1
Property Income	0.6	1.0	2.4	1.5	2.1	2.2	1.9	1.0	0.9	0.9
Sale of Goods and Services	3.0	3.1	4.0	3.4	3.8	3.9	3.8	3.8	3.6	3.4
Other (inc. social contributions)	0.4	0.5	0.5	0.4	0.5	0.5	0.5	0.4	0.4	0.4
Expenditure	31.6	31.0	33.9	31.3	31.8	34.2	32.4	31.0	29.9	29.6
Current expenditure	25.9	26.6	28.8	27.5	27.5	29.7	28.7	27.1	26.0	25.4
Compensation of employees	10.9	10.7	11.7	10.5	11.2	11.4	11.1	10.5	10.2	9.7
Use of goods and services	4.0	4.0	4.7	4.0	4.6	6.4	5.7	5.2	5.0	4.8
Interest	2.6	2.6	2.8	2.5	2.4	2.7	2.3	2.2	2.0	1.9
Domestic	1.6	1.5	1.7	1.5	1.4	1.6	1.4	1.2	1.1	1.0
External	1.0	1.0	1.1	0.9	1.0	1.1	0.9	0.9	0.9	0.8
Other Charges	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Subsidies	0.1	0.1	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Current transfers	3.5	3.4	2.9	3.1	3.3	3.1	3.3	2.9	3.0	3.1
Social benefits	3.2	3.4	3.5	3.8	3.5	3.6	3.4	3.4	3.4	3.4
Other expense (incl. capital transfer)	1.6	2.5	2.8	3.3	2.1	2.2	2.5	2.5	2.0	2.3
Net acquisition of nonfinancial assets	5.7	4.4	5.1	3.7	4.3	4.6	3.6	3.9	3.9	4.2
Purchase of assets	5.8	4.4	5.6	3.8	4.8	5.1	4.0	4.1	4.1	4.4
Foreign financed	4.5	3.1	3.9	2.2	3.3	3.5	2.9	3.1	2.7	3.1
Domestically financed	1.3	1.4	1.7	1.6	1.5	1.7	1.1	1.0	1.3	1.5
Sales of assets (-)	-0.1	0.0	-0.5	-0.1	-0.5	-0.6	-0.3	-0.2	-0.2	-0.2
Primary balance	-0.4	-0.3	0.7	0.7	1.0	1.0	1.2	1.2	1.3	1.3
Overall balance	-3.0	-2.8	-2.2	-1.9	-1.5	-1.7	-1.1	-1.0	-0.8	-0.6
Net other liabilities	-0.4	-1.0	-4.3	-3.1	-2.2	-2.2	-0.9	-0.7	-0.2	-0.1
Onlending to SOEs for investment purpose	-2.4	-0.8	-1.5	-0.8	-1.0	-1.0	-0.5	-0.1	-0.3	-0.2
Other onlending (net)	2.6	2.0	-0.9	-0.2	-0.6	-0.6	0.1	-0.6	0.1	0.1
Disbursement	0.0	0.0	-1.0	-1.0	-0.7	-0.7	0.0	-0.6	0.0	0.0
Repayment	2.6	2.0	0.1	0.8	0.1	0.1	0.1	0.1	0.1	0.1
Capitalization	-0.7	-2.1	-1.9	-2.1	-0.6	-0.7	-0.5	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0
Financing Needs	3.3	3.8	6.5	5.0	3.7	3.9	2.1	1.7	1.0	0.7
Total financing	4.2	2.8	6.5	5.0	3.7	3.9	2.1	1.7	1.0	0.7
Net domestic financing	0.2	1.4	1.0	0.8	0.4	0.4	0.1	0.4	0.0	0.1
Net external financing	4.0	1.5	5.5	4.2	3.3	3.6	2.0	1.3	1.0	0.7
Disbursement	5.9	3.4	7.7	6.3	5.8	5.8	4.8	4.9	4.5	3.9
Budget Loans	1.3	1.2	3.1	3.1	1.5	1.5	1.5	1.3	1.2	1.1
Project and Program Loans	2.2	1.3	3.1	2.4	3.3	3.3	2.7	3.5	3.0	2.6
Loans to on lend to SOEs 2/	2.4	0.8	1.5	0.8	1.0	1.0	0.5	0.1	0.3	0.2
Amortization	1.9	1.9	2.2	2.1	2.6	2.2	2.8	3.5	3.5	3.3
Net errors and omissions (+ overfinancing)	0.8	-1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Social Spending 3/	8.2	7.6	7.3	7.2	7.3	7.2	7.2	7.2	7.2	7.2
Total Public Investment	8.2	5.3	7.1	4.6	5.8	6.1	4.5	4.2	4.3	4.6
of which: public investment done by SOEs	2.4	0.8	1.5	0.8	1.0	1.0	0.5	0.1	0.3	0.2
GDP at current market prices (billions of CVEsc)	173.1	184.7	197.8	197.4	211.1	210.3	224.3	239.8	256.4	274.3

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

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

2/ On lend to SOEs for public investment execution.

3/ Covering health, education, and social protection sectors, excluding compensation of employees.

Table 4. Cabo Verde: Monetary Survey, 2017–24

(Millions of Cabo Verde Escudos, unless otherwise indicated)

