



AFRICAN DEVELOPMENT BANK GROUP  
GROUPE DE LA BANQUE AFRICAINE  
DE DÉVELOPPEMENT

# COUNTRY FOCUS REPORT

## CABO VERDE

**Driving Cabo Verde's Transformation**  
The Reform of the Global Financial Architecture







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The Reform of the Global Financial Architecture



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# ACKNOWLEDGEMENT

The 2024 Country Focus Report for Cabo Verde was prepared in the Chief Economist and Vice-Presidency for Economic Governance and Knowledge Management Complex, under the direction and supervision of Professor Kevin C. Urama, Chief Economist and Vice-President, with support from Amadou Boly, and Amah Marie-Aude Ezanin Koffi.

The preparation of this report was led by Désiré Vencatachellum, Senior Director, Country Economics Department, with Marcellin Ndong Ntah as the project management Lead, IT support from Abir Bdioui, and administrative support from Tricia Effe Baidoo. The Country Focus Report for Cabo Verde was prepared by Joel Daniel Muzima (Principal Country Economist, ECCE1), under the guidance of Guy Blaise Nkamleu (Lead Economist, ECCE1/RDGW) and Jacob Oduor (Lead Economist, ECCE2, RDGN).

The team thanks (i) Cabo Verde Country Team led by Lamin Barrow (Director General, West Africa Region), Joseph Martial Ribeiro, Deputy Director General, West Africa Region; and Mohamed Cherif (Country Manager, Senegal Country Office); (ii) the Macroeconomics Policy, Forecasting and Research led by Abdoulaye Coulibaly, Director, Officer-in-Charge; (iii) the Transition States Department (RDTs) led by Yero Baldeh, Director, (iv) the African Natural Resource Center (ECNR) led by Désiré Vencatachellum, Director, Officer-in-Charge; and (v) the Macroeconomics Policy and Debt Sustainability Division led by Anthony Simpasa, Division Manager, for their contributions.

The data in the report was compiled by the Department of Statistics led by Babatunde Samson Omotosho, Director, with significant contributions from Louis Kouakou (Manager of Socio-Economic Statistics Division, Department of Statistics), Ben Paul Mungyereza (Head of the Statistical Capacity Building Division, Statistics Department), Anouar Chaouch (Senior Statistician, Division 1 of the Statistics Department) and Momar Kouta (Senior Statistical Information Systems Officer, Division 1 of the Statistics Department).

Peer-review comments were received from Franklin Ngwu (Consultant, ECVP0), and Rajae El Alami (Consultant, RDTs). Country Team comments were received from Stéphane Regis Hauhouot (Statistical Assistant, ECST1), and Harcel Nana Tomen (Operations Analyst, RDGW4). Dr Joseph Atta-Mensah, Senior Fellow from Africa Centre for Economic Transformation, acted as an external reviewer.

The cover of the report is based on a general design by Laetitia Yattien-Amiguet and Justin Kabasele of the Bank's External Relations and Communications. Copy-editing was done by the Bank's Language Services Department (TCLS) and layout was done by Lagence Creativ.



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# ABBREVIATIONS

<b>AEO</b>	African Economic Outlook
<b>AfCFTA</b>	Africa Continental Free Trade Area
<b>AfDB</b>	African Development Bank
<b>AGBI</b>	African Green Banks Initiative
<b>BCV</b>	Bank of Cabo Verde
<b>BVC</b>	Cabo Verde Stock Exchange
<b>CF</b>	Common Framework
<b>CFR</b>	Country Focus Report
<b>CPI</b>	Corruption Perception Index
<b>CVE</b>	Cabo Verde Escudo
<b>DFI</b>	Development Financial Institutions
<b>DRM</b>	Domestic Resource Mobilisation
<b>ECF</b>	Extended Credit Facility
<b>ECMR</b>	Macro-economic Policy, Forecasting and Research
<b>ECOWAS</b>	Economic Community of West African States
<b>ENEPE</b>	National Strategy for Eradication of Extreme Poverty
<b>ETD</b>	Economic Transformation Database
<b>EUR</b>	Euro
<b>FDI</b>	Foreign Direct Investment
<b>FiTI</b>	Fisheries Transparency Initiative
<b>GDP</b>	Gross Domestic Product
<b>GFA</b>	Global Financial Architecture
<b>GII</b>	Global Innovation Index
<b>GNI</b>	Gross National Income
<b>ICT</b>	Information and Communication Technology
<b>IFIs</b>	International financial institutions
<b>ILO</b>	International Labour Organization
<b>IMF</b>	International Monetary Fund
<b>INE</b>	National Institute of Statistics
<b>M&amp;E</b>	Monitoring and Evaluation
<b>MDB</b>	Multilateral Development Banks
<b>MFIDS</b>	Ministry of Family, Inclusion and Social Development
<b>MSME</b>	Micro, Small and Medium Enterprises
<b>MW</b>	Mega Watts

<b>NbS</b>	Nature-based Solutions
<b>NPLs</b>	Non-performing Loans
<b>ODA</b>	Official Development Assistance
<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>PEDS</b>	Strategic Plan for Sustainable Development
<b>PFM</b>	Public Finance Management
<b>PNIEB</b>	Strategic Plan for Blue Economy and Investment Plan
<b>PPP</b>	Public Private Partnerships
<b>REO</b>	Regional Economic Outlook
<b>SCDI</b>	State-Contingent Debt Instruments
<b>SDGs</b>	Sustainable Development Goals
<b>SDR</b>	Special Drawing Rights
<b>SIDS</b>	Small Island Developing States
<b>SME</b>	Small and Medium Enterprises
<b>SOEs</b>	State-Owned Enterprises
<b>TVET</b>	Technical Vocational and Educational Training
<b>UN</b>	United Nations
<b>UNCTAD</b>	United Nations Trade and Development
<b>UNDP</b>	United Nations Development Programme
<b>USD</b>	United States dollar
<b>VAT</b>	Value-added tax
<b>WFP</b>	World Food Programme



# EXECUTIVE SUMMARY

**T**he Cabo Verdean economy remains vulnerable to exogenous shocks owing to its dependence on tourism-intensive activities. After a strong rebound of 17.4% in Gross Domestic Product (GDP) growth in 2022, the economy could not sustain its strong growth pace in 2023 and real GDP growth has moderated to 5.3%. The growth slowdown was impacted by climate change effects in agriculture and fisheries and by high borrowing costs owing to tighter financing conditions. Multiple exogenous shocks led to double-digit increases in energy and food prices and a 60% increase in transport prices in 2022, with the rising cost of living having a particularly negative impact on vulnerable households. Inflation has since declined from 7.9% in 2022 to 4% in 2023 with the tightening of monetary policy. The fiscal deficit narrowed from 4.6% of GDP in 2022 to 4.4% of GDP in 2023 owing to strong revenue collection. Public debt-to-GDP ratio declined from 127.1% in 2022 to 119.9% in 2023 thanks to strong nominal GDP growth. However, the fiscal space remains limited, and the primary balance deficit is insufficient to cover debt service payments. Macro-economic projections are favourable, with real GDP growth expected to average 5.2% in 2024 and 5.4% in 2025. This is premised on macro-economic stability and the forthcoming investments (for example, USD 140 million – 6% of GDP) in agricultural value chains, renewable energy (to reach 30% of total energy supply by 2025, up from 22% in 2022) and digital platform and innovation programmes.

**Cabo Verde's journey towards structural transformation demands significant changes in the growth model.** Reforms should focus on economic diversification, improving the business environment, poverty reduction and climate change risk mitigation. The agricultural labour force is 77% less productive than economy-wide productivity as low technological innovation, lack of arable land (only 10% of total land area), freshwater resources and climate change affect yields. Within services, labour productivity growth (54% over 1992–2000) has driven economic growth but on a declining trajectory and without structural transformation. This implies that the country's growth model, heavily dependent on tourism and Foreign Direct Investment (FDI) is failing to create spillover effects across the economy. The financing needs and gap to reinvigorate structural transformation is estimated at USD 163 million and USD 103 million per annum respectively until 2030.

**Reforms of the global financial architecture (GFA) are expected to promote external flows to finance Africa's (and, by inclusion, Cabo Verde's) economic transformation.** Developing countries, and small island states in particular, struggle to access low-cost financing because of weak creditworthiness. Therefore, there is now a growing consensus about the need to reform the GFA. Cabo Verde could benefit from these reforms in multiple ways, including through (i) increased access to low-cost financing from Multilateral Development Banks (MDBs) and Development Financial Institutions (DFIs); (ii) greater access to de-risking instruments for private sector investments; (iii) greater access to climate finance (green bonds, blue bonds and sustainable bonds); (iv) monetisation of its natural capital wealth (for example, fisheries and biodiversity); (v) access to concessional financing from MDBs, DFIs and bilateral donors for financing of projects related to the preservation of global public goods (for example, eco-tourism, climate adaptation and mitigation and prevention of pandemics); (vi) improved public finance management (PFM) reforms and capacity-building in debt management and domestic resource mobilisation; and (vii) tapping into diaspora remittances. Cabo Verde can build greater resilience to external shocks, foster sustainable economic growth and ensure long-term development benefits for its population by strengthening its financial resilience; increasing investments in technology and innovation to enhance climate-resilient agricultural productivity; and scaling up renewable energy.

# INTRODUCTION

Cabo Verde, an archipelagic small island state, consists of 10 islands, nine of which are inhabited. It is located 500 km off the West Coast of Africa, with an estimated population of 598,000 people. Since the 1990s, Cabo Verde has experienced strong economic growth founded on macro-economic stability, commitment to reforms for improving the business environment and public sector efficiency, and openness to the global economy. The growth-enhancing reforms led to a massive inflow of FDI, with about 75% channelled to the vibrant tourism sector. Official Development Assistance (ODA) and remittances complemented the international inflows. However, as from 2001, the rate of economic growth started to decelerate. The high dependency of the growth model on tourism exports and FDI inflows, coupled with high vulnerability to climate change, has exposed the country to several external shocks. More specifically, the five-year prolonged drought that started in 2007, the global financial crisis of 2008, the Zika virus disease outbreak in 2014, the volcanic eruption on Fogo island in 2014, the COVID-19 crisis and, more recently, the multiple exogenous shocks, which have exacerbated the economic vulnerabilities.

Furthermore, analysis of the decomposition of labour productivity tends to attest to the weaknesses of the country's growth model in supporting structural transformation. For instance, agricultural labour productivity in the country is about 77% lower than economy-wide productivity. Labour productivity growth has occurred mostly within sectors, with services, particularly tourism accounting for the largest share (about 54% over 1992–2000). Lack of capacity to enhance synergies and shared benefits of the tourism sector with the rest of the economy threatens past gains. Extreme poverty still affects 11.1% of households; income inequality measured by the Gini coefficient remains significant (last estimated at 42.4% in 2015); youth unemployment is at 27.8%; and lack of job opportunities contributes to high levels of informality (about 53% of the working population). These issues highlight significant fragility risks for Cabo Verde. The heavy reliance on a single sector like tourism makes the economy vulnerable to external shocks such as global economic downturns or pandemics. Additionally, high youth unemployment and income inequality can fuel social unrest and instability, undermining the country's development prospects. The large informal sector also tends to exacerbate the vulnerability of a significant portion of the population.

Prior to its graduation from a low-income to lower-middle-income country in 2007, Cabo Verde succeeded in using concessional loans and grants efficiently to finance transformative infrastructure, notably roads, ports, airports, water and sanitation, health units and schools. However, public debt, which had been low at 57.2% in 2008, has since increased to 127.2% in 2022, highlighting the challenges of economic growth in generating sufficient returns to reduce the indebtedness. The increased frequency and intensity of extreme weather events also poses challenges to Cabo Verde, given the limited fiscal space for financing climate actions. Therefore, a structured reform of the international financial architecture that could allow the country to access long-term financing at highly concessional terms is imperative to enhance debt sustainability.

