

Nicaragua: Seventh Review Under the Extended Credit Facility and Financing Assurances Review—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Nicaragua.

In the context of the seventh review under the Extended Credit Facility and Financing Assurances Review, the following documents have been released and are included in this package:

- The staff report for the Seventh Review Under the Extended Credit Facility and Financing Assurances Review, prepared by a staff team of the IMF, following discussions that ended on September 9, 2011, with the officials of Nicaragua on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on October 6, 2011. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A Press Release summarizing the views of the Executive Board as expressed during its October 21, 2011 discussion of the staff report that completed the request and/or review.
- A statement by the Executive Director for Nicaragua.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Nicaragua*
Technical Memorandum of Understanding*
Poverty Reduction Strategy Paper

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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NICARAGUA

Seventh Review Under the Extended Credit Facility and Financing Assurances Review

Prepared by the Western Hemisphere Department
(In consultation with other departments)

Approved by Miguel A. Savastano (WHD) and Dhaneshwar Ghura (SPR)

October 6, 2011

EXECUTIVE SUMMARY

Background. A three-year PRGF (now ECF) arrangement for SDR 71.5 million (55 percent of quota) was approved on October 5, 2007 and augmented by SDR 6.5 million (5 percent of quota) on September 11, 2008. The second and third reviews under the ECF arrangement were completed in November 2009. On November 19, 2010, the Board completed the fourth and fifth reviews of the ECF and approved an extension of the arrangement through December 4, 2011. The extension entailed a re-phasing of remaining access under the ECF. The 6th review was completed in April 2011 on a lapse-of-time basis. The staff report on the 2010 Article IV consultation was discussed by the Executive Board on July 9, 2010.

Recent developments and outlook. The Nicaraguan economy continued to post robust growth in the first half of 2011, although economic activity and inflation are expected to cool down going forward owing to the weaker global outlook. The deficit in the external current account is projected to remain large and to be financed by resilient capital flows. Strong revenue performance and expenditure restraint are projected to nearly eliminate the central government deficit in 2011, but the operating results of public enterprises will be worse than expected.

Main review issues. All quantitative performance criteria for end-June 2011 were met and the structural agenda is broadly on track. Discussions centered on the macroeconomic outlook and policies for 2011-2012, and on key structural issues, including restoring the electricity sector's financial sustainability, reforming social security, and enhancing the effectiveness of poverty alleviation measures. Staff urged officials to keep current spending in check in the remainder of 2011.

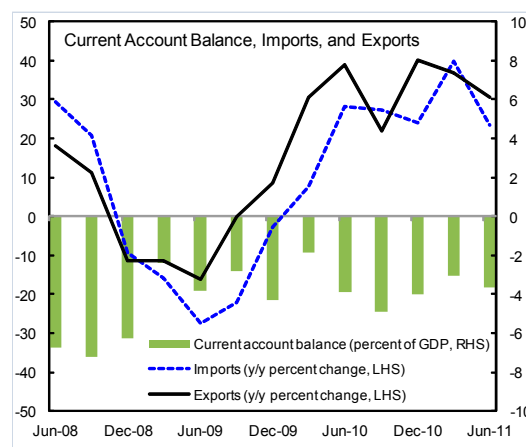
Discussions. A team comprising Messrs. M. Estevão (head), I. Samake, A. Brousseau (all WHD), and R. Fenochietto (FAD), and Ms. J. Bersch (SPR) visited Managua during August 30–September 9. The team was assisted by Mr. G. Di Bella (Resident Representative). Staff met with Central Bank President Rosales, Finance Minister Guevara, Presidential Adviser Arce, other senior officials, and representatives of the legislature, private sector and the donor community.

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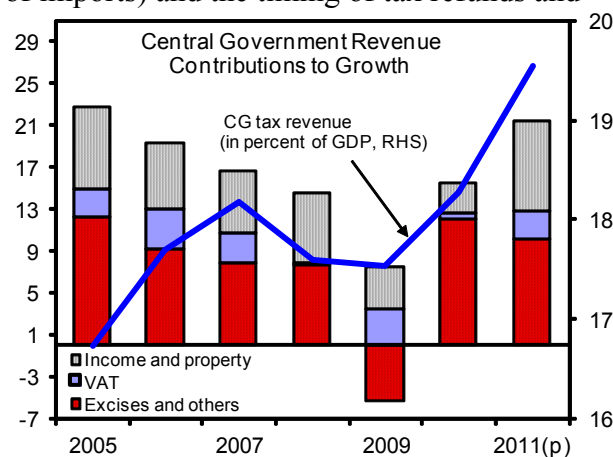
I. ECONOMIC DEVELOPMENTS SINCE THE SIXTH PROGRAM REVIEW¹

