The following item is a Letter of Intent of the government of Cape Verde, which describes the policies that Cape Verde intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Cape Verde, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.
LETTER OF INTENT

November 13, 2009

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
700 19th Street N.W.
Washington DC 20431 USA

Dear Mr. Strauss-Kahn:

1. Discussions for the 7th review of the PSI were held in Praia during September 23–October 1, 2009. The attached Memorandum of Economic and Financial Policies (MEFP) reviews implementation to date of the Cape Verde government’s macroeconomic and structural program as set out in the May 2009 Letter of Intent. It describes economic and policy developments since the sixth review under the PSI and presents the government’s objectives and policy actions for the remainder of the PSI and the medium term.

2. The government of Cape Verde reaffirms its commitment to the policy priorities of the Policy Support Instrument (PSI). The PSI provides firm support for our policies for macroeconomic stability, economic growth, and poverty reduction. The PSI has served the country well and we intend to request a new three-year PSI in early 2010.

3. The government of Cape Verde requests a modification of the program’s assessment criteria for end-2009 for net international reserves, nonconcessional external borrowing, and net domestic borrowing (Table 1). We request to lower the floor on net international reserves, raise the ceiling on nonconcessional external financing, and lower the ceiling on net domestic borrowing. Raising the ceiling on nonconcessional external financing would allow us to obtain an additional budget support loan to bolster our international reserves. This will help us weather the global economic crisis and reduce the interest costs and lengthen the maturity of government debt.

4. Under the PSI, the government will regularly update the IMF on economic and policy developments and will provide the data needed for adequate monitoring of the program. During the period of the PSI, Cape Verde will consult with the IMF on adoption of any measures that may be appropriate at the initiative of the government or whenever the Managing Director of the IMF requests such a consultation. We authorize the IMF to publish this letter of intent, the attached MEFP, and the related staff report.

Sincerely yours,

/s/
Cristina Duarte
Minister of Finance
ATTACHMENT I. MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

RECENT DEVELOPMENTS AND PROGRAM PERFORMANCE

1. **Cape Verde is coming through the global economic crisis well.** Growth has weakened reflecting the slowdown in tourism and foreign direct investment, but it is still projected at about 4 percent in 2009. An expansion of our public investment program is supporting economic activity. There are signs that the growth decline has stopped. Foreign investment has recovered slightly, and construction on several private investment projects have resumed. Twelve month inflation dropped to -1.2 percent in September and is projected at 1 percent by end-2009 reflecting a good harvest, and lower oil and food prices in international markets. International reserves have declined moderately in the first part of 2009.

2. **The government is responding to the global crisis by implementing a fiscal stimulus as agreed during the last PSI review.** We are using the policy space created by our prudent fiscal policy in recent years, the availability of additional external financing, and the excess capacity in the construction sector to accelerate our investment program. We are also increasing social spending to protect the most vulnerable social groups. Although recurrent spending has been reduced, overall spending is projected to increase by 7.4 percent of GDP relative to 2008 and, with expected shortfalls in tax revenues and land sales, the deficit is projected to reach 8.8 percent of GDP in 2009. However, net domestic borrowing, the program’s fiscal anchor, is expected to be less than -0.8 percent of GDP, substantially below the program ceiling agreed during the sixth review under the PSI.

3. **The June 2009 quantitative targets were observed by a solid margin (Table 1).**
   - Domestic borrowing was below the ceiling by 2.6 percent of GDP, thereby further reducing the domestic debt. Our mid-year review of the budget execution conducted in August (a PSI benchmark) found that tax revenues in the first half of 2009 were lower than projected, but so were expenditures.
   - Net international reserves (NIR) were above the floor by €13 million

4. **Despite some delays, all but three structural benchmarks have been met.**
   - The draft income tax codes have been submitted to the Council of Ministers and is expected to be submitted to the National Assembly before the end of the year. We have undertaken an additional round of consultations with the main stakeholders to shore up political support for the tax codes and ensure their passage by the National Assembly.
   - The BCV has prepared a report on developments of balance of payments flows, and an assessment of the interest rate sensitivity of non-resident flows into the banking
The report found that the inflows currently recorded as remittances in the balance of payments were interest rate sensitive, implying that a part of these inflows would not be remittances to support local relatives but for portfolio investment. This is consistent with the exceptionally large stock of emigrant deposits in our banking system (about one third of total deposits) and the belief of our local commercial banks that these deposits are sensitive to external interest rate differentials.