The purpose of the report is to analyse the process of structural transformation of Cabo Verde and to examine how it could be better financed by reforming the international financial architecture. The rest of the report is structured as follows. Chapter 1 presents an analysis of the recent macro-economic situation and prospects. Chapter 2 examines the process of structural transformation of Cabo Verde. Chapter 3 concludes by presenting the need to reform the international financial architecture to better finance structural transformation in Cabo Verde.





# MACRO-ECONOMIC PERFORMANCE AND OUTLOOK

## 1.1 Key Messages

- **Economic growth, though moderate, has proved resilient to exogenous shocks.** Real GDP rebounded by 17.4% of GDP growth in 2022, before moderating to 5.1% in 2023 as exports, notably from tourism services, normalised, and amid the effects on food and energy prices of the multiple exogenous shocks.
- **Inflationary pressures have started to ease owing to the tightening of monetary policy.** The Bank of Cabo Verde (BCV)'s restrictive monetary policy has gradually helped bring inflation down to 4% in 2023, compared to 7.9% in 2022.
- **Fiscal balances are improving, thanks to increased mobilisation of domestic revenue.** In 2023, the overall fiscal deficit was in line with the programmed target estimated at 4.4% of GDP, as compared to 4.6% in 2022. The fiscal deficit was financed by external disbursements (70%) and domestic loans (30%).
- **Cabo Verde's external position remains vulnerable to exogenous shocks.** This is mostly due to high levels of external debt exacerbated by high interest rates on domestic debt, limited market competitiveness and global commodity price fluctuations, as 80% of goods consumed in the country are imported. A global economic slowdown is likely to weaken tourism demand, notably from Europe (Cabo Verde's largest trade partner).
- **The macro-economic outlook is favourable with real GDP growth projected at 5.2% in 2024 and 5.4% in 2025,** boosted by energy, the digital economy and private consumption. However, main downside risks to the economic outlook include (i) an eventual disruption in global food and energy supply chains; (ii) an economic slowdown in Europe; (iii) slow pace of State-Owned Enterprises (SOEs); and (iv) climate change, all of which could undermine growth. Nonetheless, major tailwinds to growth would include: (i) macro-economic stability; (ii) strong investments in agricultural value chains, digital economy and renewable energy and (iii) vibrant tourism.
- **To build resilience, Cabo Verde should diversify its economic base to reduce dependence on tourism and external markets.** Enhancing the agricultural sector through sustainable practices and technological innovation can improve food security and economic stability. Investing in renewable energy will reduce vulnerability to global energy price fluctuations. Expanding the digital economy can create new job opportunities, especially for young people, and drive inclusive growth.



## 1.2. Introduction

This chapter presents an updated analysis of the country's economic performance for 2023, including medium-term growth projections over the period 2024–2025. It also assesses trends in, among other things, key macro-economic indicators, fiscal and monetary policies and changes in domestic and international financial flows, investment and public debt. The chapter also discusses main downside and upside risks to the outlook and provides policy options to foster high and resilient growth; supporting macro-economic stability and economic transformation; and deal with shocks that have continued to buffet the country's economy.

## 1.3. Growth performance

After a strong rebound of 17.4% of GDP growth in 2022, the economy could not sustain its strong growth pace in 2023 and real GDP growth has moderated to 5.3%. Climate change affected agriculture and fisheries production, and tighter financing conditions increased borrowing costs affecting the feasibility of new projects, including in the construction and energy sectors. On the supply side, growth was supported by agriculture, energy, digital economy and tourism. On the

demand side, private consumption bolstered growth. Real GDP per capita increased by 4.2% in 2023, although at a slower pace compared to the 16.5% real per capita income growth in 2022. This was mostly driven by the moderate economic activity in 2023 with a low population growth rate (0.9%).<sup>1</sup> The economy remains highly dependent on services (69.2% of GDP) – with tourism directly accounting for 25.0% of GDP, 23.0% of formal jobs and 55.0% of export revenues – industry (21.8%) and agriculture (7.8%).

## 1.4. Other recent macro-economic and social developments

**Monetary policy and inflation:** The BCV remained committed to maintaining headline inflation in line with the euro area and anchored on the exchange rate peg. Inflation increased from 1.9% in 2021 to 7.9% in 2022, mostly driven by supply-side factors, notably high food and energy prices induced by the multiple exogenous shocks. The BCV raised its monetary policy rate, first from 0.25% to 1% in early May 2023 and then to 1.25% in November 2023. As a result, inflationary pressures eased, and inflation decelerated to 4.0% in 2023. The exchange rate of the Cabo Verde escudo (CVE) to the US dollar (USD) declined from CVE 105.2/USD 1 in 2022 to CVE 102.1/USD

**Table 1: Cabo Verde's macro-economic indicators**

	2019	2020	2021	2022	2023(e)	2024(p)	2025(p)
Real GDP growth (%)	6.9	-20.8	7.0	17.4	5.1	5.2	5.4
Real GDP growth per capita (%)	5.9	-21.8	6.1	16.5	4.2	4.2	4.5
Inflation (%)	1.1	0.6	1.9	7.9	4.0	2.2	2.0
Overall fiscal balance, including grants (% GDP)	-1.6	-9.0	-7.4	-4.6	-4.4	-3.0	-2.1
Primary balance (% of GDP)	1.0	-4.2	-2.9	-0.8	-0.9	-1.7	-1.3
Current account (% GDP)	-4.6	-15.0	-12.7	-5.8	-6.1	-7.0	-6.8
Total population (millions)	0.6	0.6	0.6	0.6	0.6	...	...
Life expectancy at birth (years)	76.0	74.8	74.1	74.7	76.9	...	...

Sources: Data from domestic authorities; estimates (e) and predictions (p) based on authors' calculations. AfDB Statistics Department, April 2024. (...) not available.

<sup>1</sup> National Institute of Statistics (INE, 2021). National Population Census.

### Box 1: Impact of tighter international financial conditions in Cabo Verde

The tightening of global monetary policy in response to rising inflation prompted the Central Bank of Cabo Verde to follow suit. Inflation has started to ease, from 7.6% in April 2023 to 1.7% in April 2024. Credit to the economy was resilient, growing by 7.1% in 2023, as compared to 6.2% in 2022. However, the speed and magnitude of interest rate rises have started to significantly impact bank performance. NPLs increased from 7.8% in 2022 to 8.7% of total loans in 2023 as customers in the real estate and construction sectors are struggling to service their loans. Signs of financial pressure have become more evident, particularly on vulnerable households. The private savings rate declined from 33.9% of GDP in 2022 to 21.2% of GDP in 2023, as high inflation eroded real disposable incomes amid rising interest rates. Higher interest rates have led to a decline in private investment from 36.4% of GDP in 2022 to 24.1% of GDP in 2023 as firms, particularly in infrastructure sectors (e.g., energy and transport), are facing higher operation costs and rising debt-servicing costs. The profits of small and medium-sized enterprises (SMEs) remained below their pre-COVID-19 levels, thereby constraining their capacity for new borrowing in a context of rising interest rates. Cabo Verde's total interest payments increased by 9.3% in 2023, as compared to 2022. Public debt is sensitive to interest rate hikes, as 11.9% of total debt is negotiated on variable interest rates. The BCV's decision to tighten monetary policy helped narrow the interest rate differential. This prompted an inflow of emigrant deposits by 9.3% to reach EUR 685 million, equivalent to 32.4% of total deposits in the financial sector. While the effects of tightening monetary policy on inflation are starting to bear fruit, judging from the declining inflation, its implications for economic growth are still to be ascertained.

1 in 2023, representing an appreciation of 2.9% supported by adequate foreign exchange reserves.

17.0% of revenues and 12.0% of exports, below the respective thresholds of 23% and 21%.

**Fiscal balance and debt dynamics:** The fiscal deficit was in line with the programmed target estimated at 4.4% of GDP, as compared to 4.6% in 2022. The fiscal deficit was financed by external disbursements of loans (70%) and domestic loans (30%). Streamlining of arrears in collection of the value-added Tax (VAT) and the use of electronic invoicing boosted tax revenues from 18.1% of GDP in 2022 to 18.9% in 2023. This ultimately contributed to the improvement of the fiscal position. The primary balance deficit, although improving, remains insufficient to meet interest payments.<sup>2</sup> Cabo Verde's risk on external debt is "moderate" but overall public debt remains at "high" risk of debt distress. The ratio of government debt-to-GDP reduced from 127.7% of GDP in 2022 to 119.9% of GDP in 2023 as a result of higher nominal GDP growth and fiscal overperformance. In 2023, debt service stood at

**Current account balance:** Cabo Verde's current account deficit deteriorated from 5.8% of GDP in 2022 to 6.1% of GDP in 2023, driven by high import bills and lower exports. Merchandise exports, which constitute 11.9% of GDP and consisting of processed fish, clothing and footwear parts, and scrap iron, have dropped by 3% in 2023, reflecting low productivity and weak external demand. The current account deficit is largely financed by FDI (5.5% of GDP), remittances (14.1% of GDP), and ODA (4% of GDP). Cabo Verde is vulnerable to global commodity price fluctuations as 80% of the goods consumed in the country are imported. International reserves increased from EUR 626 million in 2022 (6.3 months of imports cover) to EUR 728 million in 2023 (6.7 months of imports cover), boosted by the disbursement of USD 21.2 million under the International Monetary Fund (IMF)'s Extended Credit Facility programme.

<sup>2</sup> Estimates using IMF (2024) staff report data show that total interest payments increased from EUR 48.7 million in 2022 to EUR 53.3 million in 2023, corresponding to 9.3% nominal annual growth.

**Financial sector:** Despite the adverse external environment, Cabo Verde's financial sector has shown signs of resilience. Total assets increased by 9.3% to reach USD 2.9 billion (137.1% of GDP) in 2022<sup>3</sup>. An estimated 44%<sup>4</sup> of micro, small and medium-sized enterprises (MSME) report access to finance as a major bottleneck for private sector growth. Meanwhile, the financial sector remains sound, with a capital adequacy ratio of 21.4%, well above the 12% minimum regulatory requirement. Non-performing loans (NPLs) as a percentage of gross loans increased from 7.8% in 2022 to 8.7% by end-2023. The increase in the NPL ratio in 2023 is linked to the unwinding of COVID-19 credit moratoriums and exacerbated by rising interest rates (see Box 1).

**Social developments:** Cabo Verde performs relatively well on major socio-economic indicators, but poverty and unemployment remain challenges, particularly in the rural areas. Cabo Verde's life expectancy, at 76.9 years in 2023, is the second highest in Africa after Mauritius. Poverty incidence, measured by the national poverty line of USD 2.77/person/day, increased from 26% in 2019 to 31.1% in 2022, exacerbated by COVID-19. Extreme poverty affects 11.1%<sup>5</sup> of households and 85% are female-headed, working in informal sector (63.6%). An estimated 9% of the population was experiencing food insecurity<sup>6</sup> in 2022. Income inequality in Cabo Verde, as measured by the Gini<sup>7</sup> coefficient, was last estimated at 42.4% in 2015, slightly below sub-Saharan Africa's average of 44.2%. Unemployment increased from 11.3% in 2019 to 12.1% in 2023, reflecting COVID-19-related job losses. Youth unemployment rates are at 27.8%, with 33.4% for young women and 22.9% for young men. Approximately 53% of the employed population works in the informal sector. <sup>8</sup>Cabo

Verde ranks 1st out of 52 African countries and 89th out of 166 countries in the world in the Sustainable Development Goals (SDGs) Index 2023, based on overall performance in all 17 SDGs.