1. **Output growth remained strong through June and inflationary pressures were contained.** As in 2010, private consumption and investment were the key growth drivers on the demand side, while construction and manufacturing performed strongly on the supply side. In light of this outturn, the growth projection for 2011 was revised upward to 4 percent. Headline inflation was 9 percent by mid year (broadly unchanged from end-2010) and is expected to decline to 8 percent by the end of 2011, as world commodity prices ease. The rate of exchange-rate crawl remains unchanged at 5 percent a year.

2. **The balance of payments position did not deteriorate.** Export and import growth remained strong in the first semester and remittances increased almost 10 percent in nominal terms. On net, the external current account deficit through June 2011 was slightly larger than in 2010—broadly in line with projections. Capital inflows, however, were stronger than projected, including because of higher FDI and capital transfers, and gross international reserves barely declined during January-June (compared to a projected loss of US\$70 million).



3. **The fiscal performance of the central government was stronger than envisaged.** The pickup of economic activity (especially of imports) and the timing of tax refunds and withholding boosted central government revenues above program projections in the first half of 2011 by nearly 1 percent of GDP (after accounting for the effects of the end-2009 tax reform, Box 1). Added to expenditure restraint, which kept total spending about 0.2 percent of GDP below projections, the central government's overall deficit (before grants) was lower than projected by about 1 percent of GDP. The rest of the public sector performed broadly as programmed, with higher-than-projected expenditures by the Social Security Institute offset by capital gains.



¹ Completed on April 27, 2011 (EBS/11/56).

Box 1. Nicaragua: The 2009 Tax Reform

In late 2009, Congress approved a tax reform comprising:

- (1) the introduction of a minimum corporate income tax of 1 percent on gross receipts;
- (2) the elimination of several exemptions on excise taxes;
- (3) an increase in the withholding rate on agricultural market transactions;
- (4) an increase in the standard personal income tax deduction (from C\$50,000 to C\$75,000); and
- (5) the introduction of a 10-percent withholding on dividends and interest.

The reform has produced significant additional fiscal revenues. Staff estimates suggest that these measures increased tax revenues by 1.14-percent of GDP by the end of 2011. About one half of these extra revenues would come from income taxes.

Further progress in eliminating tax exemptions and improving tax administration is nonetheless necessary. The Nicaraguan tax system continues to have numerous tax exemptions and loopholes, particularly on VAT (e.g., on food, clothes, medicines, and oil and its derivatives) and corporate income taxes.

These remaining exemptions and other concessions have limited the broadening of the tax base.

Nicaragua: Impact of tax reform (Percent of GDP)	
Income tax	
Personal	0.08
Corporate	0.49
Excise taxes	0.46
Other	0.11
Total tax reform	1.14

4. **Monetary policy accommodated the increase in net international reserves while keeping net domestic assets on target.** Constrained by the economy's high degree of dollarization, monetary policy continued to aim at protecting the international reserves position, while providing a nominal anchor to the economy. The stronger-than-expected fiscal outturn together with a pickup in currency demand contributed to higher-than-programmed net international reserves, which allowed the Central Bank to reduce its short-term debt.

5. **Banks' balance sheets strengthened as of end June, but credit growth remained subdued.** Nonperforming loans (excluding restructured and reprogrammed loans) stood at about 3 percent of total (gross) loans, banks' profitability continued to improve, and deposits (in local and foreign currency) rose again, fueled by foreign-aid flows. Credit to the private sector, however, increased modestly in the first half of the year, as demand from consumers and agricultural producers was weak, while banks' liquidity remained ample. Deposit and lending rates continued to decline.

Nicaragua: Selected Financial Indicators, June 2009–June 2011					
	Jun-09	Dec-09	Jun-10	Dec-10	Jun-11
Banks' liquidity coverage					
Liquidity coverage	31.6	37.9	40.3	36.4	36.8
Required coverage	20.2	21.6	20.0	19.6	19.3
Banks' deposits					
In foreign currency ^{1/}	68.9	72.8	73.6	73.3	73.5
Cumulative increase ^{2/}	5.9	15.2	18.1	21.6	12.7
Of which : foreign currency	7.4	22.2	19.2	22.3	13.0
Credit to the private sector ^{3/}	-6.2	-7.8	-3.0	5.9	1.4
NPLs	3.0	3.3	3.5	3.0	2.9
Source: Central Bank of Nicaragua.					
^{1/} Percent of total deposits.					
^{2/} By end of period, in percent.					
^{3/} Cumulative increase (since January 2011).					