	2017	2018	2019		2020		2021	2022	2023	2024
		Prel.	Prog.	Proj.	Prog.	Proj.	Proj.			
Net foreign assets	60,227	56,396	60,076	62,589	60,076	65,536	71,495	75,788	81,717	88,044
Foreign assets	86,730	83,533	87,678	88,786	87,678	93,531	98,616	103,452	109,934	116,825
Of which: gross international reserves	57,330	58,649	65,780	66,889	65,780	71,214	77,193	82,778	88,847	95,316
Foreign liabilities	-26,519	-27,233	-27,698	-26,293	-27,698	-28,091	-27,218	-27,760	-28,314	-28,878
Net domestic assets	120,878	127,234	136,456	133,822	136,456	143,291	149,364	158,397	167,035	175,833
Net domestic credit	145,938	156,614	162,715	157,713	162,715	169,682	170,670	177,892	185,166	192,876
Net claims on general government (net)	33,068	40,284	40,832	37,460	40,832	41,400	39,423	40,034	40,193	40,512
Investment in TCMFs 1/	11,053	11,070	11,070	4,637	11,070	4,637	4,637	4,637	4,637	4,637
Net claims on the central government	24,818	32,659	33,674	33,420	33,674	34,099	33,882	34,317	34,284	34,392
Credit to central government	35,920	46,866	47,881	47,627	47,881	48,306	48,089	48,524	48,491	48,599
Deposits of central government	-11,102	-14,207	-14,207	-14,207	-14,207	-14,207	-14,207	-14,207	-14,207	-14,207
Of which: project deposits	-47	-56	-56	-56	-56	-56	-56	-56	-56	-56
Net claims on local government and other agencies 2/	-1,938	-3,446	-3,913	-597	-3,913	-3,769	904	1,081	1,272	1,483
Credit to the economy	112,869	116,330	121,884	120,253	121,884	128,281	131,247	137,858	144,973	152,364
Other items (net)	-25,060	-29,380	-26,259	-23,891	-26,259	-26,391	-21,306	-19,495	-18,130	-17,043
Broad money (M2)	181,105	183,630	196,532	196,411	196,532	208,827	220,859	234,185	248,753	263,877
Narrow money (M1)	81,953	86,806	92,905	92,848	92,905	98,717	104,404	110,704	117,590	124,740
Currency outside banks	9,342	9,571	10,243	10,237	10,243	10,884	11,511	12,205	12,965	13,753
Demand deposits	72,612	77,235	82,662	82,611	82,662	87,833	92,894	98,499	104,626	110,987
Quasi-money	93,394	91,862	98,316	98,255	98,316	104,466	110,485	117,152	124,439	132,005
Foreign currency deposits	5,758	4,963	5,312	5,308	5,312	5,644	5,969	6,329	6,723	7,132
(Change in percent of broad money, 12 months earlier)										
Net foreign assets	1.3	-2.1	2.0	3.4	2.0	2.8	1.9	1.9	2.5	2.5
Net domestic assets	5.2	3.5	5.0	3.6	5.0	3.5	4.0	4.1	3.7	3.5
Net domestic credit	4.8	5.9	3.3	0.6	3.3	3.5	3.0	3.3	3.1	3.1
Net claims on the central government	1.5	4.3	0.6	0.4	0.6	0.2	0.0	0.2	0.0	0.0
Credit to the economy	4.4	1.9	3.0	2.1	3.0	3.3	2.9	3.0	3.0	3.0
Other items (net)	0.4	-2.4	1.7	3.0	1.7	-0.1	1.0	0.8	0.6	0.4
Broad money (M2)	6.5	1.4	7.0	7.0	7.0	6.3	5.9	6.0	6.2	6.1
Memorandum items:										
Emigrant deposits	63,251	63,869	68,154	68,112	68,154	72,418	76,590	81,212	86,263	91,508
Emigrant deposits/total deposits (percent)	36.8	36.7	36.6	36.6	36.6	36.6	36.6	36.6	36.6	36.6
Excess reserves/total deposits (percent)	11.1	13.4	…	…	…	…	…	…	…	…
Money multiplier (M2/M0)	3.2	3.2	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Money velocity (Nominal GDP/M2)	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Credit to the economy (percent change) 3/	7.0	3.1	4.8	3.4	4.8	4.1	4.8	5.0	5.2	5.1
Broad money (M2 in percent of GDP)	104.6	99.4	99.4	99.5	99.4	98.9	98.5	97.7	97.0	96.2

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

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

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

3/ Percent change, year over year.

Table 5. Cabo Verde: Financial Soundness Indicators of the Banking Sector, 2010–19
(End-year; percent unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019Q1	2019Q2	2019Q3
Capital adequacy												
Regulatory capital to risk-weighted assets	12.8	15.2	14.2	15.1	15.6	16.2	17.1	17.3	16.2	16.4	17.0	17.0
Regulatory Tier 1 capital to risk-weighted assets	13.0	15.9	13.9	13.7	14.4	15.0	15.9	16.4	16.1	16.5	17.1	17.0
Asset quality 1/												
Nonperforming loans to total loans	4.1	6.9	8.9	11.7	14.3	13.3	14.2	13.2	12.2	12.2	12.3	12.1
Nonperforming loans net of provisions to capital	17.1	40.2	47.9	53.5	62.8	49.4	42.5	35.0	26.0	31.2	32.8	29.9
Provisions to nonperforming loans	73.1	57.0	53.7	51.6	48.8	54.4	58.5	64.1	71.0	66.6	63.8	64.1
Earnings and profitability												
Return on assets	0.7	0.4	0.2	0.3	0.2	0.4	0.3	0.4	0.3	0.3	0.7	1.1
Return on equity	9.1	5.6	2.7	3.5	3.1	4.8	4.2	6.4	4.8	4.4	9.5	14.4
Interest margin to gross income	76.1	76.2	75.5	75.3	71.8	73.1	76.7	77.0	79.6	83.8	83.1	81.7
Noninterest expenses to gross income	67.0	68.5	76.5	78.1	72.5	75.8	66.4	60.2	69.6	52.1	52.4	50.6
Liquidity 2/												
Liquid assets to total assets	8.1	7.1	15.0	22.1	30.3	30.3	23.7	22.1	21.4	23.6	23.3	23.4
Liquid assets to short-term liabilities	10.5	9.7	21.1	29.0	37.3	37.0	28.6	26.6	25.5	28.4	27.9	27.1
Additional indicators												
Government deposits over total deposits	9.5	7.6	9.7	11.4	13.5	12.6	14.6	15.8	18.3	17.6	17.0	18.0
Demand deposits over total deposits	43.8	43.4	42.0	45.5	43.2	42.8	44.0	48.3	50.5	50.5	49.6	49.9
Total credit over total deposits	79.1	85.9	79.0	67.4	61.5	59.5	55.6	55.8	55.2	53.8	53.0	52.8
Personnel cost over cost of operations	49.0	49.9	50.1	48.4	54.8	56.6	58.8	58.3	66.6	58.7	57.6	58.8

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

Table 6. Cabo Verde: Schedule of Reviews Under the PCI, 2019–21		
Program Review	Test Date	Review Date
Board discussion of the PCI request		July 15, 2019
First Review	September 30, 2019	March 1, 2020
Second Review	March 31, 2020	September 2, 2020
Third Review	September 30, 2020	January 15, 2021

Appendix I. Program Statement

Praia, February 20, 2020

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

Madame Managing Director:

The government of the Republic of Cabo Verde has been implementing an ambitious reform agenda in the context of its Strategic Plan for Sustainable Development (PEDS), to improve growth prospects, reduce regional disparities and enhance the country's resilience to shocks. This reform agenda is supported by the International Monetary Fund (IMF) through the Policy Coordination Instrument (PCI) covering the period July 2019–January 2021, approved by the IMF Executive Board on July 15, 2019.