## 1.5. Macro-economic outlook and risks

**Economic growth:** Macro-economic prospects are favourable, with growth expected to average 5.2% in 2024 and 5.4% in 2025, premised on macro-economic stability, and the forthcoming investments in agricultural value chains, renewable energy expansion, and the implementation of the Cabo Verde digital platform and innovation programme. **Inflation** is projected to average 2.1% over 2024–2025 on the back of weaker demand and declining food and energy prices. **The fiscal deficit** is expected to narrow to 3.0% of GDP in 2024 and 2.1% in 2025, owing to fiscal consolidation measures, higher tax revenues and privatisation of SOEs. **The current account deficit** is projected to narrow to 5.2% of GDP in 2024 and 4.4% in 2025, supported by tourism receipts and remittances. **Risks to the growth outlook** include an economic slowdown in Europe, disruptions in global food and energy supply chains, limited progress in state enterprise reform and impacts of climate change. Actions to reduce fiscal risks from state enterprises and address infrastructure gaps are fundamental for sustainable growth.

## 1.6 Policy options to foster high and resilient growth: supporting macro-economic stability and economic transformation

Despite rebounding strongly from the COVID-19 pandemic, Cabo Verde's economy is experiencing

3 Banco de Cabo Verde (2022). Financial stability report.

4 World Bank (2023). "Cabo Verde: Accelerating Growth and Fostering Resilience. Country Economic Memorandum." World Bank, Washington, D.C.

5 MFIDS (2022) National Strategy for the Eradication of Extreme Poverty – ENEPE (2022–2026).

6 WFP (World Food Programme). 2023. "Limited Emergency Operation (LEO) Cabo Verde (June 2022–November 2023)." Operation Database. <https://www.wfp.org/operations/cv01-limited-emergency-operation-leo-cabo-verde-june-2022-november-2023>

7 World Bank (2024). <https://data.worldbank.org/indicator/SI.POV.GINI?locations=ZF>.

8 INE (2022) – Inquérito Multiobjectivo Continuo – Emprego. 2022. National Institute of Statistics of Cabo Verde.

As Cabo Verde's economic growth is moderating, addressing long-standing structural constraints such as inter-island transportation gaps, debt vulnerabilities, dependency on food imports, and skills mismatches is crucial to enhancing synergies and shared benefits of tourism with the rest of the economy and achieving sustainable long-term growth.

moderate growth, and the fiscal space has been reduced. Achieving macro-economic stability and economic transformation requires adoption of a mix of short-term and long-term policies to enhance a paradigm shift in the current development model toward economic diversification.

#### ***In the short term***

- **To achieve faster disinflation and anchor inflation expectations at a lower cost to the economy, tailored monetary policy adjustments are needed.** As core inflation remains elevated, the Central Bank should keep policy rates high enough to ensure that inflation expectations remain firmly anchored.
- **Addressing exchange rate pressures should be a key short-term priority.** The appreciation of the domestic currency has continued owing to strong external buffers. As Cabo Verde adopts an exchange rate peg to the euro, the Central Bank should ensure an accumulation of an adequate level of reserves to preserve the peg and avoid price distortions in the economy.
- **Investments in agricultural transformation and agrobusiness are critical for boosting local food production and diversifying import sources to address rising food prices.** Supporting Cabo Verdean smallholder farmers can trigger an agricultural revolution to feed Cabo Verde, especially in urban areas. This requires provision of affordable finance, improved food production technologies (for example, certified drought-resistant seeds), and mechanisation services.
- **Reduce the debt burden through governance reforms to strengthen debt management capacity.** This implies adherence to expenditure reallocations, improved revenue collection (for example, e-invoicing) to offset falling ODA, and enhancing efficiency of non-performing SOEs, and an extension of domestic debt maturities

to reduce gross financing needs and medium-term vulnerabilities.

#### ***Medium to long-term policies***

- **Scaling up domestic resource mobilisation is imperative to accelerate Cabo Verde's structural transformation.** Measures aimed at improving corporate income tax and VAT collection, revenue linked to strategic infrastructure (for example, airport and ports concessions), and diaspora remittances will be determinant in narrowing the fiscal deficit.
- **It is crucial to create a more conducive environment for private sector investment in infrastructure to accelerate Cabo Verde's economic transformation.** Increasing the level of participation of the private sector in the economy is crucially important in the delivery of infrastructure. The process of privatisation of non-performing SOEs and infrastructure concessions (for example, ports and airports) can be the first steps to attracting private sector investment and skills, but it will be important to improve the capacity of the public sector to structure and negotiate them with the private sector. The Bank could provide technical assistance and advisory services to build capacity across government, including through the African Legal Support Facility.
- **Accelerating structural transformation efforts and financing their implementation will be key to unlocking Cabo Verde's development potential.** While well-designed structural reforms are important to boost the level and sustainability of economic growth, their implementation depends partly on scaling up financing for structural transformation and enhancing spending efficiency. Boosting domestic resource mobilisation plays a critical role in that regard as Cabo Verde's government bears primary responsibility for financing its development.



- **Cabo Verde is vulnerable to climate change, ranking 130 of 180 countries on the 2021 Global Climate Risk Index.**

The prolonged drought that started in 2017 led to a loss of 93% of cereal production and 34% of tuber production in 2021. The incidence of drought and extreme rainfall

events also affect marine and coastal assets through sea-level rise, ocean warming and acidification.<sup>9</sup> Hence, strengthening capacity for mainstreaming all technical and macro-economic aspects of climate change and the global decarbonisation agenda are critical to enhance climate resilience.

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<sup>9</sup> See the report: African Development Bank (2023): Country Focus Report 2023 Cabo Verde – Mobilizing Private Sector Financing for Climate and Green Growth.

# TAKING STOCK OF THE COUNTRY'S STRUCTURAL TRANSFORMATION PROGRESS

## 2

### 2.1. Key Messages

- **Cabo Verde has exhibited remarkable resilience against multiple shocks, but its structural transformation has been slow and uneven.** The Cabo Verdean economy grew by an average of 2.5% throughout 1980–2022, well below lower middle-income countries (4.1%) and Africa (3.0%). Growth was mostly driven by labour productivity with the services sector – notably tourism – accounting for 54% of total labour productivity growth over 1991–2000 – amid limited structural transformation.
- **Cabo Verde's economy has been transforming without a marked level of industrialization, but through a low skills-intensive services sector, notably tourism, with limited economic diversification.** During the 1980–2010 period, economic liberalisation policies, macro-economic stability and good governance helped attract large inflows of FDI into the tourism sector, the main driver of growth. However, there has been limited economic transformation with excess labour being absorbed by high-productivity industry and low skills-intensive services sectors, without significant gains in productivity in agriculture or more industrialisation.
- **Cabo Verde has several key opportunities for building resilience that can be leveraged to foster sustainable development.** The young and growing working-age population presents a significant opportunity to harness the demographic dividend. By investing in Information and Communications Technology (ICT) infrastructure and technical and vocational educational training (TVET), Cabo Verde can equip its youth with the necessary skills to meet private sector demands, thereby boosting productivity and economic growth. As financing needs to accelerate structural transformation are huge (estimated by AfDB at USD 163 million annually by 2030), the country should explore innovative financing instruments with the support of the private sector MDBs and DFIs.
- **The country's commitment to political stability, strong democratic institutions and recent improvements in transparency and anti-corruption measures create a conducive environment for implementing effective reforms and attracting investments.** Furthermore, Cabo Verde's strategic investments in renewable energy and climate-resilient infrastructure can mitigate the adverse impacts of climate change while promoting sustainable development. Addressing the challenges of the informal sector by formalising employment and integrating social safety nets can enhance economic stability and inclusivity. Investments in the blue economy and climate-resilient infrastructure (ports and airports) can position the country to benefit from the free movement of people and goods as part of the Africa Continental Free Trade Area (AfCFTA) agreement.

## 2.2. Introduction

This chapter presents a comprehensive overview of recent progress in Cabo Verde's economic transformation in a changing world, identifies its key trends and outlines its characteristics. It also estimates the financing needs to fast-track structural transformation. It takes both a historical perspective and a forward-looking approach on structural transformation, comparing Cabo Verde's performance with that of Africa and other peer countries and drawing lessons for the future. The impact of a wide array of socio-economic, financial, governance, and external factors on Cabo Verde's structural transformation (or lack thereof), as well as the financing needs and financing gaps, is estimated with the objective of highlighting the main pull and push factors and guiding both evidence-informed policymaking and investment opportunities.

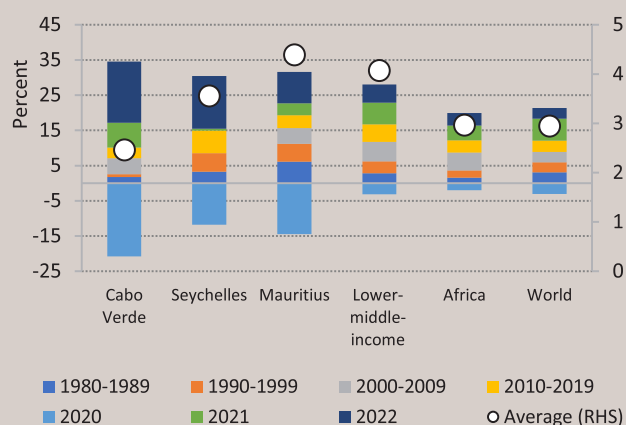
## 2.3. Taking stock of economic performance and transformation in Cabo Verde

Prior to the adoption of the exchange rate peg in 1998, Cabo Verde's economic growth was marked by a period of weak performance, averaging 1.8% during 1980–1989 – a period that coincided with a centrally planned economy. Growth decelerated further to 0.8% during 1990–1999, severely impacted by the

1998 financial crisis, as the economy relied heavily on remittances, ODA and FDI, notably in the tourism sector. The adoption of economic liberalisation policies following the exchange rate peg to the euro, underpinned by strong institutions and political stability, stimulated trade and FDI and propelled Cabo Verde's real GDP growth to an average of 4.6% during 2000–2009 and 3% over 2010–2019 (Figure 2.1). However, the COVID-19 pandemic highlighted the vulnerabilities of Cabo Verde's economic growth model with the collapse of real GDP growth by 20.8% in 2020 – the largest contraction since independence in 1975. The economy has rebounded strongly to 7% in 2021 and 17.4% in 2022, as the authorities succeeded in adopting a COVID-19 mitigation plan and maintained macro-financial stability with the support of international partners.

In per-capita terms, by contrast, Cabo Verde's growth performance has been remarkable. (Figure 2.2). Cabo Verde's average real GDP per capita growth sustained a strong momentum over the 2000–2009 and 2010–2019 decades. This enabled the country to become the only non-extractive economy in sub-Saharan Africa to transition to lower-middle-income status in 2007, in such a relatively short time (World Bank, 2018). At the peak of the COVID-19 pandemic in 2020, Cabo Verde's real GDP per capita growth dropped sharply by 21.6%, sparking concerns over the

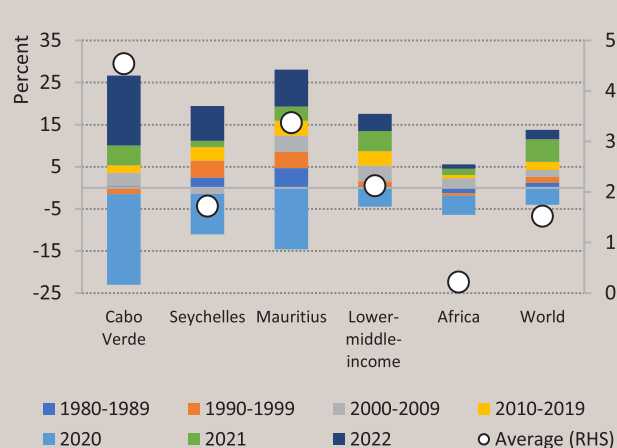
**Figure 2.1: Cabo Verde's real GDP growth vs Africa, world and peer countries**