6. **Program performance was satisfactory.** All quantitative performance criteria (QPCs) for end-June 2011 were met (Table 1). On the structural agenda, the Assembly approved legislation regulating microfinance institutions in June (structural benchmark for end-July) and the study on employment practices in the public sector (structural benchmark for end-September) is underway and is expected to be finalized before December.

II. OUTLOOK

7. **Near-term global prospects are less favorable and more uncertain than envisaged during the sixth review.** Since the completion of the sixth review in late April, growth prospects for the United States and other key trading partners have weakened considerably, while world food and fuel prices have remained high. Moreover, fiscal pressures on European countries have increased uncertainty about future aid flows.

8. **A new government is scheduled to take office in January 2012.** Presidential elections are scheduled to take place on November 6 and a second round of voting (if needed) would be completed before the end of the year. International observers have been allowed to monitor the elections. President Ortega continues to be ahead in the latest opinion polls.

9. **Against this backdrop, staff revised the macroeconomic framework for 2011-12.**

Real GDP growth is now projected to moderate to 3¼ percent in 2012, with risks about balanced around this figure.

Inflation is expected to decline

below 8 percent, as second-

round effects from high world

commodity prices peter out.

However, the external current

account deficit is projected to

increase to 18½ percent of

GDP in 2012 (from 15¾

percent in 2011) because of a

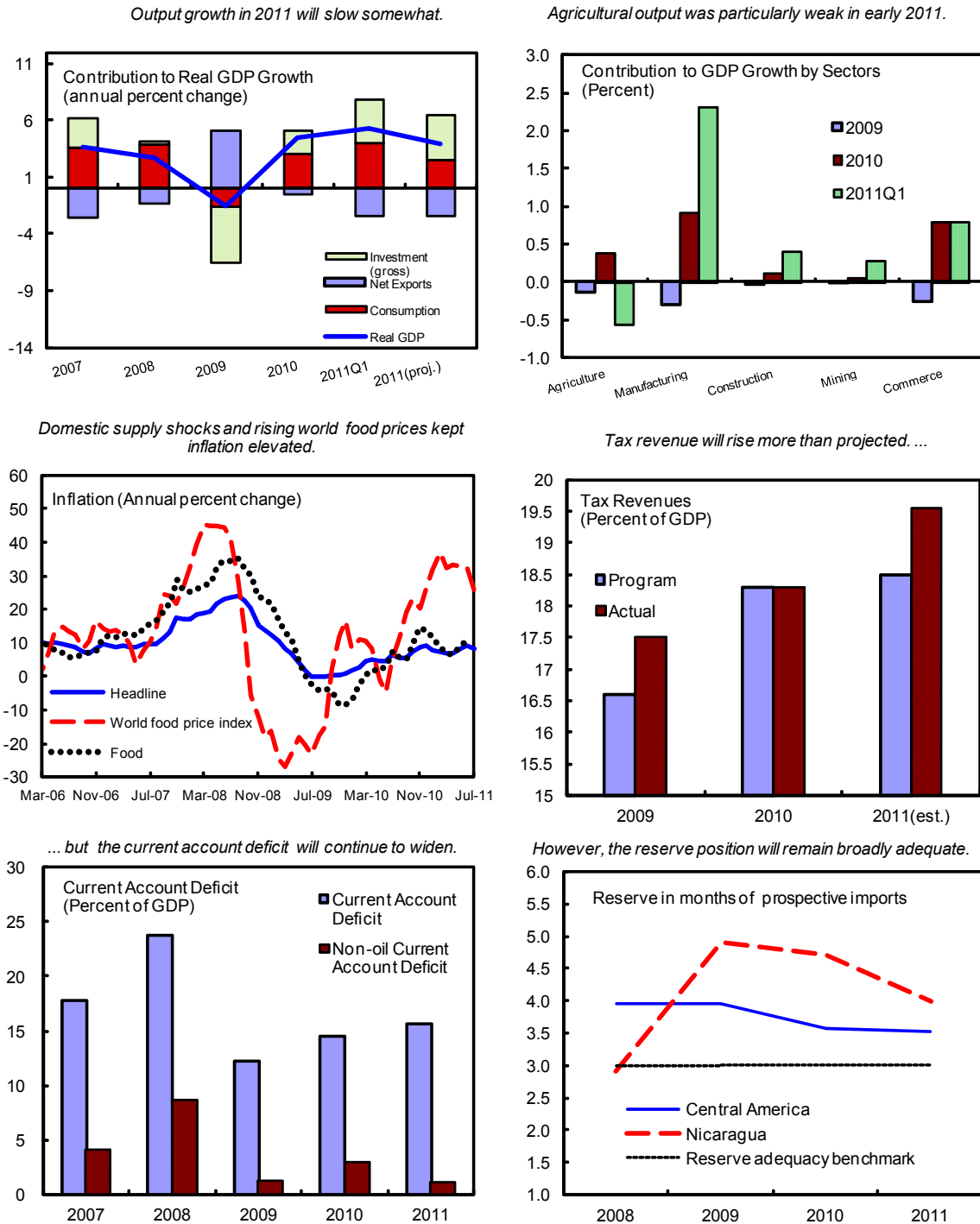
moderation in export growth and still-high oil prices. International reserves are projected to remain broadly stable in 2012 (assuming that net capital inflows are US\$20 million higher than currently projected).²