- Financial controllers for each line ministry were appointed on October 14, 2009. The process has taken longer than originally envisaged because of the legal procedures to screen the candidates and nominate the selected.

- A report of contingent liabilities has been prepared and discussed by the Council of Ministers. The Cabinet welcomed the report, asked that the report be continuously updated to closely monitor contingent liabilities, and requested that the updated report be submitted on an annual basis.

- We have also prepared a medium term fiscal framework (MTFF) that was included in the budget write up and attached to the submission of the 2010 budget to the National Assembly. The MTFF documents the implied debt trajectory of the current pace of external borrowing for the investment program. Our associated DSA concluded that while the debt service will rise, it remains manageable.

- We are preparing a memorandum on the modalities for strengthening monetary and fiscal policy coordination, aimed at improving our liquidity management, limit the burden of monetary management on the BCV, and improve our ability to adjust monetary and fiscal policies in the event of external shocks. Finalization of the memorandum has been delayed because of administrative reasons but is expected before end-November.

- Work is well underway to harmonize prudential regulations for onshore and offshore banks, in line with the 2009 FSAP recommendations. We are preparing a new banking law to be submitted for approval for the Council of Ministers to implement our strategy for the sector (¶16).

I. MACROECONOMIC OUTLOOK AND POLICIES FOR 2010 AND THE MEDIUM TERM

5. In 2010 and over the medium term, fiscal policy will remain anchored on preserving international reserves and ensuring debt sustainability, and monetary management will remain focused on keeping external capital flows stable. The PSI’s quantitative assessment criteria for end-2009 and indicative targets for 2010 are set out in Table 1.
A. Macroeconomic Outlook for 2010

6. The outlook for 2010 is positive, helped by the incipient global recovery and strength of our policies.

- **Real GDP growth** is expected to recover moderately in 2010 as ongoing private construction projects are getting back up to full steam and tourism and FDI flows pick up. The pace of our largely externally-financed investment program will also continue to help sustain growth.

- **Inflation** will continue to be low, consistent with the peg to the euro and the high pass-through of international prices in our open economy, and the outlook for a good agriculture harvest following the recent unusually generous rainfall. We forecast CPI inflation to average about 1-2 percent in 2010.

- **International reserves** are expected to remain between 3½–4 months of imports. Imports are expected to slow further due to the weakened external inflows. While the current account deficit will widen, it will be financed by mostly concessional funds secured by the government.

B. Fiscal Policy for 2010 and the Medium Term

7. **Continued fiscal discipline remains key to our macroeconomic program.** Net domestic borrowing in 2010 will continue to be contained to protect international reserves. The 2010 budget authorizes a net domestic borrowing up to a maximum of CVEsc 4.0 billion (2.7 percent of GDP), but the budget includes a number of provisions that we do not expect to execute. Thus, we expect net domestic borrowing in 2010 (the PSI’s fiscal anchor) to be around or less than 1 percent of GDP, consistent with a further reduction in domestic debt and maintaining a solid international reserve coverage. We are committed to maintaining a low level of net domestic borrowing over the medium term.

8. **The rapid implementation of our largely externally financed investment program will continue.** We are now reaping the rewards of our efforts over the last few years to strengthen and streamline our project preparation and appraisal capacity and capacity to mobilize concessional external financing for our investment program. These efforts have resulted in a substantial improvement in our project implementation ratio from below 60 percent earlier in the decade to around 90-95 percent currently. It has also resulted in a large number of projects prepared with our external partners over a number of years that are now ready for implementation. The pace of our investment program is expected to continue in 2011–12, but should return to more moderate levels after the completion of the current large infrastructure projects.
The investment program is aimed at supporting long-term private sector-led growth based on services exports in line with the Cape Verde Poverty Reduction and Growth Strategy. It addresses critical infrastructure bottlenecks in roads, airports, sea ports, and electricity and water supply. We are also investing in social housing to reduce illegal construction activities and address social challenges arising from increasing inter-island labor movements associated with the uneven employment opportunities, thereby further improving inter-island mobility and the flexibility of our domestic labor market. We are also investing in new sea vessels to patrol our waters and carry out our commitment to the international community to combat drug smuggling and human trafficking through our waters. Project appraisals carefully prepared with the help of our development partners confirm that the economic and social return from these projects should be high. Absorptive capacity is not expected to be a major constraint because of continued high unemployment (around 18 percent), the high import content of most projects, and the use of donor country contractors that will supply equipment, material, and some personnel. Implementation capacity has also been strengthened through improvements in our procurement system.