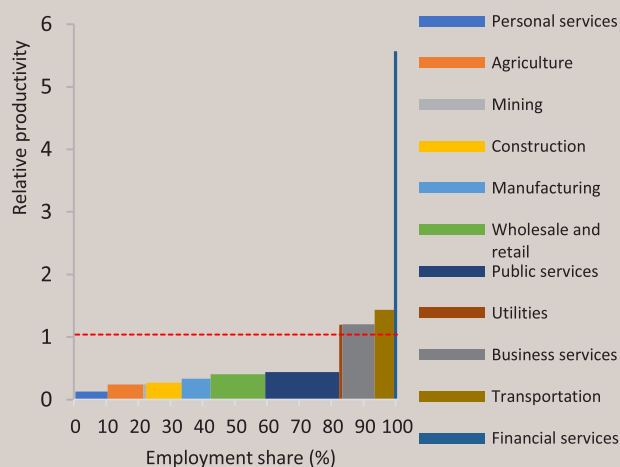
Note: The decades are based on simple averages

Source: African Development Bank statistics and IMF World Economic Outlook database

**Figure 2.2: Cabo Verde's real GDP per capita vs Africa, world and peer countries**

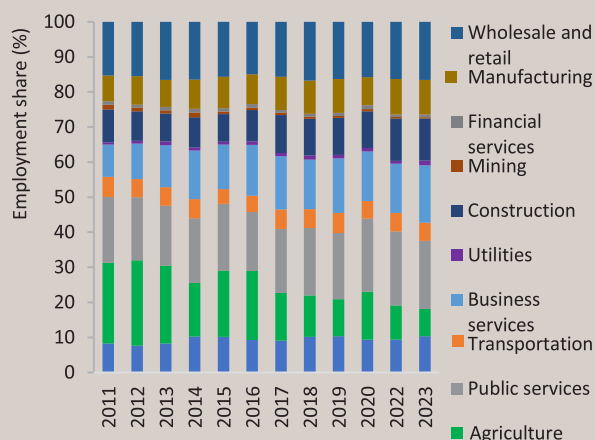


**Figure 2.3: Relative sectoral productivity and employment shares in Cabo Verde, 2018**



Source: Staff calculations using Cabo Verde's National Accounts for GDP value-added by sector, and the International Labour Organization database on employment statistics.

**Figure 2.4: Sectoral employment shares in Cabo Verde, 2011-2023**



Source: Staff calculations using Cabo Verde's National Institute of Statistics Employment Survey, 2011-2023.

ability of the country's growth model, driven by all-inclusive tourism,<sup>10</sup> to sustain job creation and poverty reduction. However, the post-COVID-19 period shows a rapid growth rebound in annual real GDP per capita, well above that of its peers, the African continent, and the world at large.

## 2.4. Country's structural transformation: drivers, bottlenecks and opportunities

### (a) Country's structural/economic transformation

According to the African Economic Outlook (2024), structural transformation is understood as the shift of an economy's structure from low-productivity, labour-intensive activities to higher-productivity, capital- and skill-intensive activities. Figure 2.3 depicts the relative labour productivity of 11 main sectors in Cabo Verde on the vertical axis and the employment share of each sector on the horizontal axis. Relative productivity is calculated as the

ratio of each sector's labour productivity to the average labour productivity of the economy. The horizontal dashed line represents the productivity level of the economy. The agricultural sector, which employed 11.8% of the workforce in Cabo Verde in 2018 (Figure 2.4), is 77% less productive than economy-wide productivity. Scarcity of fresh water and arable land (only 10%<sup>11</sup> of the land is arable), plus high vulnerability to climate change drives low agricultural productivity.

In contrast, utility (water and electricity) and business services, together employed 11.4% of the workforce, and are 15% more productive than the average of the economy. In between, personal services, mining, construction, wholesale and retail trade, public services and manufacturing all have productivity below the economy-wide average. Productivity gap in public services may signal declining efficiency in overall public administration governance, as evidenced by the deterioration of the country's ranking in the Mo Ibrahim Index<sup>12</sup> over the past decade. In one extreme lies the

<sup>10</sup> COVID-19 restrictions and disruptions in travel and logistical supply chains led to a sharp contraction of Cabo Verde's growth in the tourism sector by 71%, resulting in the temporary loss of 23,000 jobs.

<sup>11</sup> World Bank (2018).

<sup>12</sup> Cabo Verde's performance in the Mo Ibrahim Index of African Governance have deteriorated by -1.2 points over the 2012-2021 decade, currently ranking 4th out of 54 countries in Africa.



financial services which, although accounting for only 0.8% of total employment, are five times more productive than the average economy. This partly reflects the impact of relatively high interest rates for credit operations on banking sector profitability indicators.<sup>13</sup>

More concerning is the 68% productivity gap in the manufacturing sector compared to the economy, in a sector that accounted for 9.5% of total employment in 2018 and is traditionally associated with structural change. Manufacturing employs fewer workers. In addition, its relative productivity is below that of tradeable services, such as business and financial services and wholesale and retail trade. Furthermore, Cabo Verde's manufacturing sector remains undiversified and most of its production processes involve low-complexity systems relying on imported products. Key sub-sectors include cement, tuna and crustaceans processing, clothing and footwear, beverages and liquor distillation (AfDB, 2019).

#### **(b) Unpacking the country's structural transformation through labour productivity decomposition**

Figures 2.5 and 2.6 show the decomposition of labour productivity in Cabo Verde, using the McMillan and Rodrik methodology.<sup>14</sup> Labour productivity in Cabo Verde grew at 10.1% on average during 1992–2000, well above Africa's 1.5% average growth rate over 1991–1999. The country's growth is attributed to strong productivity growth within agriculture, industry and services. Cabo Verde's impressive growth success story 1992–2000 period was underpinned by the implementation of structural reforms in good governance, infrastructure development, human resource development and strategic partnerships

to attract FDI and remittances (AfDB, 2012). Productivity growth within agriculture accounted for 37% of the labour productivity growth in 1992–2000 (Figure 2.5). Meanwhile, over the past three decades, labour productivity in Cabo Verde has grown with limited structural change, implying that labour exiting low-productivity agriculture has been absorbed by manufacturing, wholesale and retail trade services. This is not surprising, given that Cabo Verde, unlike many African countries, has the lowest share of employment in agriculture on average.<sup>15</sup>

Productivity growth within non-agriculture sectors was strong during 1992–2000, with services accounting for 54% of total labour productivity growth, notably in tourism, which was the largest recipient of FDI (75%),<sup>16</sup> while manufacturing accounted for 9% of total productivity growth. Since 2001, productivity growth within non-agricultural sectors has been declining and growth was reducing during the 2011–2021 period. This shows signs of fatigue in Cabo Verde's growth model, which is driven by tourism, remittances and FDI, exposing the country to vulnerabilities from exogenous shocks (World Bank, 2018). If the current pattern of lack of structural change and fading dynamic productivity growth within non-agricultural sectors continues, overall labour productivity growth will eventually stall in Cabo Verde.

It is therefore imperative to develop policies aimed at scaling up capital investments, skills and technological innovation to boost productivity within modern sectors such as agri-business value chains and food processing, manufacturing and value-addition services linked to the tourism sector. This will preserve past gains and maintain structural transformation. Cabo Verde has potential

13 According to the Central Bank of Cabo Verde's Financial Stability Report (2022), average interest rates on credit operations remained above 8.7% in 2022. Returns on equity increased from 16.8% in 2021 to 19.9% in 2022. Similarly, returns on assets increased from 1.4% in 2021 to 1.5% in 2022.

14 McMillan, M., and D. Rodrik. (2011). "Globalization, Structural Change, and Productivity Growth." Working Paper 17143, National Bureau of Economic Research, Cambridge, MA.

15 Employment share in agriculture in Cabo Verde stood at 10% in 2022, as compared with 52% average in Africa, according to the World Bank database: <https://data.worldbank.org/indicator/SL.AGR.EMPL.ZS>.

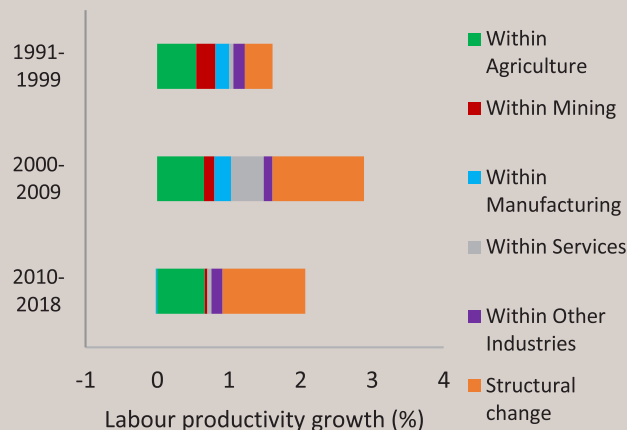
16 United Nations Industrial Development Organization (2021). Cabo Verde Country Industry Profile.

**Figure 2.5: Structural change in Cabo Verde, 1992-2021**



Source: Staff calculations based on World Bank and International Labour Organization (ILO) databases

**Figure 2.6: Structural change in Africa, 1991-2018**



Source: Staff calculations using the Economic Transformation Database (ETD) (Kruse et al. 2023)

to harness the blue economy through sustainable exploitation of its fisheries resources and marine biodiversity and by taking advantage of the Exclusive Maritime Special Economic Zone. Cabo Verde's peers such as Mauritius have succeeded in diversifying their economies beyond tourism by attracting private sector investments in other strategic services such as the financial sector. Therefore, Cabo Verde should endeavour to attract private sector banks and digital industries to reduce dependence on tourism services.

### (c) Rapid growth in income and jobs embodied in services exports: new evidence

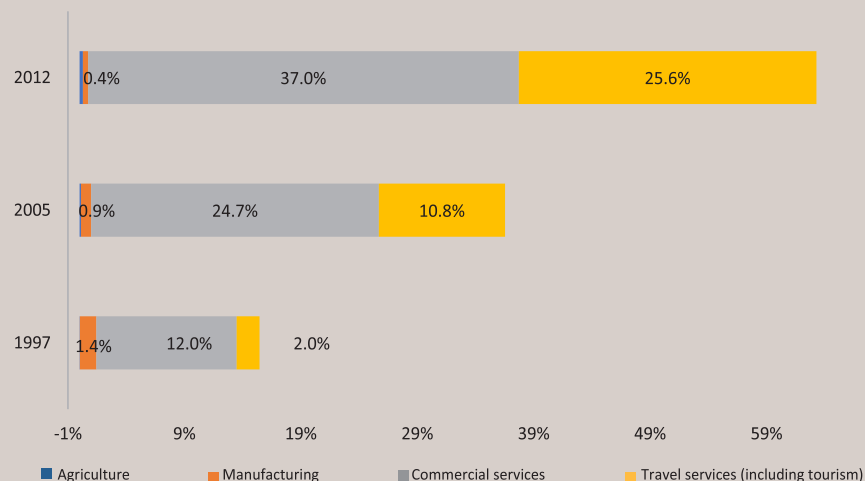
In the previous section, structural transformation was assessed through the lens of labour productivity decomposition. However, such an approach has limitations, due to lack of sector disaggregated data. Unlike the ETD database, World Bank data do not distinguish between manufacturing, mining and other industries. Furthermore, the analysis does not consider the implications of climate

change, gender and informality in labour mobility decisions and, most importantly, the role of foreign demand in driving structural change, in a country that is constrained by a small market size. Figure 2.7 shows the contribution of exports from selected sectors as a share of domestic value-added.

The share of agricultural exports in domestic value-added is almost non-existent, ranging from 0.03% in 1997 to 0.28% in 2012. Similarly, the share of manufacturing sector exports in domestic value-added is decreasing, while it is increasing in commercial and travel services (including tourism). The results are consistent with the broad patterns of structural transformation documented above, where within services, labour productivity was the driving force behind Cabo Verde's recent structural changes. These results bear strong policy implications for Cabo Verde's regional integration in the context of tariff liberalisation and free movement of labour under the AfCFTA. Cabo Verde's intra-Africa trade remains low,<sup>17</sup> in part constrained by non-tariff barriers. Therefore,

17 Intra-African exports account for 31% of Cabo Verde's global exports while intra-African imports account for 28% of Cabo Verde's global imports (see Tralac (2018): Cabo Verde: Intra-Africa Trade and Tariff Profile. Trade Data Update, Issue No.18, September 2018).