As indicated in the attached Program Statement (PS), economic and financial developments have been clearly positive, the outlook is favorable, and performance under the PCI has been strong. In particular, Cabo Verde's economy grew by 6.1 percent in real terms in the January-September 2019 period compared to the same period of 2018, according to preliminary data from the National Statistics Institute (INE). At the same time, inflation remained subdued, international buffers were comfortable, the public debt-to-GDP ratio continued to decline gradually, and the soundness of the banking sector improved. The government met all reform targets under the PCI, as well as all continuous and quantitative targets at end-September except for the floor on tax revenue that was missed by a small margin.

The government believes that policies and reform measures set forth in the attached PS are adequate to achieve the objectives of the PCI-supported program stated in the PS dated June 21, 2019. Nonetheless, the government will take any additional measures that may prove necessary to reach the program objectives. It will consult the IMF–at its own initiative or whenever the Managing Director requests such consultation–before adopting any such measures or in advance of revisions to the policies contained in the attached PS. Moreover, the government will continue to provide the IMF with such information as the IMF may request in relation with progress made in implementing the economic and financial policies and in achieving the program objectives.

Based on program performance presented in Tables 1 and 2 of the PS, as well as policies and reforms for 2020 outlined in the attached PS, we are requesting the completion of the first review of the PCI program for Cabo Verde by the IMF Executive Board, as well as the modification of quantitative targets for the second and third reviews.

Given the needed program ownership, we wish to make this letter available to the public, along with the PS and the attached Technical Memorandum of Understanding, as well as the Staff Report for the first review of the PCI program. Therefore, we authorize the publication of these documents and their posting on the IMF's official webpage, in accordance with IMF policies. We will also post these documents, including the Portuguese versions, on the government official webpage.

Sincerely,

/s/
Olavo Correia
Vice-Prime-Minister and
Minister of Finance

/s/
João Serra
Governor of the
Banco de Cabo Verde

Attachment: Technical Memorandum of Understanding.

Attachment I. Program Statement for the Period January 2020–January 2021

1. **This Program Statement (PS) sets out the economic program for 2020–21**. Consistent with medium-term objectives set out in the PS dated June 21, 2019, the economic program focuses on key areas of the government's reform agenda: strengthening the fiscal position, ensuring debt sustainability, enhancing the framework and implementation of monetary policy, fostering the stability of the financial system, and promoting durable and inclusive growth.

A. Recent Economic and Financial Developments

2. **Macroeconomic developments have been clearly positive in the last four years**. After lackluster growth during 2009–15, real GDP rose by 4.9 percent in 2016; 3.7 percent in 2017; 5.1 percent in 2018, and by 6.1 percent through the third quarter of 2019. This expansion has been driven by sustained activity in the construction, industry, commerce and tourism sectors. In 2019, growth also benefitted from the positive developments in the transport sector supported by reforms implemented during the year, including the privatization of the airline and the expansion of its international routes. Based on these developments, real GDP is expected to expand by 5.5 percent in 2019.

3. **Inflation has remained low**. After the spike in 2018 to 1 percent year on year (0.3 percent in 2017), inflation declined slightly to 0.7 percent in October 2019. However, it inched up to 1.9 percent at end-December mainly due to higher food prices.

4. **The external position strengthened further in 2019, contributing to the buildup of international reserves**. The current account deficit declined from 7.9 percent of GDP in 2017 to 5.3 percent of GDP in 2018 thanks to increased exports of goods, tourism receipts, and remittances, and because of deceleration in imports. The same trend continued in 2019, leading to a current account deficit of 1.5 percent of GDP at end-September. Gross international reserves rose to €630 million in September 2019, equivalent to 6 months of prospective imports of goods and services. Under the revised projections, the current account deficit would stand at 3 percent of GDP in 2019 and international reserves at €608 million. Final data on international reserves for 2019 show that they totalled €661 million at end-December.

5. **Money supply expanded by 5.2 percent at end-November compared with end-December 2018, while credit growth remained relatively low**. Growth in broad money was driven mainly by the strong increase in net foreign assets that more than compensated the decline in net domestic assets. Through end-November, credit to the economy rose only moderately (2.9 percent compared with end-December 2018). The weak expansion in credit to the economy can be explained by: (i) banks' prudent lending practices in an environment of high non-performing loans; (ii) reduced demand for credit by the airline company (Cabo Verde Airlines - CVA) following its privatization in early 2019, and by some State-Owned Enterprises (SOEs) that resorted more to external financing onlent by the central government; and (iii) the write-off of non-performing loans by some banks.

6. There were changes in banks' interest rates in the second half of 2019. In June 2019, the central bank (Banco de Cabo Verde – BCV) reduced the interest rate of the overnight lending facility from 4.5 percent to 3.0 percent to improve the effectiveness of monetary policy transmission mechanism. This change, combined with increased competition in the banking sector and improved perception of macroeconomic risks, supported some decline in lending rates. Banks' average lending rates declined from 10 percent in June to 9.6 percent in October, with a higher reduction at the short end of the market. During the same period, interests on deposits were stable.

7. The financial system remains sound. Banks are well-capitalized and profitable, and in compliance with prudential norms. However, their assets' quality continues to be affected by the high level of non-performing loans (12.1 percent at end-September 2019). In 2019, the government acquired 27 percent of shares in Caixa Economica from a foreign investment group to preserve correspondent banking relationships (CBRs). The government plans to sell these shares to private investors in 2020, in line with its reform agenda.

8. The stock of public debt is projected to decline further in 2019. Improvement in the fiscal position, and progress in the restructuring of loss-making SOEs have contributed to a decline in the ratio of public debt-to-GDP. From 125.9 percent of GDP in 2017, the ratio declined to 124 percent at end-2018, and it's projected to decline to 123 percent of GDP at end-December 2019.