Consistent with the above, for 2010 we expect an overall fiscal deficit of around 10 percent. External borrowing in 2010 is budgeted at 12.2 percent of GDP, up from 9.4 percent of GDP in 2009, but because of normal implementation delays it will likely be around 11 percent of GDP. A part of our external borrowing (2.9 percent of GDP) will be on-lent to Enapor, a state owned company that operates the ports, to help them to obtain financing at more favorable terms for their infrastructure investments. Enapor is a profitable and financially sound company with a proven track-record of servicing their debt to the government. Thus, this amount in our fiscal accounts is recorded below the line as negative domestic financing consistent with the accounting practice and the 2001 IMF Government Finance Statistics Manual.

The Government of Cape Verde remains firmly committed to keeping the risk of debt distress low. The window for highly concessional financing will likely be reduced as our income level rises. Our borrowing strategy is designed with that in mind. We have taken measures to improve our debt management capacity and our capacity to conduct debt sustainability analyses (DSA), including through technical assistance from the World Bank and the Fund, and have reinforced the staffing of our Debt Management Unit. Going forward, we will use the DSA framework to ensure that the fiscal stance and the external borrowing embedded in the MTFF remains sustainable. We will present an updated MTFF for the period 2011–13 in the budget write-up for the 2011 budget. The DSA will show the projected debt trajectory and assess debt sustainability.

To ensure continued low risk of debt distress, external borrowing will continue to be mostly on concessional terms, and scaled back to past trend after the completion of the current large infrastructure projects. Our debt portfolio is mainly on long term and highly concessional, implying a low risk profile. We will maintain debt service-to-revenues at a manageable level. In that regard, we will accelerate our efforts to enhance revenue
collection and broaden the tax base to keep the debt service-to-revenue ratio low, including through a rationalization of tax exemptions. Fast implementation of the broad range of tax legislation prepared with IMF assistance and submitted to the National Assembly will be instrumental to achieve this. Expanding revenue collection while ensuring international attractiveness for businesses is critical for our development.

13. The government will continue to take action to address contingent liabilities arising from state-owned enterprises (SOEs). The Council of Ministers decided to take a bold action to put both the electricity company Electra and the airline TACV on a viable restructuring plan. Electra’s finances should recover as the new investments are completed and a consolidated TACV is being prepared to be delivered to private partners as soon as global conditions permit. While TACV has balance sheet weaknesses, it is a functioning airline with unrecorded market value. In particular, TACV is nearing International Air Transportation Association (IATA) membership that will allow it to partner with other IATA members and further raise its market value. The first step in this process has been achieved in early 2009, when, for the first time ever, TACV was registered as an IOSA Operator, under the IATA Operational Safety Audit (IOSA) program, after meeting the world aviation’s leading quality and safety standards. The government will continue to monitor state-owned enterprises and update the risk assessment continuously. To reinforce the control, the Council of Ministers has approved the Law of State Enterprises and a Public Managers Law will be approved by end of 2009. The approval and implementation of these reforms will create a new model for parastatals management based on performance and permit better control and monitoring of the sector, by establishing a set of rules and procedures which will serve as a framework for the regulation of sector, permitting a restructuring of the public enterprises in order to become an instrument for economic policies. Moreover, they will allow a change of paradigm in the management of the parastatals, to become result/objective oriented

C. Monetary Management and Financial Sector Issues

14. Consistent with the peg and largely open capital account, the BCV policy rate will continue to follow the euribor adjusted for the country risk premium to preserve the stability of external capital flows. The liquidity crunch in Europe, an increased risk premium for peripheral economies, and the loss of reserves forced the BCV to raise the rate in October 2008 and hold it steady at 5¼ percent since. This rise helped stem the reserve loss in mid-2008 when the euribor spiked. As the global crisis recedes, risk premium narrows, and reserves firms, the BCV could have room to gradually lower the interest rate spread. The BCV will continue to monitor closely capital flows to adjust the policy rate to prevent potentially destabilizing capital flows from occurring.