**Figure 2.7 Sectoral exports as a share of domestic value-added (%), 1997–2012**



Source: Staff calculations using Cabo Verde's National Accounts

### Box 2: AfDB is powering growth and structural transformation through energy investments in Cabo Verde

The role of energy in supporting structural transformation is undeniable. According to United Nations Conference on Trade and Development -UNCTAD (2017), development of modern energy infrastructure is directly linked to structural transformation through increased labour productivity in agriculture and industry (including manufacturing). In Cabo Verde, electricity access was challenging at the beginning of the 21st century with only 60.3% access rate. The situation was daunting in rural areas with less than 34% electricity access. Cognizant of these challenges, the African Development Bank successfully co-financed with the Japan International Cooperation Agency, the network transmission and distribution electricity project in six islands. The project helped build 385.4km of power distribution lines and exceeded its targets in terms of new electricity connections by 347% (10,435 people in urban areas) and 119.1% (2,060 people in rural areas). The 49 million Units of Account (UA), equivalent to USD 64.6 million, also targeted improvement of operational performance of the power utility and reduce losses. Today, 95.5% of the population has access to electricity (94.9% in urban and 96.9% in rural areas). Renewable energy supply increased from 1.2% in 2010 to 22% in 2022. The challenge now lies on harnessing the potential of renewable energy as to reduce the dependence on fossil fuels which still account for 80% of total electricity generation.

policy reforms aimed at boosting investments in infrastructure (energy, maritime ports and airports) and skills supporting light manufacturing and modern services (for example, ICT) will be critical to position the country in the regional and global markets. The Bank has supported Cabo Verde in enhancing structural transformation through the electrification of six islands as part of its High Fives of Light up and Power Africa (see Box 2).

#### (d) Drivers to accelerate structural transformation

The discussion in the previous sections highlighted the role of labour reallocation and within-sector productivity in fostering economic growth in Cabo Verde. Since structural transformation can play a pivotal role in aiding countries to attain socio-economic development at a much faster pace,

it is paramount to understand the main drivers to ensure the adoption of suitable policy reforms to harness the process. This section provides an analytical assessment of potential drivers of structural transformation in Cabo Verde, with a focus on (i) governance; (ii) exchange rate; (iii) trade policy; (iv) business environment; (v) urbanisation; (vi) technology and physical capital; (vii) quality of public infrastructure (for example, energy, water and sanitation, transport, and telecommunications); and (viii) human capital development.

**Governance:** Cabo Verde offers a stable and predictable political environment for investors (AfDB, 2019). In Transparency International's 2023 Corruption Perception Index (CPI), Cabo Verde had improved four places since 2022, being the 30th least corrupt country in the world and the 3rd in Africa. Over the past decade, Cabo Verde consistently ranked in the top four in the Mo Ibrahim Index. Cabo Verde's score on political stability in the World Bank's governance index improved from 78.8/100 in 2021 to 81/100 in 2022. Similarly, regulatory quality improved from 60.5/100 to 60.8/100 in the same period. However, rule of law deteriorated slightly from 61/100 to 60.8/100; government effectiveness score fell from 52.4/100 to 51.9/100; voice and accountability dropped from 76.8/100 to 76.3/100; and control of corruption also deteriorated from 82.4/100 in 2021 to 81.1/100 in 2022.

**Exchange rate:** as discussed in previous sections, Cabo Verde adopted an exchange rate peg to the euro in 1998. This has brought significant benefits, including price stability, smooth build-up of foreign reserves, stimulated trade and FDI (AfDB, 2012). Recent assessment by the IMF (2024) points to an

undervaluation of the real effective exchange rate which enhances structural transformation, based on the findings in McMillan et al. (2014).

**Trade policy:** Cabo Verde's openness to trade<sup>18</sup> and increased integration into the global economy offers a favourable environment for foreign investment in high-productivity sectors.

**Business environment and labour market flexibility:** Cabo Verde's business environment is constrained by weak enforcement of competition and sector regulations and strong presence of the State in various sectors.<sup>19</sup> Cabo Verde's Labour Code and Law No. 80/VIII/2014 promotes flexibility in the labour market,<sup>20</sup> including access to work and residence permits for foreign investors irrespective of the amount invested (2023 Investment Climate Statement).

**Urbanisation:** A report by the Organisation for Economic Co-operation and Development (OECD)/United Nations (UN)<sup>21</sup> shows that since 1990s, African cities had been able to maintain a stable pattern, with urbanisation translating into economic growth and improved living standards. In 2022, an estimated 68% of the population in Cabo Verde lived in urban areas, compared to 27% in 1982. Erratic weather conditions and the constant search for jobs in tourism-intensive islands of Sal and Boavista has placed significant pressure on urban infrastructure, undermining economic growth.

**Technology and physical capital:** Cabo Verde has made significant strides in digital transformation in a bid to position the country as a digital hub in the mid-Atlantic and to drive structural change.

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The evolution of labour productivity in Cabo Verde has not reflected a dynamic nature of structural transformation with excess labour being absorbed by high productivity industry and low-skills intensive services sectors, without significant gains in productivity in agriculture or more industrialization.

18 The country ranks 42nd of 169 countries surveyed in The Global Economy. Trade openness is measured as the ratio of exports plus imports as a percent of GDP. [https://www.theglobaleconomy.com/rankings/trade\\_openness/](https://www.theglobaleconomy.com/rankings/trade_openness/).

19 According to the World Bank (2024b) Private Sector Country Diagnostic, the State has a direct and indirect participation of 10% or more in at least 33 firms, accounting for 18% of GDP and employing 3,100 workers.

20 Cabo Verde scores 79.5/100 ("Reasonable Access to Decent Work") in the Labour Right Index (2022) developed by the Center for Labour Research. <https://labourrightsindex.org/lri-2022-documents/cabo-verde.pdf>.

21 OECD/UNECA/AfDB (2022), Africa's Urbanization Dynamics 2022: The Economic Power of Africa's Cities, West African Studies, OECD Publishing, Paris, <https://doi.org/10.1787/3834ed5b-en>.



### Box 3: AfDB unlocking opportunities for structural change in Cabo Verde

The African Development Bank has adopted a multipronged approach to support Cabo Verde's quest for structural change by addressing its most urgent development needs in infrastructure while harnessing opportunities for digital transformation. The EUR 50 million Praia Technology Park is helping to develop a digital economy infrastructure that will spur ICT innovations and entrepreneurship. The project comprises data centres, business centres and incubation centres for start-ups. Strategic partnerships have been established with international ICT tech companies to enhance the sustainability of the Technology Park business model. As energy is a key pre-requisite for digital transformation, the Bank is proud to have partnered with the European Investment Bank and others private investors to co-finance the EUR 63 million for the Cabeólica wind power plant, which now supplies 20% of the nation's electricity, making Cabo Verde a model country on clean energy. A second phase of Cabeólica is planned for 2024 to expand production capacity. Meeting this investment goal is expected to deliver an additional 25 MW in Cabo Verde's national power supply and continue to increase renewable energy penetration from 22% in 2022 to 30% by 2025, according to the Energy Sector Master Plan (2018–2040).

The e-government development index<sup>22</sup> increased from 0.405 in 2010 to 0.566 in 2022.<sup>23</sup> The proportion of the population using the Internet in Cabo Verde has increased from 37% in 2013 to 61.9% in 2022, surpassing the 36% average for sub-Saharan Africa.

**Quality of public infrastructure:** Cabo Verde ranks 9th out of 54 in the 2022 Africa Infrastructure Development Index with a score of 49.8/100, as compared to 47.96/100 in 2019. The country faces a scarcity of fresh water and 90% of the water consumed is desalinated. Water access rates are 93% in urban and 80% in rural areas, while 21% of the national population lacks access to basic sanitation services. Renewable potential, namely wind and solar photovoltaic, has been estimated by Gesto (2011)<sup>24</sup> at 258 MW and 315 MW which, if properly harnessed, could drive green industrialisation. The Bank is supporting Cabo Verde to enhance a just energy transition and digital transformation as part of the implementation

of its High Fives of Light up and Power Africa and Industrialise Africa (Box 3).

**Human capital development:** Cabo Verde made significant strides in investments in education. The share of education spending as a percentage of government spending (15.1%) is above the world average (12.7%) in 2021. However, there are persistent gaps in knowledge-intensive employment<sup>25</sup> critical to drive the fourth industrial revolution and structural transformation. As a result, Cabo Verde ranks 91st out of 132 economies surveyed in the 2023 Global Innovation Index (GII) of the World Intellectual Property Organization.

#### (e) Key bottlenecks to fast-paced structural transformation

**Demographic challenges:** Cabo Verde's population is young, with a median value of 28.8 years in 2024, as compared to the world median of 30.5 years (Worlddata.info, 2024). The working age

22 EDGI (2022) United Nations E-Government Survey. <https://publicadministration.un.org/egovkb/en-us/Reports/UN-E-Government-Survey-2022>

23 <https://publicadministration.un.org/egovkb/en-us/Data/Country-Information/id/32-Cabo-Verde>.

24 Gesto. Energy Plan for Cabo Verde. <http://www.energiasrenovaveis.cv/2011>.

25 According to the GI (2023), knowledge-intensive employment in Cabo Verde stood at 17.6% in 2019, that is, a 0.46 percentage point decline compared to 2015 levels.

population<sup>26</sup> grew on average by 1.1% per year over 2000–2022, as compared to 0.5% during 1980–2000. This puts significant pressure on the labour markets, given the scarcity of jobs. The evidence also indicates that rising working age population can contribute to realising the demographic dividend by boosting growth through increased productivity. It can also generate higher savings rates, as working-age adults tend to produce more than that they consume (UNDESA, 2023). Cabo Verde is investing in ICT infrastructure and TVET to improve the skills of the growing youth labour force and meet the needs of the private sector.

**Climate change:** A higher frequency and intensity of extreme weather events (for example, droughts, floods and storms) has impacted water resources, infrastructure and agricultural productivity. Evidence shows that the volcanic eruption in Fogo island in 2014–2015 resulted in USD 30.5 million (1.7% of GDP) of losses, with 85% being infrastructure damage and 15% resulting from agricultural production and tourism losses (Government of Cabo Verde, 2015).

**Informal sector:** Data from INE (2022) indicates that approximately 53% of the employed population in Cabo Verde works in the informal sector. These are mostly low-skilled workers that exited low-productivity primary sectors (for example, agriculture and fisheries), and mostly women (63.6%) owing to the adverse effects of climate change and were left with the default option of joining informal services and other precarious jobs in the tourism industry in urban centres without any form of social safety nets and integration into the formal tax system.

**Political issues:** Cabo Verde enjoys political stability underpinned by strong democratic institutions. The country has displayed strong commitment to reforms, and corruption and bribery are not widespread as evidenced by the recent improvement by four points in the 2023 CPI index by Transparency International. This development reflects reduced pressure of political instability as a source of concern.

**Financial constraints:** Despite the recent efforts to enhance access to financial services, approximately 44%<sup>27</sup> of MSME perceive access to finance as their biggest obstacle for business growth. High interest rates on credit operations, lack of guarantees for “bankable projects”, and the risk aversion of banks – as evidenced by the low rate of loan-to-deposit ratio (54.3% in 2023) – all undermine credit expansion to the private sector, constraining production and employment growth.

In short, Cabo Verde faces several key vulnerability drivers that threaten its socio-economic stability and development prospects. Demographic challenges arise from a young and rapidly growing working-age population, which places significant pressure on the labour market owing to the scarcity of jobs. While this demographic trend has the potential to yield a demographic dividend, the lack of adequate employment opportunities remains a critical issue. Climate change poses another major risk, with increased frequency and intensity of extreme weather that have severely impacted water resources, infrastructure and agricultural productivity. The informal sector is also a significant fragility driver, with approximately 53% of the workforce employed in low-skill, precarious jobs without social safety nets, exacerbating vulnerability among the population. This is particularly true for women. High interest rates, lack of guarantees, and the risk aversion of banks, which stifles credit expansion and constrains production and employment growth. Despite these challenges, Cabo Verde benefits from political stability and strong democratic institutions, although these positive aspects alone are insufficient to counterbalance the other fragility drivers without comprehensive and targeted interventions.