B. Budget Execution at end-September and Projections for 2019

9. Budget execution has been in line with projections. Preliminary data show that at end-September, the primary surplus reached CVE 2.5 billion, much higher than projected. Total revenue stood at CVE 37.8 billion, below projections (CVE 41.6 billion) because of shortfalls in grants, taxes on international trade, and nontax revenue. Expenditures totalled CVE 39.2 billion, lower than the CVE 45 billion projected, mostly due to the slow execution of capital outlays caused by some procurement bottlenecks. As a result, the overall fiscal deficit was better than projected. Net other liabilities were also below projections due to lower disbursements of onlending to SOEs, repayment of CVE 1.4 billion by the airport management company (ASA), and a lower execution on capitalization. Consequently, financing needs totalled CVE 3 billion at end-September, well-below projections. Taking into account preliminary data at end-November, revised projections for 2019 indicate that both revenues and expenditures will be below target, and the programmed primary balance of 0.7 percent of GDP will be achieved, helping keep financing needs at 5 percent of GDP, lower than the projected level of 6.5 percent.

C. Performance Under the Policy Coordination Instrument

10. There was a strong performance in the implementation of the PCI program (Tables 1 and 2). The government met all reform targets and all non-quantitative continuous targets as well as all quantitative targets at end-September, except for the floor on tax revenue that was missed by a small margin.

11. All reform targets were met.

- The draft 2020 budget submitted to parliament in October and approved in December 2019 was in line with commitments under the PCI program, targeting a primary surplus of about 1 percent of GDP, needed to put the fiscal position on a stronger footing and to reduce the stock of public debt below 100 percent of GDP over the medium term.

- Financial information on cash flow performance of the six largest SOEs was compiled in July. This information will help improve fiscal reporting and manage fiscal risks generated by SOEs.

- The first quarterly report monitoring actual performance of six key SOEs against their budget was completed in December.

- The BCV started publishing the minutes of the Monetary Policy Committee meetings to improve communication on monetary policy. The first publication took place in June 2019, ahead of the July target date under the PCI program, and subsequent minutes were released within one month of the meeting as programmed.

- The reform target on reducing the overnight interest rate corridor to improve the monetary policy transmission mechanism was met well ahead of schedule. In June 2019, the BCV reduced the overnight corridor by 150 basis points by decreasing the margin on overnight lending rates. The overnight interest rate corridor is now symmetrical with overnight rates linked directly to the policy rate.

- A review report on exemptions was completed in December in the context of revisions to the tax benefits code.

12. Quantitative targets at end-September were met, except for the floor on tax revenue.

- The primary balance target was met, mainly because of under-execution of capital expenditure.

- The tax revenue floor was missed by a small margin because of lower-than-programmed taxes on international trade, consistent with lower than-anticipated imports of goods.

- The ceiling on net other liabilities was met. Net other liabilities stood at CVE 1.7 billion in September, compared with a target of CVE 6.3 billion.

- There was no accumulation of domestic or external payment arrears.

- The ceilings on nominal level of new concessional external debt of the central government was met, in line with budget execution at end-September.

- The zero limit on new nonconcessional external debt of the central government was observed.

- The floor on net international reserves was met with a wide margin.

13. All non-quantitative continuous targets under the PCI program were also observed. The government did not impose or intensify restrictions on the making of payments and transfers for current international transactions; it did not introduce multiple currency practices; it did not conclude bilateral payments agreement inconsistent with Article VIII; and it did not impose or intensify import restrictions for balance of payments reasons.

14. The following reform measures were also taken in 2019:

- The privatization of the airline company (TACV) through the sale of 51 percent of State's shares to a strategic partner in March, and the sale of 10 percent of the remaining shares (49 percent) in the new airline Cabo Verde Airlines (CVA) in December. As regulated by the relevant law, the 10 percent were offered to the company's staff and to Cabo Verdean living abroad.

- The completion of the restructuring of the housing program managed by the housing company (IFH).

- The granting of the concession for inter-island maritime transportation to the private sector, with 51 percent stake in the capital held by a foreign investor, and 49 percent held by domestic investors (July).

- The adoption by the Council of Ministers of the draft Central Bank Organic Law (December).

- The adoption by parliament of the law creating a Sovereign Private Investment Guarantee Fund (June).

- The signing and ratification of the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters (November).

- The activation of the settlement center for tax-related issues (December).

- The completion of the second phase of the VAT Monitoring Strategy (December).

- The introduction of the second phase of taxpayers' registration (December).

- The approval of the law creating the Council of National Public Finances (November).

D. Economic Policies and Structural Reforms for 2020–21

15. Government policies and reforms for 2020-21 will aim to support the achievement of medium-term objectives which are: enhancing revenue collection, strengthening expenditure management and advancing SOEs reforms to support fiscal and debt sustainability; improving monetary policy transmission mechanism; strengthening the financial system; promoting access to finance and improving the business climate to enhance growth prospects.

16. The sustained implementation of policies and reforms under the PEDS, which are reflected in the PCI program, is expected to improve medium-term prospects. Consequently, the economic growth momentum of recent years is expected to continue with the real GDP growth stabilizing at about 5 percent in 2020 and in the medium term. Continued dynamism in the tourism sector, and increased activity in the transportation sector are expected to boost growth. The latter will be driven by ongoing reforms in air and maritime transport, as well as the completion of key infrastructure projects, notably the construction of the port in Maio island and of the cruise ship terminal in Sao Vicente island. Progress in other structural reforms, particularly in the SOEs sector would also enhance medium-term growth prospects. Inflation is projected to remain below 2 percent on average, in line with the outlook in the euro area. The external current account is projected to improve further thanks to continued strong performance in exports of goods and services, notably tourism, and in remittances. International reserves are expected to remain above 5 months of prospective imports of goods and services in 2020 and in the medium term.

17. The economic outlook is subject to downside and upside risks. For Cabo Verde, downside risks are mostly related to weaker-than-projected global economic conditions, particularly in the euro area, potential increase in energy prices, the impact that uncertainties on Brexit might have on tourism activities from the UK (which accounts for some 25 percent of arrivals), and the impact of climate change and natural shocks. There are, however, some upside risks, including better-than-projected tourism performance, and more-than-anticipated increase in foreign direct investment. The government will endeavor to sustain fiscal consolidation and structural reform efforts and to take needed corrective actions if downside risks materialize.