15. We are exploring how to improve monetary transmission mechanism, and in particular the functioning of the government security market, to ensure that the BCV’s policy rate is appropriately influencing market interest rates. A critical issue is how to
address the market distortions created by the existence of one large institutional investor with low price sensitivity that is hampering price discovery. As a first step, we intend to regularize public security issuance arrangements by (i) improving the predictability and regularity of issuance, (ii) start issuing benchmark series that would facilitate secondary market activity; (iii) encouraging active bidding by all participants, and (iv) clearly signaling a willingness to accept market outcomes. We are also considering the advantages of using treasury bills to mop up structural excess liquidity.

16. **The government is revisiting its strategy regarding the offshore sector.** In this regard, the ongoing overhaul of banking regulation will harmonize prudential norms for onshore and offshore banks. This law would also give more timely enforcement tools to the central bank to end forbearance in line with the 2009 FSAP’s recommendations.

II. POVERTY REDUCTION STRATEGY AND THE NEXT PSI

17. **We consider that the PSI has served the country well, helping to support growth and reduce poverty, and intend to request a new three-year PSI program in early 2010.** We are conducting an internal ex post assessment of the current PSI. Our preliminary conclusion is that the PSI program has helped to improve economic performance and leverage the government reform program, serving as a facilitator to introduce structural reforms. It has also a catalytic role for donor support and strengthens the credibility of the government policies. During the PSI, Cape Verde was invited to join the WTO, graduated from LDC status and was accepted as a special partner of the EU. As a facilitator of reforms, the PSI is helping to advance the objectives of our Poverty Reduction and Growth Strategy. Cape Verde is on track to achieve most of the MDGs by 2015, including halving the 1990 poverty level.

18. **On the other hand, it was with great dissatisfaction that the government received the news that countries must now participate on the financing of technical assistance missions.** We believe that that was one of the key strengths of the PSI program. As you know, there are no financial commitment under the program, thus we believe that countries under a program should benefit of the Fund’s knowledge resources, especially when they are linked to structural benchmarks established under the program. In the case of Cape Verde, taking into account its vulnerabilities, we believe that without the Fund’s support the rate of implementation and success of the program would be limited. Thus, we request the IMF to reconsider its decision or design a better way to channel technical assistance where is needed with the lowest burden possible for the countries. We should not jeopardize the successful milestone that together we have reached, especially given the present global environment.
Table 1. Cape Verde: Quantitative Assessment Criteria and Indicative Targets for 2009-10 under the PSI

<table>
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<tr>
<th>Stock with adjusters</th>
<th>Cumulative Flows from End-Dec, 2008</th>
<th>Cumulative Flows from End-Dec, 2009</th>
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<td>Indicative Targets</td>
<td>Assessment Criteria</td>
<td>Assessment Criteria with adjusters</td>
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<td><strong>Quantitative targets</strong></td>
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<td>Ceiling on net domestic borrowing of the central government 2</td>
<td>...</td>
<td>-0.1</td>
</tr>
<tr>
<td>Ceiling on net domestic assets of the central bank 4</td>
<td>-3.8 11</td>
<td>-0.9</td>
</tr>
<tr>
<td>Ceiling on the accumulation of new domestic payment arrears by the central government</td>
<td>...</td>
<td>0.0</td>
</tr>
<tr>
<td>Ceiling on the accumulation of new external payment arrears by the central government 5</td>
<td>...</td>
<td>0.0</td>
</tr>
<tr>
<td>Ceiling on the contracting or guaranteeing of non-concessional external debt with original maturity of more than one year by the central government 6</td>
<td>...</td>
<td>8.8</td>
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<tr>
<td>Ceiling on the outstanding stock of nonconcessional external debt with a maturity of less than one year by the central government 7</td>
<td>...</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Floor on net international reserves of the Bank of Cape Verde (BCV)</strong> 8</td>
<td>270.9 11</td>
<td>13.1</td>
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<tr>
<td><strong>Floor on the regulatory capital ratio of individual banks</strong> 9</td>
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<td>Program assumptions</td>
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<tr>
<td>Nonproject external financial assistance, including credit line (program assumption)</td>
<td>...</td>
<td>0.8</td>
</tr>
<tr>
<td>External debt service</td>
<td>...</td>
<td>0.5</td>
</tr>
<tr>
<td>Land sales</td>
<td>...</td>
<td>0.4</td>
</tr>
<tr>
<td>Clearance of end-2006 stock of domestic arrears</td>
<td>...</td>
<td>0.6</td>
</tr>
</tbody>
</table>