Nicaragua: Key Economic Indicators, 2009–12					
	2009	2010	2011		2012
			6 th Rev. Prog. ^{1/}	Rev. Proj.	Proj.
Real GDP growth (percent)	-1.5	4.5	3.5–4.0	4.0	3.3
Inflation (end of period, in percent)	0.9	9.2	8.5–9.5	8.0	7.5
Current account deficit ^{2/}	-13.4	-14.8	-17.8	-15.7	-18.4
Gross reserves (US\$ million) ^{3/}	1,573	1,799	1,743	1,818	1,811

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).
^{2/}Percent of GDP.
^{3/}Includes the SDR allocation for SDR 105.1 million (US\$165 million) of September 2009.

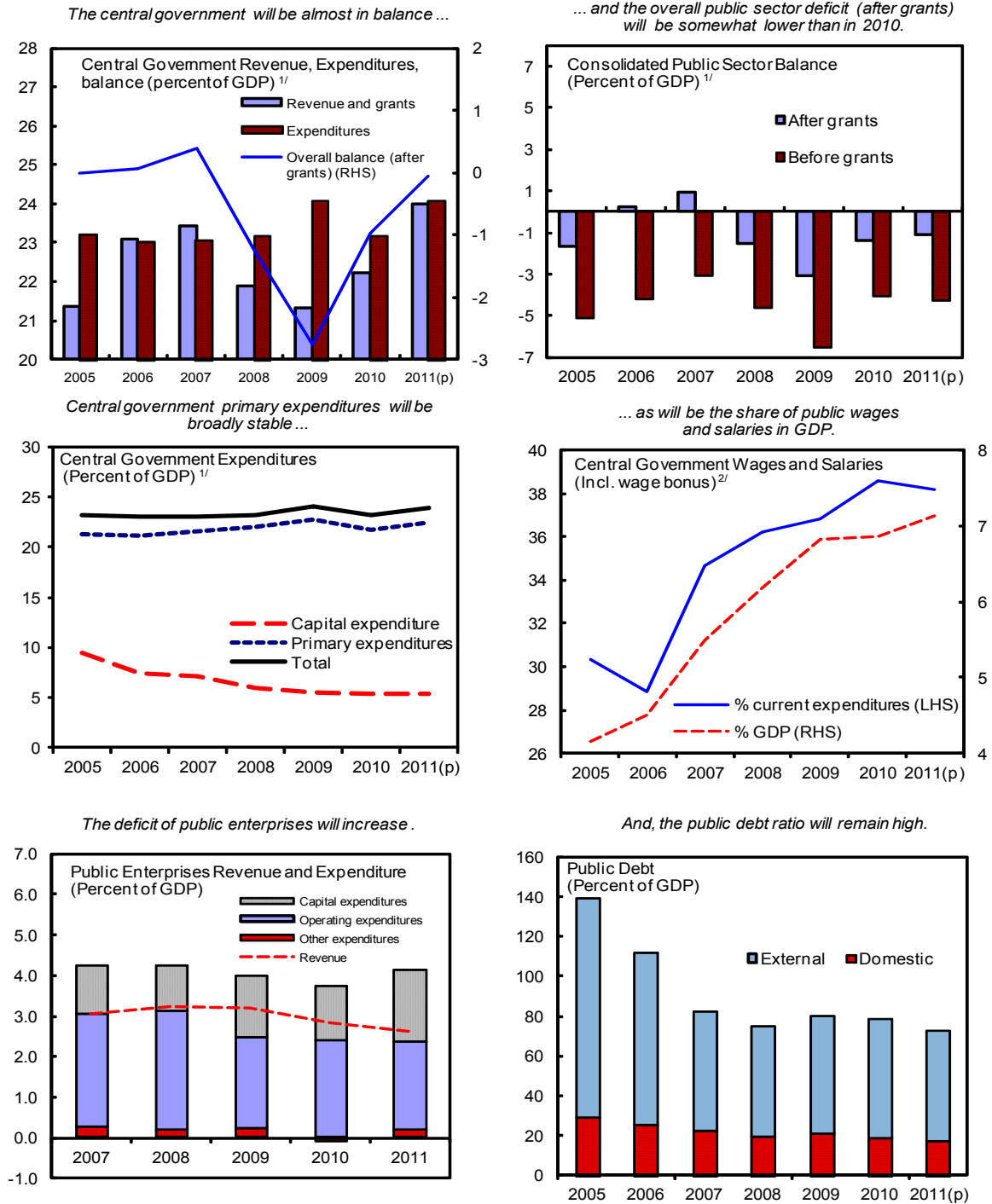
² The balance of payments projections in Table 7 show a “financing gap” of US\$65 million for 2012. Officials believe that US\$45 million of this gap would be covered by a budget-support loan from the Inter-American Development Bank.