E. Fiscal Policy and Debt Sustainability

18. The medium-term fiscal framework is built on continued improvement in the fiscal position to reduce the ratio of public debt to GDP in the medium term. Hence, the primary surplus is projected to increase from 0.7 percent of GDP in 2019 to 1.3 percent of GDP by 2024. To achieve these results, tax and nontax revenues are projected to be in the range of 28–29 percent of GDP during 2021-24, and total expenditures are projected to gradually decline from 32.4 percent of GDP in 2021 to about 30 percent of GDP in 2024, while preserving social and capital spending at around 7 percent of GDP and 4 percent of GDP respectively during the projection period. Taking into account the impact of SOEs reforms on onlending and capitalization, financing needs are projected to decline from 5 percent of GDP in 2019 to 0.7 percent of GDP in 2024, helping reduce the stock of public debt from about 123 percent of GDP projected in 2019 to 91.9 percent of GDP at end-2024. Fiscal reforms will continue to be implemented to support the achievement of these objectives, giving priority to modernizing the tax system and administration, broadening the tax base, improving compliance with tax obligations, and enhancing expenditure management, particularly for capital expenditure.

19. The 2020 budget is geared towards the achievement of the abovementioned medium-term objectives, which are also reflected in the PCI program. It targets a primary surplus of CVE 2.1 billion, equivalent to 1 percent of GDP, needed to contain financing needs and bring the ratio of public debt to GDP below 120 percent in 2020. To reach this target, tax and nontax revenues are projected at CVE 62.5 billion (29.7 percent of GDP), and grants at about CVE 6 billion (2.8 percent of GDP), while expenditures are budgeted at 34.2 percent of GDP as discussed below.

20. Revenue performance is expected to improve further in 2020. Total revenue is budgeted at CVE 68.4 billion (32.5 percent of GDP), increasing by over 10 percent compared with estimates for 2019. Tax revenue is budgeted at CVE 48.1 billion, an increase of over 14 percent compared with 2019, driven by the expected strong performance in tax on goods and services and tax on income and profits, which account for close to 80 percent of tax revenue; as well as the compensation of cross-liabilities estimated at CVE 1.7 billion. Non tax revenue is projected at CVE 14.4 billion. Improved collection in this category reflects expected privatization/concessions receipts (CVE 4.6 billion); higher revenue from sale of goods and services (CVE 8.3 billion) which reflects the impact of fees introduced in 2019 and other nontax revenue measures. Budgetary grants are projected at CVE 5.9 billion, which cover budget support for CVE 1.8 billion; food aid for CVE 212 million; and other grants including project-related grants for CVE 3.9 billion. The latter amount includes CVE 3.5 billion from the Netherlands' contribution to the cruise ship terminal construction project; the European Union's support for the competitiveness program; and Luxemburg's support for the internship and training programs for employability and for the water and sanitation sector program.

21. The expected strong economic growth and sustained implementation of reform measures will help achieve the revenue mobilization objectives. Collection of tax and nontax revenue will benefit from the projected economic expansion of 5 percent in 2020; the full year effect of tax measures introduced in 2019, notably the increase in the corporate income tax rate for offshore banks, and in excises on tobacco, sugarcane rum, soft drinks and juices; and the introduction of specific tax on packs of cigarettes; as well as the impact of new measures planned for 2020, which include:

- Improved digitalization of the tax administration for collection, inspection and audit.
- Enhanced penalty framework and deterrent measures.
- Reduction of informal activities notably through the introduction of incentives for the use of electronic payment systems.
- Strengthening of administrative and decision-making capacity in tax administration.
- Refocusing on management of financial and nonfinancial assets.
- Enhancing of post-customs clearance controls.

- Streamline exemptions on value-added tax, on import duties and on excises. Specific actions in this area will be based on the report adopted by the Council of Ministers in late 2019.

- Continued strengthening of tax arrears collection.

22. Expenditure amounts to CVE 72 billion (34.2 percent of GDP). Current spending amounts to CVE 62.4 billion, with mandatory expenditures accounting for about 81 percent covering wages and salaries, and common charges which comprise interests on public debt, transfers to municipalities, social security charges for civil servants, pensions and tax refunds.

- *Wages and salaries* are projected at CVE 24 billion (11.4 percent of GDP). The budgeted increase reflects the full year impact of 2019 measures in the education, judicial and health sectors (reclassification, recruitment, and promotion), new recruitments, and the impact of other measures in the civil service related to phasing-in and revision of special statutes (Army and Police), promotions and advancement (Police and Health sector), and expenditures covered with revenue from court fees.

- *Spending for goods and services* are projected at CVE 13.4 billion, equivalent to 6.4 percent of GDP. They increase significantly compared with 2019 estimates mainly reflecting the impact of: (i) the offsetting of accounts in relation with cross-debt compensation with some companies, including public enterprises (CVE 1.6 billion), which is a one-off item also reflected in revenues; (ii) the cost of local elections scheduled for 2020 (CVE 160 million); (iii) the broadening of fiscal coverage to other relevant public institutions (hospitals, universities, the judiciary, and security agencies); (iv) the counterpart funding of externally-financed investment (CVE 800 million); and the purchase of medical equipment (CVE 272 million).

- *Interests on public debt* is projected in line with changes in the stock of public debt. They are budgeted at CVE 5.7 billion, a moderate increase compared with 2019. With external debt contracted on highly concessional terms, interests on domestic debt continue to represent the highest share, about 59 percent of total charges on public debt.

- *Other non-interest current expenditures are budgeted* at CVE 19.3 billion, covering subsidies, current transfers, social benefits and other expenses.

23. Based on the efficient implementation of measures presented above, the fiscal position will improve further in 2020. The primary surplus is budgeted to increase from CVE 1.3 billion in 2019 to CVE 2.1 billion in 2020 (1 percent of GDP), while the overall balance is budgeted to narrow from CVE 3.7 billion (1.9 percent of GDP) to CVE 3.6 billion (1.7 percent of GDP). Taking into account the projected decline in other liabilities (net) from CVE 6.2 billion in 2019 to CVE 4.7 billion mostly because of a decline in capitalization, consistent with progress made in 2019 in public enterprises reforms, financing needs would decline from CVE 9.9 billion in 2019 (5 percent of GDP) to CVE 8.3 billion (3.9 percent of GDP). They would be covered mostly with net external financing totaling CVE 7.5 billion, mainly from the World Bank and the African Development Bank; and net domestic financing amounting to CVE 797 million from issuance of government securities.