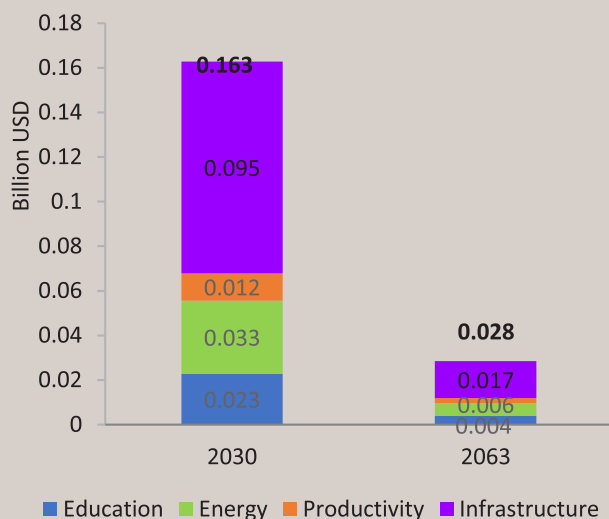
## 2.5. Finance to fast-track Cabo Verde’s structural transformation: How much is at stake? Country’s commitment to structural change

### (a) Structural change in the national development plan

<sup>26</sup> <https://data.worldbank.org/indicator/SP.POP.1564.TO.ZS?locations=CV>.

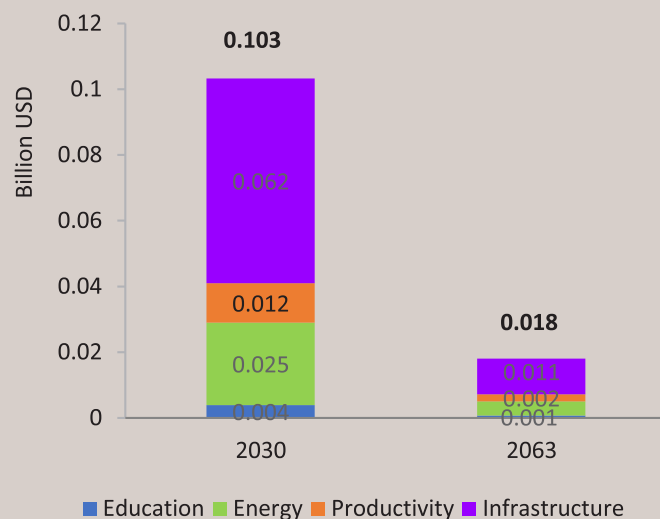
<sup>27</sup> World Bank (2023). “Cabo Verde: Accelerating Growth and Fostering Resilience. Country Economic Memorandum.” World Bank, Washington, D.C

**Figure 2.8: Annual financing needs**



Source: Staff calculations based on the database from Sachs et al. (2023), UNESCO, CIA, EIA, NASA, IMF, and World Bank.

**Figure 2.9: Annual financing gap**



Source: Staff calculations based on the database from Sachs et al. (2023), UNESCO, CIA, EIA, NASA, IMF, and World Bank.

The country's Strategic Plan for Sustainable Development (PEDS, 2022–2026) is grounded on four main pillars, notably (i) economic recovery and diversification – aimed at turning Cabo Verde into a circular platform in the mid-Atlantic; (ii) social development – intended to promote human capital development, social inclusion and eradication of extreme poverty; (iii) environmental sustainability – targeting climate action, climate resilience, quality of the environment and biodiversity conservation; and (iv) governance and national sovereignty – aimed at consolidating the gains made in democracy and national sovereignty, fostering greater participation of the diaspora in national economic development and promoting regional integration.

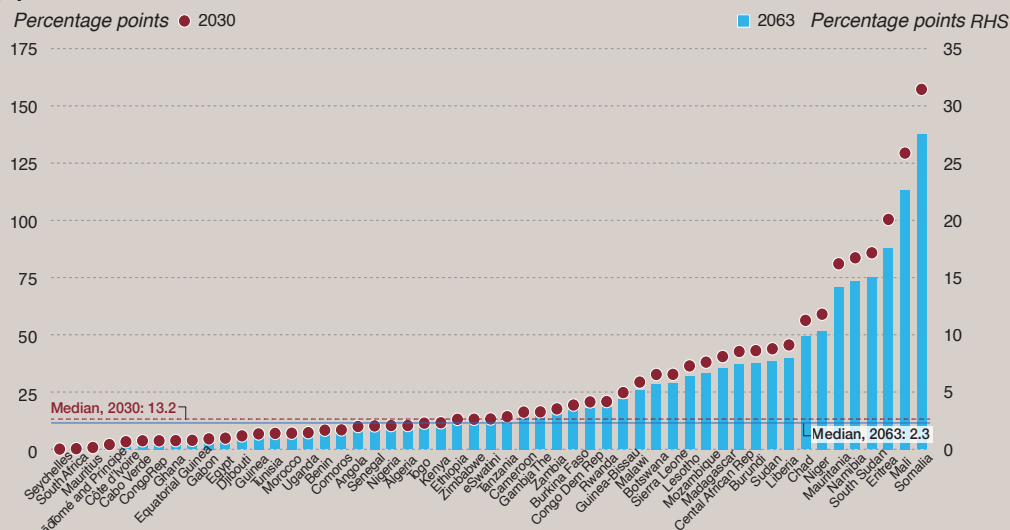
#### (b) Financing needs and financing gap

To enhance structural transformation, it is critical for a small island nation such as Cabo Verde to access financing in a context of limited fiscal space owing to a high debt burden and exacerbated by high borrowing costs and limited concessional loans. This section discusses AEO (2024) estimates of financing needs and financing gaps to achieve some key SDGs that are more directly linked to

achieving the transformation and require far more investment than others, in particular Goals 4 (Quality education); 7 (Energy); 8 (Productivity); and 9 (Infrastructure). For each African country, annual financing needs and the associated financing gap are calculated for both the 2030 Agenda for Sustainable Development and the African Union's Agenda 2063.

According to the AfDB (2024) estimates, Cabo Verde would need USD 163 million, or about 7.3% of the country's projected 2024 GDP, annually until 2030 to accelerate its structural transformation process (Figure 2.8). The largest financing needs are in infrastructure (about USD 95 million per year until 2030, or 4.2% of GDP), given the need to invest in multi-modal inter-island transportation infrastructure (for example, maritime ports, airports and ferries) as well as to enhance regular maintenance and expansion of the 1,228 km of national road network. This is followed by energy (USD 33 million per year, or 1.5% of GDP), in part to meet investment needs in renewable energy and realise the Government's targets of 30% share of renewable energy penetration by 2025, 50% by 2030, and 100% by 2040. Education and

**Figure 2.10: Required increase in tax-to-GDP ratio to close the estimated annual financing gap in Cabo Verde**



productivity-enhancing research and development account for 1% and 0.5% of projected 2024 GDP.

When the deadline for Agenda 2063 is used as a reference, the annual financing needs fall to USD 28 million, or about 1.2% of Cabo Verde's projected 2024 GDP (Figure 2.9). Again, the bulk of these resources are in infrastructure (61% of the total), highlighting the critical investment needs in the sector, followed by energy (21%) and education (14%).

Given, the current country performance levels on these critical sectors and their projected values, which are assumed to change in line with GDP per capita, the annual financing gap to fast-track structural transformation is estimated at USD 103 million per annum until 2030 (or about 5% of Cabo Verde's 2024 GDP) under the SDG framework and USD 18 million per annum until 2063 (or about 1% of GDP) under the Agenda 2063 deadline, with a longer time horizon and spread of investment across each SDG target. Overall, infrastructure remains the main contributor to Cabo Verde's financing gap (61.1%), followed by education (22%), energy (11%) and productivity (5.6%).

### (c) Closing the financing gap through domestic resource mobilisation

Figure 2.10 displays the required increase in countries' current tax-to-GDP ratios to close their financing gap by 2030 or 2063. Cabo Verde will need to increase this ratio by a median of about 3.7 percentage points – bringing the current median ratio to 23% of GDP – to be able to close its financing gap by 2030, assuming that all the mobilised additional tax revenues are efficiently deployed and allocated to that objective. A median increase of 0.6 percentage points will be required to close the financing gap by 2063. The enormity of median tax-to-GDP ratio of 23% required to close the financing gap and fast-track structural transformation casts doubt on the country's capacity to mobilise the funding. The international financial architecture, with contributions from the private sector, should therefore be an integral part of the financing strategy.

## 2.6. Concluding remarks and policy recommendations

The above analyses strongly suggest that accelerating Cabo Verde's structural transformation



#### **Box 4: AfDB fostering economic transformation through food production and transport infrastructure for market integration**

Food security is critical for Cabo Verde's socio-economic development as the country imports an estimated 80% of its consumer goods, straining the trade balance and foreign reserves. Therefore, the Bank is currently preparing a EUR 20 million agricultural value chains programme targeting eight islands of the archipelago. The project will also support blue economy interventions aimed at boosting the income of fishers and fish processors in coastal areas from 6% in 2019 to 12% by 2024. Overall, the project targets the creation of 2,700 direct jobs, of which 30% are women. The project will contribute to improve the nutritional status of 1800 people, that is 16% of the country's total population at risk of food insecurity. Cabo Verde's trade and regional integration is constrained by unreliable inter-island transportation infrastructure. The Bank has partnered with the European Union and the Government of Cabo Verde to finance the modernization of the Ports of Maio and Palmeira to position the country to benefit from the implementation of the AfCFTA. When completed, these two ports will significantly transform the economy of Cabo Verde with annual passenger traffic rising by 34% from 41,700 to over 55,000 in 2024. Merchandise traffic will rise by 184% from 150,900 tons to 429,000 tons.

will require a multipronged approach, consisting of the following elements, spearheaded by the Government with support from the private sector, DFI, and MDBs:

- **Establish and institutionalise endogenous development plans and policies tailored to areas of comparative advantage as priorities and implement them consistently, while avoiding policy reversals that tend to disrupt progress.** The development of multi-annual sectoral master plans should be accompanied by the establishment of coordination committees with adequate responsibility and power that bring together various stakeholders to guide investment decisions.
- **Scale up investments to build requisite human capital suited to local realities, circumstances and development priorities.** Cabo Verde needs to scale up investments in education at all levels to build and improve the quality and relevance of technical and soft skills required to drive its development agenda tailored to local contexts and circumstances. More specifically, the country needs to prioritise scaling-up skills in science, technology, engineering, and

mathematics to leverage its resources and drive structural transformation.

- **Scale up domestic resource mobilisation (DRM) and prioritise prudence in PFM.** Cabo Verde must own its development agenda and have the primary responsibility for financing its structural transformation. Tax-to-GDP ratio – around 18.6% of GDP in 2023 – is above Africa's average of 15.6%; therefore, instead of increasing the tax burden, the country should strengthen DRM by broadening the tax base, reducing tax incentives and rationalising tax expenditures. Strengthening tax compliance through improved tax inspections and audits is critical to boost DRM. Enhancing the formalisation of the informal economy could also boost DRM. The size of the informal sector in Cabo Verde significantly limits the tax base and revenue as there are 33,000 informal enterprises generating 40,000 jobs. Adoption of incentive schemes such as social insurance, pension schemes and simplified taxation – conditioned on registration – can contribute to boosting domestic tax collection. As institutional capacity remains weak, the Bank's PFM Academy could help respond to the urgent need for accelerated capacity development

through the provision of training, technical assistance, and policy dialogue.