Figure 1. Nicaragua: Recent Economic Developments



Source: Nicaraguan authorities; and Fund staff calculations.

Figure 2. Nicaragua: Selected Fiscal Indicators, 2005–11

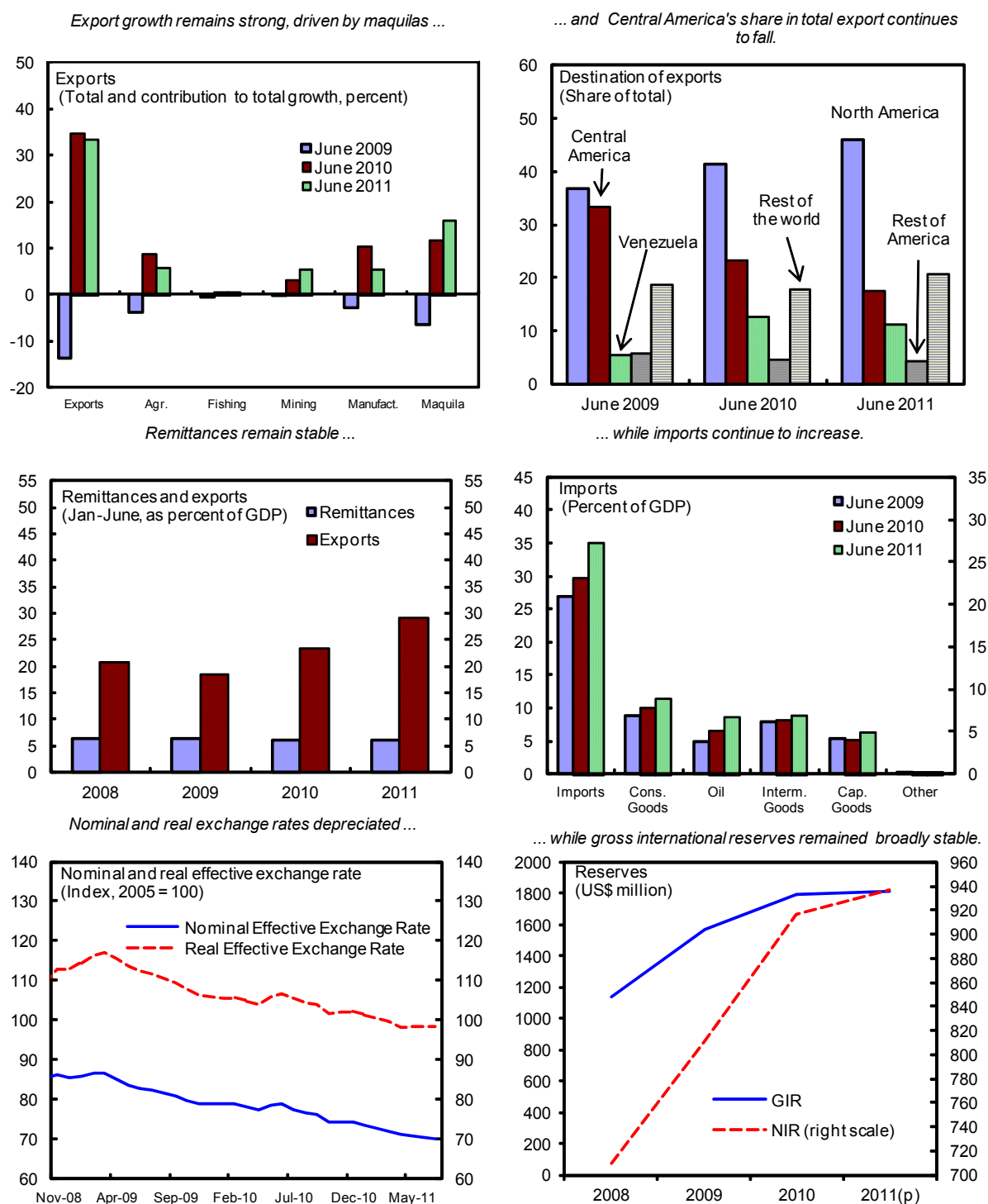


Source: Nicaraguan Authorities; and Fund staff calculations.

1/ Includes the 2010-11 wage bonus.

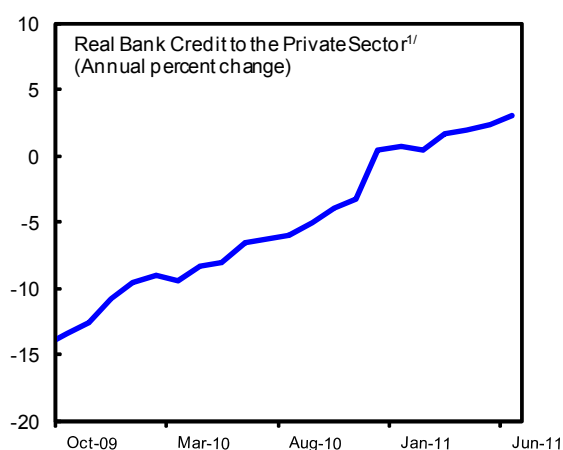