24. Budget execution will be carefully monitored to safeguard the achievement of programmed objectives. It will be guided by a careful cash flow management to prevent accumulation of domestic and external payment arrears or unplanned debt accumulation. In the same vein, the PAYLOG system will be used to ensure that suppliers are paid within a maximum period of 45 days. In addition, if the midyear budget execution outturn points to a shortfall in budgetary resources, expenditures commitments will be curtailed in line with Cabo Verde law.

25. The government will take actions to further enhance public debt management. Capacity development will be pursued in collaboration with development partners, through training and technical assistance. In addition, the borrowing policy will be built on adherence to the zero limit on non-concessional external loans under the PCI program. The projected external borrowing for 2020 mostly covers infrastructure projects and budget financing (Table 3).

26. The government decided to create a fund to guarantee private investment using resources from the offshore Trust Fund (TF) set up in 1998. The TF (totaling some 106 million euros at end-December 2019) was set up in the context of a donor-supported domestic debt reduction operation. It was a counterpart to twenty-year bonds (TCMF - *Titulos Consolidados de Mobilizacão Financeira*) that were expected to be amortized through 2018. At the end of the 20-year period, it was decided, after negotiations with bond holders, to close the TF and to use the resources from it to create a Sovereign Private Investment Guarantee Fund (SPIGF), following a proposal originally laid out in the government's PEDS in 2017, and an Emergency Fund needed to support government's preparedness in responding to climate-related shocks. Parliament approved a law in late 2018 under which the TCMFs would be replaced by new bonds to be amortized in 20 years and remunerated at an interest rate of up to 3 percent. In June 2019, Parliament approved the law creating the SPGIF, which became effective in early August 2019, after promulgation by the President of the Republic. As of end-December 2019, the TCMFs were held by the BCV and the Pension Fund (INPS).

27. The creation of the SPIGF reflects the government's efforts to facilitate access to finance for the private sector, one of the key impediments to growth, without jeopardizing fiscal and public debt sustainability. Through the guarantee mechanism, the Fund is expected to help Cabo Verdean companies investing in capital-intensive sectors to secure access to international capital markets. The Fund is not operational yet and, upon operationalization, its initial financing capacity is estimated at no more than 5 percent of GDP.

28. The government is preparing a Strategy Note that will provide the conceptual framework addressing key issues on the asset and liability sides of the use of resources saved in the Trust Fund (new Reform Target). The Strategy Note will be completed by end-April 2020 and before the operationalization of the SPIGF, with support from IMF staff. It will cover the following key points:

- The treatment of TCMFs, notably the issuance of bonds that will replace them and the modalities of their repayment.

- The statistical recording of assets and liabilities in public finance statistics.
- The key components of the legal framework that would govern the management and operations of the SPIGF, to ensure that it will be in line with international best practice. To this effect, the Strategy Note will help clarify the following aspects of the SPIGF: (i) the governance arrangements for the administration of the fund; (ii) the asset management principles, and the selection criteria for projects for which a guarantee would be provided; (iii) the accumulation and withdrawal rules; (iv) the transparency and accountability mechanisms; (v) the revenues expected from the SPIGF and the projected costs of its liabilities; (vi) risks to the SPIGF net earnings position; and (vii) mechanisms to ensure that the fund is not loss-making.

F. Monetary Policy

29. Monetary policy will continue to be geared toward supporting price stability and protecting the peg to the euro. The BCV finds that the current monetary policy stance will help achieve these objectives, given the government continued fiscal consolidation efforts, low inflationary pressures, an adequate level of reserves, and low interest rates in the euro area. Therefore, the BCV intends to maintain the Monetary Policy Rate unchanged at 1.5 percent. Nonetheless, as in the past, the BCV stands ready to take any appropriate actions should macroeconomic conditions change in the euro area or domestically. The BCV will continue to strive to build precautionary reserves to protect the credibility of the exchange rate regime and meet the reserve accumulation target under the PCI. Its reserve target will continue to be set to cover about 30 percent of broad money.

30. The BCV will continue to take the necessary actions to improve liquidity management and enhance the monetary policy transmission mechanism. It will effectively implement measures introduced in recent years, particularly the reduction in the overnight interest rate corridor; the issuance of Monetary Regularization Securities (TRM) through fixed rate tenders instead of variable rate tenders to ensure a better linkage between TRMs' rate and the policy rate; and the timely release of minutes of the Monetary Policy Committee meetings to enhance communication on the policy orientation (**Continuous reform target**). Actions to strengthen near and medium-term forecasting capacity as well as monetary policy analysis at the BCV will continue in 2020, notably through the finalization of the composite index of economic activity and the framework for medium-term projections.

31. The government has decided to recapitalize the BCV. The recapitalization will help cover losses incurred by the central bank through end-2018, partly because of the revaluation of assets denominated in US dollars. The 2019 tranche (CVE 700 million) was released in late December; the 2020 budget has allocated CVE 300 million, and the last tranche is reflected in the MTFF for 2021-24.

G. Financial Sector Reforms

32. The financial system is stable and adequately capitalized, and banks are profitable, although assets quality remains relatively weak, and the system over-liquid. Financial stability indicators show that at end-September 2019, most prudential norms were met, and banks' profitability had improved. However, the level of nonperforming loans (NPLs), remains high at 12.1 percent of total loans (12.2 percent of total loans at end-2018). The BCV will continue to work with banks to address NPLs, and particularly legacy loans relating to default in loans that financed real estate projects in the tourism sector following the global financial crisis. Legacy NPLs represent the largest portion of NPLs. In addition, the financial system is over-liquid, consistent with the high level of emigrants' and the pension fund's (INPS) deposits, in an environment of low credit growth.