1 Quantitative assessment criteria and benchmarks are described in the technical memorandum of understanding.
2 For purposes of calculating program adjusters, foreign currency amounts will be converted at current exchange rates.
3 Excluding borrowing for clearance of arrears and net late payments. The ceiling will be adjusted upward by the cumulative upward deviation in external debt service, and by the cumulative downward deviation in nonproject external financial assistance and land sales relative to program assumptions. The ceiling will be adjusted downward by the cumulative downward deviation in external debt service and by the cumulative upward deviation in land sales relative to program assumptions. The ceiling will be adjusted upward by the costs of restructuring state-owned enterprises up to a limit of CVE 1.5 billion.
4 The ceiling will be adjusted upward by the cumulative upward deviation in external debt service and by the cumulative downward deviation in nonproject external financial assistance relative to program assumptions. The ceiling will be adjusted downward by the cumulative downward deviation in external debt service relative to program assumptions. The ceiling will be adjusted upward by the costs of restructuring state-owned enterprises up to a limit of CVE 1.5 billion.
5 This assessment criterion is on a continuous basis.
6 This assessment criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), August 24, 2000), but also commitments contracted or guaranteed for which value has not been received. Excluded from this performance criterion are rescheduling arrangements, the Portuguese credit line, and borrowings from the Fund.
7 The term “debt” has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt. Excluded from this performance criterion are rescheduling arrangements, the Portuguese credit line, borrowings from the Fund, and normal import-related credits.
8 The floor on net international reserves of the Bank of Cape Verde will be adjusted downward by the cumulative upward deviation in external debt service, by the cumulative downward deviation in nonproject external financial assistance relative to program assumptions, and by the costs of restructuring state-owned enterprises up to a limit of 13.5 million euros. The floor will be adjusted upward by the cumulative downward deviation in external debt service relative to program assumptions. Additionally, in the case Cape Verde participates in any SDR allocation(s) between June 30, 2009 and the test date, the floor on net international reserves will be adjusted upwards by the equivalent of the amount of the cumulative additional SDR allocation(s) up to the test date measured at program exchange rates.
9 The floor on banks’ regulatory capital ratios is an indicative floor for all test dates. This indicative target is continuous.
10 Does not include the positive flow caused by the allocation of € 9.3 million SDRs to Cape Verde.
11 Differs from IMF Country Report 09/198 because of a small upward revision of net international reserves by the Bank of Cape Verde.
<table>
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<th>Structural Benchmark</th>
<th>Timing</th>
<th>Status</th>
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<tbody>
<tr>
<td></td>
<td>Reset to be implemented in June 2009.</td>
<td></td>
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</tr>
<tr>
<td>Promote financial stability</td>
<td>Prepare a quarterly report on developments on balance of payments flows, including an assessment of interest sensitivity of non-resident flows into the banking system.</td>
<td>End-Dec. 2008.</td>
<td>Met with delay.</td>
</tr>
<tr>
<td></td>
<td>Reset to be implemented in June 2009.</td>
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<tr>
<td></td>
<td>Reset to be implemented in June 2009.</td>
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<tr>
<td>Strengthen debt management</td>
<td>Submit to the Council of Ministers a report on contingent liabilities of the state assessing potential risks based on the 2007 or more recent data, including those risks arising from state-owned enterprises.</td>
<td>End-Mar. 2009.</td>
<td>Met with delay.</td>
</tr>
<tr>
<td></td>
<td>Reset to be implemented in June 2009.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strengthen debt management</td>
<td>Conduct a mid-year review of fiscal performance, including projections for end 2009, justifying that the envisaged borrowing is consistent with debt sustainability.</td>
<td>End-August 2009.</td>
<td>Met.</td>
</tr>
<tr>
<td>Strengthen debt management</td>
<td>Include a medium-term fiscal framework (MTFF) for 2010-2012 in the 2010 budget’s write up (“Enquadramento”) describing the implied debt trajectory and justifying that the envisaged borrowing is consistent with debt sustainability.</td>
<td>End-October 2009.</td>
<td>Met.</td>
</tr>
<tr>
<td>Strengthen fiscal-monetary policy coordination</td>
<td>BCV to prepare a short memorandum on strengthening monetary-fiscal policy coordination in managing liquidity to be discussed by PSI Monitoring Committee and endorsed by Ministry of Finance and BCV.</td>
<td>End-August 2009.</td>
<td>Not met.</td>
</tr>
<tr>
<td>Strengthen the financial sector</td>
<td>Inform the Fund of measures taken in the event that the capital ratio of one (or more) banks falls below 10 percent.</td>
<td>Continuous effective June 2009.</td>
<td>Met.</td>
</tr>
</tbody>
</table>