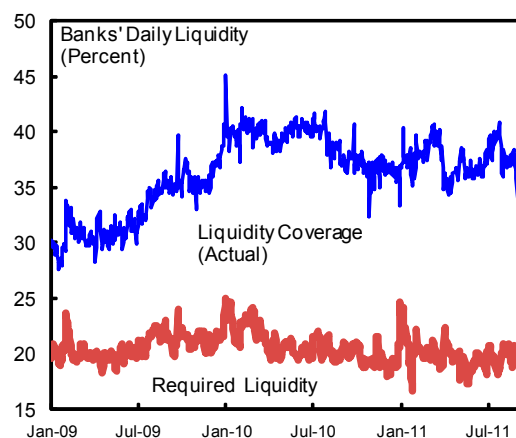
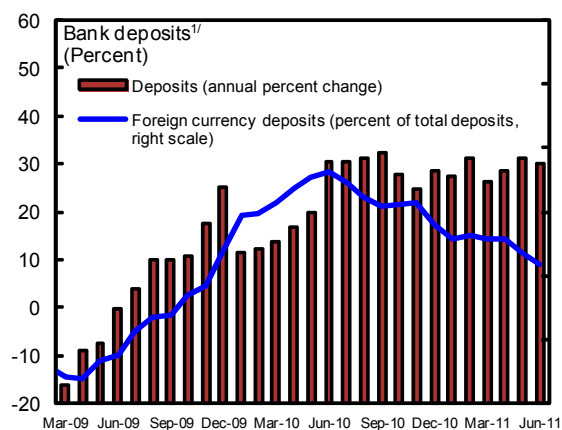
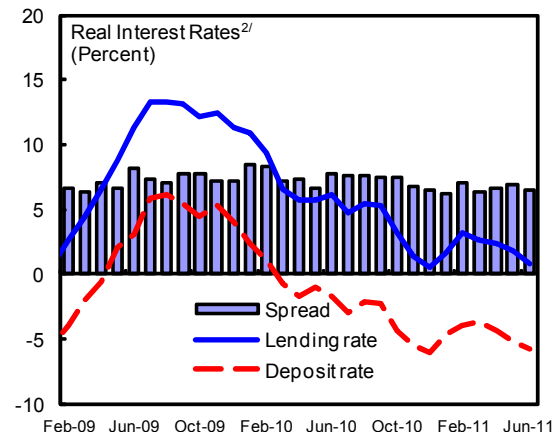
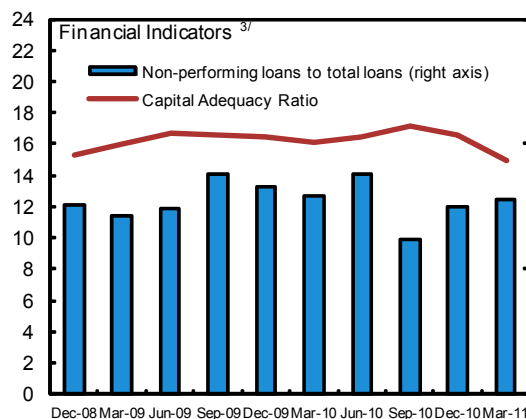
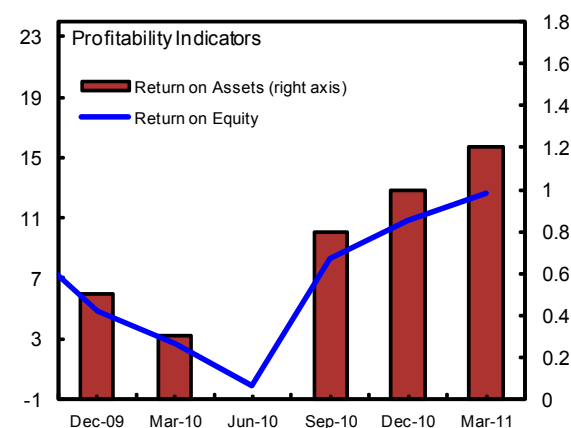
2/ In 2007, the salaries of teachers and service staff from autonomous colleges were transferred from municipalities to the central government budget.