33. Financial sector reforms will continue to focus on deepening financial intermediation, enhancing banking supervision and facilitating financial inclusion. In this context, the following reforms will be put in place:

- Implementation the recommendations from the 2013 and 2015 asset quality review.
- Revamping of the public credit registry and information system by end-December 2020 (**Reform Target**). Key measures under this reform will cover the completion of the procurement and the development of the relevant software system.
- Creation of a functional central registry of mobile collateral by end-December 2020 (**Reform Target**).
- Strengthening of bank's lending standards and risk management practices through enhanced supervision.
- Development of a centralized official balance sheets database for the corporate sector to support risk-based supervision. In this context, the BCV plans to work with the National Statistics Institute (INE) to design financial indicators relevant for risk assessment, in relation with the banking system supervision.
- Improvement of the AML/CFT framework in line with FATF (Financial Action Task Force) requirements to limit further loss of correspondent banking relationships. To this end, a national commission will be established as recommended by the National Plan for Evaluation of AML/CFT Risk (December 2020). Continued negotiations to secure new correspondent banks.
- Ensure the proper functioning of the Financial Stability Committee. This includes the appointment of the Committee's participants and the establishment of an operating regulation and quarterly meetings.
- Ensure the functioning of the National Commission for the development of the financial system. For the effective operation of the Commission, the following actions will be taken: the

appointment of the Commission's members, the holding of periodic meetings, the definition of operating regulations, the adoption by the Council of Ministers of the Action Plan for the development of the financial system. The Commission is expected to prepare the Action Plan for the development of the financial system (June 2020).

- Implement the main recommendations of the report on access to financing for SMEs, dated February 2015. Priority actions will include: strengthening the public credit information systems, continued training to increase staffing and capacity of the banking supervision department, strengthening the BCV's capacity to carry out effective bank supervision by hiring additional staff with relevant expertise.

- Implement the measures specified by the EU, to keep the country off the gray list, in the sense of reducing the risk associated with the country. Key measures will include: becoming a member of the Global Forum and/or to have a satisfactory rating; putting in place a network of agreements covering all EU member states, amending or abolishing the harmful tax regimes, becoming member of the Inclusive Framework or implementing the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) minimum standard.

- Implement the recommendations made in the assessment by the EU in the Global Action on Cybercrime Extended, about combatting cybercrimes.

H. Public Enterprises Reforms

34. Public enterprises reforms will remain a key priority of the government's reform agenda. Building on progress made in 2019, the government will continue to reduce the State's role in productive activities and strengthen the financial position of SOEs to be restructured to significantly reduce fiscal risks. The following measures are planned for 2020:

- Sale of the remaining State's shares (39 percent) in CVA (First quarter).

- Privatization of: INPHARMA (June 2020); EMPROFAC (June 2020); ELECTRA (December 2020) and; CV Handling (June 2020).

- Licensing of port services through concession (ENAPOR, May 2020); establishment of a concession arrangement for airport services (ASA, June 2020).

- Complete a report on the liabilities of the privatized SOEs, outlining implications for the government budget.

- Prepare quarterly reports on the six key SOEs, analyzing their financial performance in comparison with their approved budgets (**Continuous reform target**).

I. Other Structural Reforms

35. The government will push ahead with the broader reform agenda under the PEDS. Priority will continue to be given to creating a business-friendly environment to support private sector development, particularly small and medium-sized enterprises, attract FDI, and create job opportunities. The following actions are planned for 2020.

- Facilitate access to finance, notably through a sharing of risks with the private sector. In this context, the financial ecosystem put in place by the government in 2019 will become fully operational with the three institutions working together to support small and medium-size enterprises through: (i) guarantees (*Pro Garante*, with World Bank support); (ii) venture capital (*Pro Capita* with commercial banks' participation) and; (iii) capacity development (*Pro Empressa*).

- Publication of the agenda for improving the business climate.

- Adoption of the agenda for promoting medium and small-sized enterprises and diversifying the economy.

- Expedite procedures for setting up businesses, particularly with respect to digital entry and indexing in the Commercial Register.

J. Program Monitoring

36. Program targets. Progress in the implementation of policies and reforms under the PCI will continue to be monitored through quantitative targets and standard non-quantitative continuous targets presented in Table 1, as well as reform targets presented in Table 2. Program quantitative targets are defined in the Technical Memorandum of Understanding attached to this Program Statement.

37. Program review. The second review of the program is scheduled to be completed by the IMF Executive Board no later than September 2, 2020; and the third and final PCI review no later than January 15, 2021.

Table 1. Cabo Verde: Quantitative Targets Under the PCI[1] (2019–20)

	Cumulative flows from the beginning of the year												
	2019							2020					
	end-June		end-September			status	end-December	end-March		end-June	end-September		end-December
	Proj.	Actual	Quantitative Targets (QT)	Adjusted QT	Actual		Proj.	Quantitative Targets (QT)	New Quantitative Targets (QT)	Proj.	Quantitative Targets (QT)	New Quantitative Targets (QT)	Proj.
Quantitative targets							(Millions of Cabo Verde escudos)						
Primary balance, floor [2]	456	1,551	841	-335	2,510	Met	1,324	644	-2,023	-1,705	1,388	-1,783	2,093
Tax revenue, floor	19,965	20,219	31,362	31,362	30,652	Not met	42,022	10,471	10,471	21,961	33,648	33,033	48,066
Net other liabilities, ceiling [3]	3,575	2,674	6,345	6,345	1,657	Met	6,204	872	1,022	2,700	3,611	3,611	4,718
Nonaccumulation of domestic arrears [4]	0.0	0.0	0.0	0.0	0.0	Met	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Non-accumulation of external payment arrears [4]	0.0	0.0	0.0	0.0	0.0	Met	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Nominal level of new concessional external debt of central government, ceiling	3,784	2,982	9,563	9,563	7,785	Met	12,483	1,122	3,822	5,928	8,330	8,975	12,137
							(Millions of US dollars)						
Nominal level of new nonconcessional external debt of central government, ceiling	0.0	0.0	0.0	0.0	0.0	Met	0.0	0.0	0.0	0.0	0.0	0.0	0.0
							(Millions of euros)						
Net international reserves, floor [2]	526	571	528	514	634	Met	606	572	572	589	566	600	652
Non-quantitative continuous targets													
Non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions						Met							
Non-introduction or modification of multiple currency practices						Met							
Not concluding bilateral payments agreement which are inconsistent with Article VIII						Met							
Non-imposition or intensification of import restrictions for balance of payments reasons						Met							
Memorandum items:							(Millions of Cabo Verde escudos)						
Social spending	5,550	5,248	8,685		8,149		14,198	3,252	3,024	6,076	11,521	10,714	15,122
Net onlending	1,877	-130	3,647		-288		2,126	672	672	1,832	2,638	2,638	3,395
Capitalization	1,698	2,806	2,698		1,944		4,078	200	350	869	973	973	1,448
Program assumptions													
Project and budget support grants	1,326	622	2,401		1,225		5,127	444	579	1,284	1,783	2,265	5,959
External debt service	3,765	3,473	5,648		5,607		5,980	1,874	1,667	3,389	5,623	5,537	6,874
Sales of assets	2	50	2		82		100	0	0	0	0	0	1,224
Project and budget support loans	2,591	2,393	7,231		6,828		10,810	451	3,151	4,601	6,553	7,198	10,035

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

[1] Foreign currency amounts will be converted at current exchange rates.