- **Build and deepen markets (for goods and services, and capital and finance) at national and regional levels.** Ongoing investments in the modernisation of the Ports of Maio and Palmeira and airport concessions are expected to improve efficiency in inter-island transport infrastructure and promote trade. This will also enable Cabo Verde to better position itself to benefit from the AfCFTA agreement. However, institutional support and capacity-building, especially for structuring PPPs, is critical in order to maximise the benefits from infrastructure concessions and privatisation of SOEs.
- **Create targeted and streamlined incentives to catalyse mobilisation of private capital flows to support Cabo Verde's endogenous development plans, in key sectors for structural transformation.** As financing needs for structural transformation remain huge (for example, about USD 163 million/annually), Cabo Verde could incentivise private sector participation (domestic and external) to support structural transformation. The use of innovative financing instruments such as blended finance and guarantees could increase private participation in infrastructure for green growth by de-risking the sector. The development of sustainable finance instruments (including green bonds and loans; and sustainability bonds and loans), as well as carbon credit markets, could boost private sector investment in green sectors.
- **Invest in natural capital accounting, beneficiation and conservation and include it in the system of national accounts to expand the size of the economy.** According to the World Bank (2021)<sup>28</sup>, Cabo Verde's

natural capital wealth grew by 258% from 1995 to 2018, mostly driven by renewable energy resources, forest, timber, ecosystem services, protected areas, cropland and pastureland. However, these figures underestimate the country's natural wealth amidst the abundance of fisheries resources, marine biodiversity and green wealth. Therefore, MDBs, bilateral donors and DFIs should seek greater synergy in strengthening capacity-building for natural capital accounting in small island developing countries, including Cabo Verde, to expand the size of the economy. Recent data from AfDB (2023) shows that Cabo Verde is not deriving a fair share of its natural resources rents which declined from 33.3% in 2010 to 11.5% in 2020. Cabo Verde has been a candidate for the Fisheries Transparency Initiative (FITI) since February 2023. The country successfully prepared its first FITI report in 2022 and a second report is expected by December 2024. These reports will contribute to improve the dissemination of transparency fisheries practices, including strategies to fight illegal fishing and overfishing.

- **Invest in youth entrepreneurship development programmes to harness Cabo Verde's demographic dividend.** With an estimated 65% of the population under the age of 25, Cabo Verde is in the pre-demographic dividend phase and must take proactive steps to create jobs and skills. With 53% of the working age population engaged in informal activities, and TVET enrolment rates averaging 5% of the population, reaping the benefits of the demographic dividend from the Cabo Verdean youth would significantly depend on investment in human capital development and on creating economic and job opportunities for young people.
- **Launch an ambitious national digitalisation programme for broad-based**

<sup>28</sup> World Bank. 2021. The Changing Wealth of Nations 2021: Managing Assets for the Future. Washington, DC: World Bank. doi:10.1596/978-1-4648-1590-4.

**policy implementation to accelerate structural transformation.**

The Bank's EUR 50 million ongoing investment in the Praia Technological Park aims to position Cabo Verde as a digital hub in the mid-Atlantic. The project comprises data centres, conference centres and incubation labs for start-ups to equip young people with adequate digital and entrepreneurship skills to compete in the labour market. This is part of the Bank's Jobs for Youth in Africa Strategy, aimed at providing opportunities for decent jobs and thereby creating hope for young people and women, for a brighter future.

- **Take proactive actions to harness governance of macro-economic policies**

**and business environment necessary to improve risk profiling and perceptions and to harness innovative global capital and financial instruments needed to build capacity in project preparation.**

Cabo Verde must build capacity in project preparation and implementation, enhance governance of macro-economic policies and create a better investment climate to improve risk profiling and perceptions. The country could emulate the Bank's Strategy for Economic Governance in Africa and devise strategic reforms to promote transparency and accountability in public service delivery, stimulating government effectiveness and building business enabling environments.

# FINANCING STRUCTURAL TRANSFORMATION IN CABO VERDE

## 3.1. Key Messages

- **Cabo Verde's journey towards structural transformation demands significant investments in infrastructure, human capital, climate action and productivity-enhancing technology.** Consequently, the current call for reforms of the international financial system offers a pathway for Cabo Verde's meaningful participation in resource allocation decisions that will help to unlock vital resources for these investments.
- **The failure of the GFA to deliver development financing at scale to small island developing states (SIDS) such as Cabo Verde, as well as other developing nations, has amplified calls for reforms.** Cabo Verde's immense financing needs for enhancing structural transformation (for example, USD 163 million/annually until 2030 – or about 7.3% of projected 2024 GDP), in addition to those required for emergency and climate action, need a system that is quick, accountable and transparent to support debt resolution mechanisms and unlock resources at affordable conditions.
- **Existing debt resolution and initiatives, such as the G20's Common Framework (CF), are deemed slow and cumbersome and do not cover middle-income countries in debt distress.** Expanding the CF to middle-income countries with significant official debt or requiring debt restructuring could ensure future credibility of the CF. Enhancements, such as "Brady bonds" initiatives, debt relief for climate purposes and sovereign debt authority systems, are also imperative for expediting debt workouts and ensuring sustainable debt management.
- **Implementation of the proposed reforms could significantly increase financing for Cabo Verde's structural transformation and propel the country to a higher level of economic development.** In particular, the recycling of SDRs through MDBs could increase financing for Cabo Verde. The recent decision by the IMF board allowing countries to channel their SDRs through MDBs is a step in the right direction towards increasing access to financing for social and climate projects by developing nations, including Cabo Verde.

## 3.2. Introduction

The chapter presents the external financing needs of the country to achieve structural transformation while dealing with the threat of climate change. It uses the Bank's estimates on financing needs and gaps to fast-track structural transformation (AEO, 2024) and to finance climate actions (AEO, 2022 and 2023) respectively by 2030. The chapter uses the Bank's estimates to assess the country's capacity to increase the tax-to-GDP ratio to close the financing gap and thereby fast-track structural transformation by 2030 and 2063. It also gives reasons for the need to reform the international financial architecture.

## 3.3. Cabo Verde's stance on the need to reform the international financial architecture

Cabo Verde has displayed a strong record regarding commitment to reforms for sustainable development. These have been sustained by political stability, strong institutions and rule of law, and limited levels of corruption. In the early years following the country's independence in 1975, Cabo Verde succeeded in mobilising ODA consisting of soft loans and grants, and remittances from the diaspora, which were estimated to account for 40% to 60% of GDP. With the advent of the graduation from low-income to lower-middle-income income status in 2007, Cabo Verde lost a significant portion of concessional financing, with repercussions for economic growth. In the years before the country's graduation, Cabo Verde had access to several preferential trade agreements, which helped protect the economy from shocks and mobilise resources that allowed the country to enhance resilience to the financial crises. According to OCDE (2019), the use of the "small states exception" by MDBs has also helped ensure predictability and gradual phase-out of concessional financing. Furthermore, with the option of a "blend" window provided by some MDBs, including the African Development Bank and the World Bank,

Cabo Verde was able to increase access to non-concessional funding from USD 7.11 million before the graduation to lower middle-income country (2000–2007) to USD 279 million after the graduation (2008–2016).

Following the graduation, Cabo Verde's human development indicators, which had recorded impressive growth, were challenged owing to shrinking financing for sustainable development. From 2008 to 2016, Gross National Income (GNI) declined from USD 3,500 to USD 3,000; inequalities between islands increased as the benefits of the booming tourism sectors were shared across the urban and rural areas. Now, after 17 years since graduation to a lower-middle-income country, Cabo Verde's GDP per capita has only grown marginally by 0.8% on average per annum, moving from USD 3,268 in 2008 to USD 3,754 in 2022. In contrast, public debt increased from 57.2% of GDP in 2008 to 127.2% of GDP in 2022. This sharp increase in public debt highlighted the difficulties the country has been facing in continuing to raise international capital on affordable borrowing terms, including access to highly concessional loans and grants.

As the debate regarding the reform of the international financial architecture gains momentum, Cabo Verde, as a SIDS that is highly vulnerable to climate shocks, is expected to benefit from initiatives championed by MDBs such as the African Development Bank and the Inter-American Development Bank, aimed at issuing hybrid capital targeting green, social and sustainability bonds to finance projects in critical areas for structural transformation, notably food security, access to water and sanitation, health and climate change. These priorities are in line with the statement made by the African Group of Negotiators<sup>29</sup> during the African Caucus in July 2023 at Sal Island in Cabo Verde, which calls for (i) the reforms of the GFA (notably within the IMF and World Bank) to be extended beyond climate change, and also covers issues of hunger, poverty, public goods and SDGs;

29 African Climate Wire (2023). African Governors Propose Targeted Reforms to Climate Finance Architecture. <https://africanclimatewire.org/2023/07/african-governors-propose-targeted-reforms-to-climate-finance-architecture/>.



(ii) addresses the unsustainable levels of public debt in African economies –specifically arguing for a “tripling of concessional financing” complemented with grants; (iii) calls for capital increases amid reluctance by developed nations; and (iv) advocates lowering the cost of borrowing for African countries, by adopting measures such as debt relief and cancellation and debt restructuring; (v) advocates for the scale-up of private climate financing to USD 2.8 trillion with electricity access being accorded at least USD 20 billion/year; and (vi) calls for the prevention of illicit financial flows.

Specifically, Cabo Verde could benefit from the reform of the GFA in multiple ways through (i) increased access to low-cost financing from MDBs and DFIs; (ii) greater access to de-risking instruments for private sector investments; (iii) greater access to climate finance (green bonds, blue bonds and sustainable bonds); (iv) monetisation of its natural capital wealth (for example, fisheries and biodiversity); (v) access to concessional financing from MDBs, DFIs and bilateral donors for financing of projects related to the preservation of global public goods (for example, eco-tourism, climate adaptation and mitigation, prevention of pandemics, etc.); (vi) improved PFM reforms and capacity-building in debt management and DRM; and (vii) tapping into diaspora remittances.

### 3.4. Mobilising additional resources for Cabo Verde’s structural transformation

Chapter 2 of this report contained a granular discussion and analysis on the evolution of structural transformation in Cabo Verde. Achieving significant progress in structural transformation requires policy and regulatory reforms to encourage innovation and entrepreneurship, as well as major investments in infrastructure, human capital and technology. Specifically, Cabo Verde needs to invest in ICT infrastructure and TVET to equip young people

with the right skills required by the private sector. In addition, the modernisation of ports and airports is vital to expand the economy and take advantage of the AfCFTA. To succeed in its structural transformation and reach the SDGs, Cabo Verde needs investments of about USD 163 million per year. The Bank estimates that financing the four key pillars directly relevant to fast tracking structural transformation alone will require filling a financing gap of USD 103 million per year (see Chapter 2 above). This investment will need be financed by external flows and domestic, private and public resources.

Reforms of the GFA should support increasing external flows to finance Cabo Verde’s economic transformation. After reaching a peak of 11.9% of GDP in 2006, FDI net inflows to Cabo Verde have been erratic and are down to 5.5% of GDP in 2022 (Figure 3.1). Remittances, which accounted for 28.2% of GDP in 1980s, have since declined by 50% to reach 14.1% of GDP in 2022, as migrant workers in host countries struggle to sustain work opportunities amidst the economic crisis and declining disposable incomes on account of high inflation. Similarly, net ODA, which used to account for 55.4% of GNI in 1985, has dwindled significantly, currently accounting for less than 3.8% of GNI in 2022, according to World Bank data (2024a). It is unlikely that traditional ODA to Cabo Verde will increase in the short term because donor countries are facing many competing priorities owing to shrinking fiscal space.