1 Measures outstanding at the time of the 7th PSI review.
1. This memorandum sets out the understandings between the Cape Verdean authorities and the IMF staff regarding the definition of assessment criteria and indicative targets and reporting requirements for the seventh and eighth reviews under the Policy Support Instrument.

I. QUANTITATIVE ASSESSMENT CRITERIA AND INDICATIVE TARGETS

A. Net Domestic Borrowing Excluding for Clearance of Arrears and Net Late Payments

2. **Net domestic borrowing excluding for clearance of arrears and net late payments** is defined as the cumulative change since the start of the calendar year of the net credit to the central government from the banking and nonbanking sectors less (1) the cumulative clearance during the calendar year of the stock of arrears as of the end of the previous year and (2) the cumulative payments during the first three months of the calendar year of expenses authorized by the previous year’s budget, plus the expenses accrued during the current year that will be paid during the first three months of the next calendar year as provisioned for in the budget law (late payments or *atrasados*).

- The ceiling will be adjusted upward by
  - the cumulative upward deviations in external debt service, by
  - the cumulative downward deviations in nonproject external financial assistance and land sales relative to program assumptions, and by the costs of restructuring state-owned enterprises up to a limit of CVE 1.5 billion.

- The ceiling will be adjusted downward by
  - the cumulative downward deviation in external debt service and by
  - the cumulative upward deviation in land sales relative to program assumptions.

3. **Net credit to the central government from the banking and nonbanking system** is defined as the overall position of the main central government institutions vis-à-vis the banking and nonbanking system—that is, the stock of all outstanding claims on the central government (loans, advances), and all other government debt instruments, such as long-term government securities, held by the BCV, commercial banks, and nonbank institutions, less all deposits held by the central government with the BCV and with commercial banks. The INPS is not included in central government accounts. Net credit to the central government excludes claims on the Trust Fund (TCMFs).

4. **Reporting requirements.** Data on the implementation of the budget compiled by the Ministry of Finance and Public Administration will be provided on a quarterly basis, to be
submitted no later than five weeks after the end of each quarter, including (i) government domestic revenue by category; (ii) external budget support grants; (iii) government expenditure, including primary current expenditure, domestic and external interest payments, and capital expenditure, including domestically and budget support financed capital expenditure and estimates of externally project financed capital expenditure; (iv) the gross payment and gross accumulation of domestic accounts payable \((atrasados)\); (v) the gross payment and gross accumulation of domestic payments arrears; (vi) external loan receipts and principal payments; (vii) external arrears payments and accumulation; (viii) bank and nonbank financing; (ix) privatization and land sale receipts; and (x) any other revenue, expenditure, or financing not included above.

5. For the purposes of this memorandum, privatization and land proceeds will be understood to mean all monies received by the government from the sale or concessioning of a public company, organization, or facility to a private company or companies, organization(s), or individual(s), as well as any proceeds generated from the sale of government land and the liquidation of a public company, less restructuring costs.

B. Net Domestic Assets of the Central Bank

6. The ceiling on the cumulative change, from the beginning of calendar-year 2009, in net domestic assets of the BCV constitutes an assessment criterion. **Net domestic assets (NDA) of the BCV** are defined as reserve money minus net foreign assets of the BCV, evaluated at the current end-of-period exchange rates.

- The program ceilings for NDA will be adjusted upward by
  - the cumulative upward deviations in external debt service, by
  - the cumulative downward deviations in nonproject external financial assistance relative to program assumptions, and by the costs of restructuring state-owned enterprises up to a limit of CVE 1.5 billion.
- The ceiling will be adjusted downward by the cumulative downward deviation in external debt service relative to program assumptions.

For purposes of calculating the adjusters, these flows will be valued at current exchange rates. Reserve money comprises bank reserves and deposits of the monetary institutions and private sector with the central bank, as well as cash in circulation.