[2] The ceiling or floor will be adjusted as specified in the TMU.

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

[4] Continuous.

Table 2. Cabo Verde: Reform Targets for 2019–20 Under the PCI

Actions	Target Date	Objective	Status
Fiscal reforms			
• Complete a review report on exemptions identifying their potential impact and streamlining actions.	End-December 2019.	• Improve tax collection.	• Met
• Streamline exemptions for: (i) the VAT; (ii) import duties, and (iii) excises.	End-June 2020.	• Improve tax collection.	• In progress
• Submit to Parliament the budget for 2020 that is in line with commitments under the PCI.	End-October 2019.	• Support fiscal and debt sustainability.	• Met
• Prepare a Strategy Note on the assets and liabilities and management of the Sovereign Private Investment Guarantee Fund (SPIGF).	End-April 2020	• Provide a conceptual framework for the SPIGF.	• New
SOEs reforms			
• Implement quarterly monitoring of actual performance of 6 key SOEs against their approved budgets, starting at end-December 2019.	Continuous.	• Improve fiscal reporting and reduce fiscal risk.	• Met.
• Compile financial information on cash flow performance of the 6 largest SOEs for FY2019.	End-July 2019.	• Improve fiscal reporting and reduce fiscal risk.	• Met
Monetary reforms			
• Release the minutes of the Monetary Policy Committee meetings at least one month after each meeting, starting at end-July 2019.	Continuous.	• Improve the communication of monetary policy.	• Met
• Reduce the excessively wide overnight interest rate corridor to a maximum of 150-200 basis points.	End-December 2019; implemented in June 2019.	• Improve monetary policy transmission mechanism.	• Met
Financial sector reforms			
• Create a functional central registry of mobile collateral.	End- December 2020.	• Improve access to finance.	• In progress
• Revamp the public credit registry information system by completing the procurement of the relevant software system.	End-December 2020.	• Improve access to finance.	• In progress

Table 3. Cabo Verde: Summary of Projected External Borrowing Program for Public and Publicly Guaranteed Debt, 2020[1]

(In Million USD, unless otherwise indicated)

	New Debt		Present Value of New Debt	
	USD million	Percent	USD million	Percent
By Sources of Debt Financing	**126.2**	**100.0**	**59.5**	**100.0**
Concessional Debt	119.6	94.8	54.1	90.9
Multilateral debt	73.3	58.1	37.1	62.4
Bilateral debt	46.3	36.7	17.0	28.5
Non-concessional Debt	6.6	5.2	5.4	9.1
Semi-concessional [2]	6.6	5.2	5.4	9.1
Commercial terms	0.0	0.0	0.0	0.0
By Creditor Type	**126.2**	**100.0**	**59.5**	**100.0**
Multilateral	73.3	58.1	37.1	62.4
Bilateral - Paris Club	41.9	33.2	14.3	24.1
Bilateral - Non-Paris Club	10.9	8.7	8.1	13.6
Uses of Debt Financing	**126.2**	**100.0**	**59.5**	**100.0**
Infrastructure	58.5	46.4	24.0	40.3
Social Spending	2.3	1.8	0.9	1.6
Budget Financing	31.7	25.1	16.2	27.1
Other	33.7	26.7	18.5	31.0

Sources: Cabo Verdean Authorities; and IMF Staff projections.

[1] On disbursement basis.

[2] These loans were contracted prior to the PCI.

Attachment II. Technical Memorandum of Understanding

1. This memorandum sets out the understandings between the Cabo Verdean authorities and the IMF staff regarding the definitions of variables included in the quantitative targets and continuous targets set out in the Program Statements (PS), the key assumptions, and the reporting requirement of the Government and the Central Bank of Cabo Verde for the 18 months Policy Coordination Instrument (PCI).

QUANTITATIVE AND CONTINUOUS TARGETS

A. Floor on the Primary Balance of the Central Government

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

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

- Revenues are recorded when the funds are transferred to a government revenue account. Tax revenues are recorded as net of tax refunds.
- Central government primary expenditure is recorded on a cash basis covers recurrent expenditures and capital expenditure.

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

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

B. Cumulative Floor on Central Government Tax Revenue

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

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

C. Ceiling on Net Other Liabilities

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

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

D. Non-accumulation of Domestic Payments Arrears

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

G. Net International Reserves of the Central Bank

18. The floor on the stock of net international reserves (NIR) of the BCV constitutes a quantitative target under the program. The NIR of the BCV are defined as gross international reserves of the BCV net of its short-term external reserve liabilities, calculated at the current exchange rates. Gross reserves of the BCV are those that are readily available (i.e., liquid and marketable and free of any pledges or encumbrances), controlled by the BCV and held for the purposes of meeting balance of payments needs and intervening in foreign exchange markets. They include gold, holdings of SDRs, the reserve position at the IMF, holdings of foreign exchange and traveler's checks, demand and short-term deposits at foreign banks abroad, fixed-term deposits abroad that can be liquidated without penalty, and any holdings of investment-grade securities. Short term external liabilities of the BCV comprise liabilities to nonresidents contracted by the BCV with an original maturity of less than a year, any net off-balance-sheet position of the BCV (futures, forwards, swaps, or options) with either residents and nonresidents, any arrears on principal and interest to external creditors and suppliers, and purchases from the IMF. The program floors for the NIR will be adjusted downward by:

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

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

H. Non-accumulation of External Payments Arrears

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

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

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

I. Memorandum Item: Floor on Central Government Social Spending

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

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

OTHER DATA REQUIREMENTS

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

26. The Statement of Other Economic Flows as defined in the IMF Manual GFSM2001 or GFSM2014 relative to holding gains/losses of the previous year with ASA, Electra, EMPROFAC, ENAPOR, and IFH will be transmitted on an annual basis within three months after the end of the following year (15 months after the closing date).

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