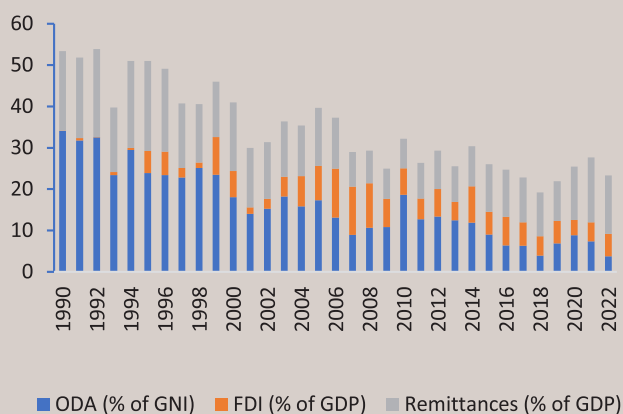
Moreover, as at end-2023, only few advanced countries – Denmark, Sweden Germany, Luxembourg and Norway met the ODA threshold of 0.7 percent of GNI. In the short run, the best hope for significantly increasing ODA to Africa, and Cabo Verde in particular, is the recycling of SDRs,<sup>30</sup> the implementation of generalised capital increase by MDBs, coupled with the implementation of the Capital Adjustment Framework reforms by the MDBs, provided that this does not result in the hardening of the lending terms and illicit financial flows.

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**Accelerating structural transformation in Cabo Verde and the rest of Africa will require a reform of the global financial architecture that can help mobilize resources at scale and on affordable terms to support growth, poverty reduction and intended climate change needs and enhance resilience.**

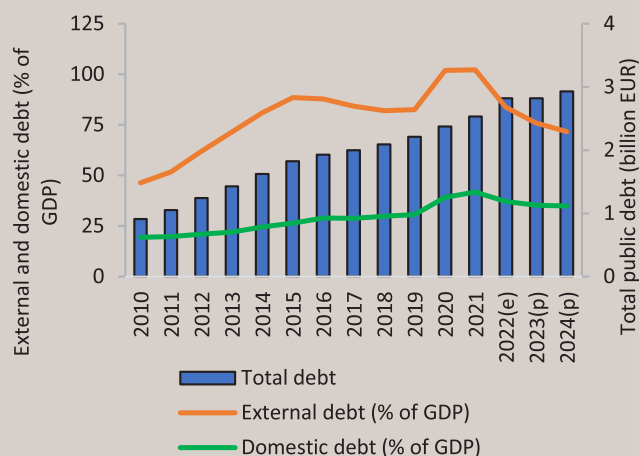
30 This innovative financing instrument offers several advantages, including the possibility of lending at least USD 4 for USD 1 equivalent SDR, through the African Development Bank, the Inter-American Development Bank and other MDBs, to finance development projects (AfDB, 2024). <https://www.afdb.org/en/news-and-events/press-releases/african-development-bank-and-interamerican-development-bank-welcome-international-monetary-funds-imf-executive-boards-decision-approving-use-sdrs-hybrid-capital-instruments-70788>

**Figure 3.1: Evolution of FDI, ODA and remittances (% of GDP) in Cabo Verde**



Source: World Development Indicators (WDI)

**Figure 3.2: Evolution of public debt (domestic and external as a share of GDP)**



Source: Ministry of Finance, Cabo Verde

### 3.5. Dealing with Cabo Verde's debt

Although the debt situation in Cabo Verde is not systemic and the risk of external debt distress improved from "high" to "moderate" in 2022, the country's current debt-to-GDP ratio of 119.9% in 2023 (Figure 3.2), makes its overall public debt still at high risk of debt distress. Furthermore, Figure 3.3 shows that the level of indebtedness is largely driven by interest rates differentials<sup>31</sup> and primary balances. This presents a concern for the future development of the small island nation amidst heightened global shocks. Addressing Cabo Verde's debt, in particular, requires reforms of the global debt and financial architecture to avoid further debt build-up, as well as actions to facilitate restructuring of the existing stock of debt. To facilitate debt restructuring there is a need to (i) prioritise access to longer-maturity and highly concessional debt; (ii) implement debt relief to free up resources for climate actions; (iii) create a sovereign debt authority and a sovereign insolvency system; (iv) convince G20 countries to

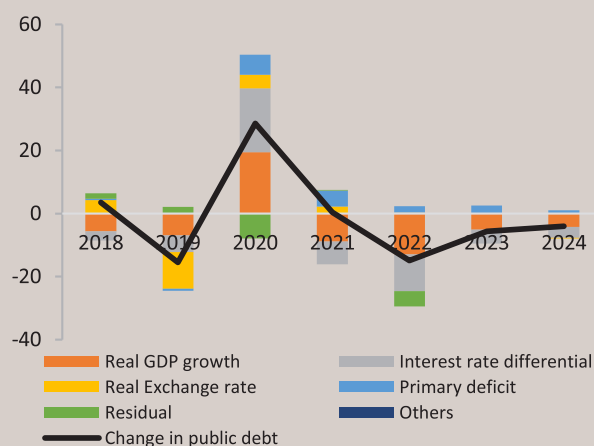
enact legislation that encourages private lenders to participate in debt workouts; (v) implement the new IMF policy of lending in arrears that would also open the door for MDBs to lend to countries during protracted debt negotiations; and (vi) expand CF eligibility to middle-income countries, such as Cabo Verde, that have significant official debt and require debt restructuring. Furthermore, there is a need to (i) further support Cabo Verde's capacity development in debt management; and (ii) improve transparency in credit ratings by private agencies.

### 3.6. Financing climate action

According to Cabo Verde's updated 2021 Nationally Determined Contributions, meeting adaptation and mitigation costs outlined in this policy will require USD 2.3 billion between 2020 and 2030, which translates to USD 213 million annually during this period. About 42.7% of this amount would be allocated to adaptation and resilience; 42.7% for mitigation; and 14.6% for loss and damage, with the Government committing to financing one-third of amount through

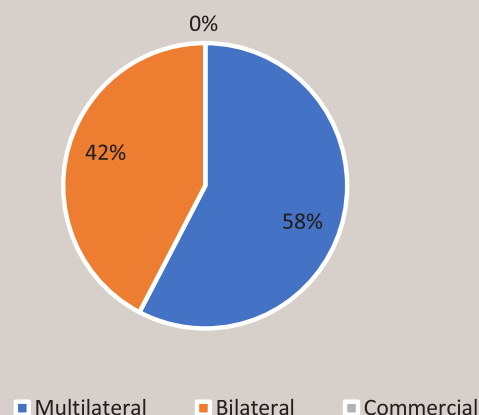
31 High borrowing costs stifle Cabo Verde's structural transformation. According to Damodaran, A. (2024), Cabo Verde's average sovereign risk premium is estimated at 9.51%. This is far above 1.1% for advanced economies and 4.9% for emerging market economies.

**Figure 3.3: Key drivers of public debt variation in Cabo Verde**



Source: Staff calculations using data from the IMF (2024)

**Figure 3.4: Decomposition of External debt in Cabo Verde (2024)**



### Box 5: AfDB deepening capital markets for green growth in Cabo Verde

Cabo Verde's capital market is on the verge of becoming a vital vehicle in driving economic diversification in the small island state. The launching in 2022 of the USD 350,000 grant for the first Capital Market Master Plan, funded by the AfDB, will propel the development of vibrant capital markets in the country. The AfDB financed the preparation of the Strategic Plan for Blue Economy and Investment Plan (PNIEB) in 2019. The project was implemented by FAO. A total of 40 projects were identified within the framework of the PNIEB, of which five operations have already benefited from financing and are being implemented. Another 16 operations were formulated by other development partners (World Bank and the United Nations).

domestic sources. Cabo Verde's national plan for adapting to climate change, approved by the Government in 2021, provides for interventions in the institutional framework, in technology and in the resilience of the most vulnerable, which will cost USD 30 million by 2026, not including the financing needs required for mitigation measures.

Cabo Verde could capitalise on its stable regulatory framework for PPPs and the experience gained in blended finance, notably from independent power producers in solar and wind energy, and leverage resources to close the private climate finance gap estimated at USD 120.3 million annually (4.2% of GDP). The Government has promoted innovative

climate financing instruments such as the social bond, envisaging environmental sustainability; and the blue fund launched on the Blu-X sustainable finance platform.

Cabo Verde could also learn from the experience of Seychelle, in harnessing the blue economy through blue bonds and debt swaps, and from Maldives in diversifying the economy beyond tourism by upgrading fishery value chains. Reform of the GFA could leverage additional funds on more advantageous terms. To ensure access to and optimal use of financing for climate change from MDBs, crucial reforms in the short term include establishing a blue grants fund and blue investment

fund, deepening capital markets (see Box 5) and enhancing macro-economic stability.

### 3.7. Policy recommendations

Mobilising resources at scale and on affordable terms for the financing of structural transformation will require the following actions:

- **Adding the country's voice to benefit from the acceleration of the scale of low-cost concessional financing for development.** **On its own**, Cabo Verde might be unable to influence the nature and shape of the current international financial architecture. However, together with other African countries, agencies and supporters from the broader international community, change is possible. This coalition of the willing must be categorical about what is required to finance African development more sustainably while also making it plain that African governments are willing to commit to good governance and accountability.
- **Adding the country's voice and benefit from the reform of the global debt architecture to make it more transparent, nimble, accessible and affordable for developing countries.** Cabo Verde could add its voice to the African Group of Negotiators and SIDS as they engage with credit rating agencies to improve their rating criteria by taking into account the value of natural capital, among others, in assessing a country's debt risk profile. This includes reforms to reduce the amount of subjectivity in credit ratings assigned to African countries by increasing transparency and distinguishing between the model-based and discretionary components of their sovereign ratings. In that regard, efforts to accelerate the creation by the African Union of an African Credit Rating Agency should be pursued. African countries, including Cabo Verde, could also argue for increased transparency on the terms of loans through voluntary disclosure of information, to avoid being trapped into signing contracts for resource-backed loans. Bilateral creditors should also facilitate debt restructuring mechanisms under the G20 CF.
- **Cabo Verde must institute reforms for strengthening its National Climate Fund and Disaster Management Systems** with appropriate and independent governance structures. This should be complemented by proactiveness on the part of international financial institutions (IFIs) in first introducing and using State-contingent debt instruments (SCDIs) and making a concerted effort to incentivise widespread adoption of sovereign SCDIs in order to support better public debt management; climate-proof public finances; and facilitate faster response with a built-in debt deferral mechanism for pre-agreed shocks so as to help avoid further human suffering and economic loss. The uptake of SCDIs would help move governments in developing countries, including in Cabo Verde, towards faster, more reliable post-disaster finance.
- **Cabo Verde could join the group of African countries and advocate for a greater voice of the continent in MDBs and IFIs, aligned with its growing continent's share of world GDP and population:** For instance, the G20 could expand its membership beyond South Africa and the African Union by inviting two or three more African countries. The IMF and the World Bank could further democratise their decision-making processes by introducing a double majority rule for most decisions (majority of shares plus majority of member countries) and change the rules allocating IMF quotas and voting rights at the World Bank to reflect new economic and demographic realities.
- **Cabo Verde could add its voice to the group of African countries and advocate for a reform of the GFA, particularly regarding the channelling of investments needed to deliver on global public goods—especially**

climate and pandemic preparedness—as well as on the SDGs. The current system has been unable to mobilise adequate financing for the continent and Cabo Verde in particular. To meet these financing challenges, the world needs a GFA that can support the development of new and innovative financing mechanisms and mobilise resources at scale and affordable cost to fund sustainable development.

- **Climate finance is a major theme for Cabo Verdean policymakers and other African countries to ponder.** Tackling the climate crisis will require significant investment in climate mitigation and adaptation infrastructure across multiple sectors including energy and agriculture and for adaptation for water, health and transport. The country hosts a wealth of

both natural and human capital, with a growing and increasingly educated young labour force. Its enormous renewable energy potential, including wind and solar, makes it an extremely attractive prospect for private investment. Cabo Verde could leverage sustainable climate finance resources and innovative mechanisms (for example, green bonds, blue bonds and sustainability bonds) from MDBs, bilateral donors and DFIs for adaptation projects that are directly linked to development and economic transformation. The country could also tap into the African Green Banks Initiative launched by the African Development Bank and benefit from blended finance instruments for climate financing, technical assistance and green finance facilities (for example, equity and subordinated debt and debt financing).





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