7. **Reporting requirements.** The preliminary monthly balance sheets of the BCV and the consolidated commercial banks will be transmitted on a monthly basis, with a maximum delay of five weeks. The definitive version of the monthly balance sheet of the BCV will be provided as soon as available.
C. Ceiling on Nonconcessional External Debt Contracted or Guaranteed by the Central Government

8. Under the program, ceilings on medium- and long-term, as well as on short-term, nonconcessional external debt constitute assessment criteria. The ceiling on medium- and long-term nonconcessional external debt is on a quarterly basis while the one on short-term nonconcessional external debt is on a continuous basis. Nonconcessional external debt is defined as debt contracted or guaranteed by the central government with a grant element of less than 35 percent, calculated using currency-specific commercial interest reference rates (CIRRs) published by the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD). Debt rescheduling and debt reorganization are excluded from the limits on nonconcessional external debt. The limits on new nonconcessional external debt contracted or guaranteed by the central government (excluding borrowing from the Fund) are specified in Table 1 of the Letter of Intent. The definition of short-term nonconcessional external debt excludes normal short-term (less than one year) import-related financing. The Portuguese government’s precautionary credit line in support of the exchange rate peg is also excluded from the definition of nonconcessional external debt. The assessment criterion on medium- and long-term nonconcessional external indebtedness applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), 8/24/00) but also to commitments contracted or guaranteed for which value has not been received. With respect to the assessment criterion on short-term nonconcessional external indebtedness, the term “debt” has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), 8/24/00).

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

D. Net International Reserves of the Central Bank

10. The floor on the cumulative change, from the beginning of calendar-year 2009, in net international reserves (NIR) of the BCV constitutes an assessment criterion under the program. The NIR of the BCV are defined as gross international reserves of the BCV net of its external reserve liabilities, calculated at the current exchange rates. Gross reserves of the BCV are those that are readily available (i.e., liquid and marketable and free of any pledges or encumbrances), controlled by the BCV and held for the purposes of meeting balance of payments needs and intervening in foreign exchange markets. They include gold, holdings of SDRs, the reserve position at the IMF, holdings of foreign exchange and traveler’s checks, demand and short-term deposits at foreign banks abroad, fixed-term deposits abroad that can be liquidated without penalty, and any holdings of investment-grade securities. External
liabilities of the BCV comprise liabilities to nonresidents contracted by the BCV with an original maturity of less than a year, any net off-balance-sheet position of the BCV (futures, forwards, swaps, or options) with either residents and nonresidents, any arrears on principal and interest to external creditors and suppliers, and purchases from the IMF.

- The program floors for the NIR will be adjusted downward by
  - the cumulative upward deviations in external debt service, by
  - the cumulative downward deviations in nonproject external financial assistance relative to program assumptions, and by the costs of restructuring state owned enterprises up to a limit of € 13.6 million. For purposes of calculating the adjusters, these flows will be valued at current exchange rates.

- The floor will be adjusted upward by the cumulative downward deviation in external debt service relative to program assumptions. Additionally, in the case Cape Verde participates in any SDR allocation(s) between June 30, 2009 and the test date, this floor will be adjusted upwards by the equivalent of the amount of the cumulative additional SDR allocation(s) up to the test date measured at program exchange rates.

11. **Reporting requirements.** A table on the NIR prepared by the BCV will be transmitted on weekly basis, with a maximum delay of two weeks.

**E. Nonaccumulation of New Domestic Payments Arrears**

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

13. **Reporting requirements.** The Ministry of Finance and Public Administration, through the D.G.T., will submit on a quarterly basis a detailed table of the stock of domestic payments arrears, including the accumulation, payment, rescheduling and write-off of domestic payments arrears during the quarter. The data are to be provided within four weeks after the end of the quarter.
F. Nonaccumulation of External Payments Arrears

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

15. External arrears are defined as total external debt-service obligations of the government that have not been paid by the time they are due, except where agreements between the government and creditors explicitly provide for a grace period after such obligations falling due. External arrears exclude arrears on external debt, pending the conclusion of debt-rescheduling agreements.

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

II. Other Data Requirements

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

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

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

20. The table of Financial Soundness Indicators and the regulatory capital ratios of individual banks will be transmitted to the IMF on a monthly basis within six weeks after the end of each month. The nomination of individual banks is optional.