Figure 3. Nicaragua: External Sector Developments



Source: Nicaraguan authorities; and Fund staff estimates.

Figure 4. Nicaragua: Monetary and Financial Sector Developments

Credit to the private sector started to grow in real terms ...*... banks' liquidity remains ample ...**... and deposits continued rising.**Banking spreads remain stable ...**... as does banks' asset quality.**Banks' profitability is rising.*

Sources: Nicaraguan authorities; and Fund staff calculations.

^{1/} Deflated by CPI.^{2/} Ex-post real interest rates based on CPI inflation.^{3/} Excluding restructured and reprogrammed loans.

III. POLICY DISCUSSIONS

A. Fiscal Policy

10. **The authorities agreed to take advantage of the strong revenue overperformance in 2011 to pay government debt.** Staff and authorities agreed that the revenue surprise observed in the first semester of 2011 will be broadly maintained in the remainder of the year. The authorities agreed that it would be appropriate to keep spending at budgeted levels and allocate the excess revenues to reduce debt levels.³

Nicaragua: Central Government, 2011				
	6 th review indicative targets	Revised targets	6 th review indicative targets	Revised targets
	(In C\$ million)		(In percent of GDP)	
Revenues	31,600	33,453	20.0	21.1
Expenditures	37,955	38,192	24.0	24.1
Current ^{1/}	29,299	29,657	18.5	18.7
Capital	8,656	8,535	5.5	5.4
Overall Balance (after grants)	-1,773	-104	-1.1	-0.1

^{1/}Includes wage bonus.

11. **The improved prospects for the central government balance will lower the overall fiscal deficit at the end of 2011.** However, the projected decline in the overall deficit will be somewhat lower than the improvement in the central government balance, as the operating result of public enterprises will be worse than envisaged (in part owing to higher-than-programmed investment in electricity generation and water distribution).

12. **Staff encouraged the authorities to press ahead with fiscal consolidation in 2012.** It stressed that the underlying trends pointed to a deterioration in the operating position of the social security institute (INSS) and a higher quasi-fiscal deficit of the central bank. The authorities agreed with these risks and noted that they plan to send to the National Assembly (by mid-October), a budget consistent with a central government deficit of around 0.4 percent of GDP for 2012—a substantial improvement from the 2010 outturn, which keeps the country on the path to fiscal consolidation.

13. **Medium-term fiscal risks were also discussed.** Using the updated Debt Sustainability Analysis (Annex I), staff highlighted the risks stemming from the expected deterioration in the INSS' operating balance. Staff also pointed out that the lack of clear information about debts within the electricity sector and the current low level of tariffs raised risks of future contingent liabilities to the government. The authorities agreed with the assessment and with the urgency of transforming the debate around social security reform proposals into concrete policy actions (Box 2). Until that happens, they agreed on the

³Officials indicated that they intend to pay debts of ENEL, the state-owned enterprise responsible for electricity generation, and ENACAL, the state-owned water and sewage company, with oil and electricity suppliers. However, the precise amounts and types of debt are not known to staff.

importance of keeping INSS' administrative costs under control and to strengthening the rules and transparency of asset management. They also agreed that a sustainable framework for the electricity sector was needed.

Box 2. Nicaragua: Pension Reform

Nicaragua's social security system is a pay-as-you-go defined-benefit government-administered scheme. The system has been in place since the mid-1950s,

though it is governed by a law enacted in 1982. It is administered by an autonomous agency (INSS), which has the authority to adjust pensions and contribution rates (the last adjustment was made in January 2010). In addition to old-age, survivor and disability insurance (pensions), the social security system offers medical/maternal and

Nicaragua- Social Security Contribution Rates				
	1982	1984	2000	2010
Old Age, Disability, and Survivor	5.5	5.5	10.0	11.0
Health	9.0	9.0	8.5	8.0
Occupational risks	1.0	1.0	1.5	1.5
War victims	0.0	1.5	1.5	1.5
Total	15.5	17.0	21.5	22.5

occupational-risk insurance, as well as benefits to compensate victims of the 1980s civil war. The coverage of the system is among the lowest in Latin America, with less than ¼ of the total working-age population contributing to it, and benefits mostly directed to high-income workers (roughly two-thirds of all contributions and about one-half of all benefits accrue to people in the highest per-capita consumption quintile). At the end of 2009, the social security system had accumulated reserves representing 3.2 years of pension payments, reflecting not only favorable demographics but also surpluses in its other programs (health and occupation risk).

Key parameters. Workers must contribute a minimum of 15 years and be at least 60 years of age to qualify for a pension (55 for teachers and miners). Pension benefits are based on an average wage over the 3-5 years prior to retirement. Replacement rates (defined as the ratio of pensions to average wage) vary according to years of contributions and income, and range between 55 percent and 100 percent. High-wage workers are also entitled to a family allowance of 10-15 percent of their average wage. The minimum pension is equivalent to the minimum wage of industry and contributions are calculated on income up to a maximum of US\$1800 per month (25 times the minimum wage). Indexation of pensions is done on an ad-hoc basis, with the exception of the minimum pension, which is automatically adjusted in line with increases in both the minimum wage and the pace of exchange rate devaluation. Currently, about three-quarters of all pensioners receive the minimum pension. The maximum pension is fixed at US\$1500 per month.

Outlook. According to end-2009 independent actuarial estimates, it is necessary to increase pension contribution rates (from 11.0 percent to 24.7 percent of covered earnings) to keep the system solvent. If changes are not made, the estimates show that the system would become insolvent by 2021.

Reform options. On October 2010, the INSS published a report that recommended strengthening the pension system by: (1) increasing the taxable earnings cap according to the general wage growth; (2) increasing the minimum required contribution period for receiving full pension to 30 years; (3) using the average earnings of the whole working life as the reference salary; (4) abolishing the minimum pension; (4) increasing gradually the retirement age from 60 to 65 years for workers born between 1967 and 1975; (5) increasing the contribution rate of new entrants; and (6) developing a complementary pension system that allowing individual accounts to raise pension amounts. These individual accounts would be managed by the INSS with an interest rate equivalent to the rate of return on the INSS investment portfolio.

B. Monetary Policy and the Financial System

14. **It was agreed that containing inflation and protecting the international reserves position should remain the main objectives of monetary policy.** Reflecting the strong balance of payments outturn in the first half of the year, the target for reserve accumulation in 2011 was revised upwards (to an increase of US\$20 million from a loss of US\$55 million envisaged in the previous review). International reserves as a ratio of months of imports remain higher in Nicaragua than observed, on average, across Central American countries, and the authorities showed commitment to keeping this ratio around current levels. It was agreed that it would be reasonable to formulate a monetary program for 2012 aiming at only modest declines in net international reserves and inflation. Staff endorsed the central bank's objective to improve short-term liquidity management.

15. **Staff stressed the importance of continued close monitoring of the financial system and welcomed the new law regulating the microfinance sector.** The authorities agreed and underscored that the banking sector is well capitalized and liquid. In addition, they noted that the Superintendency of Banks plans to conduct stress tests (on a pilot mode) later in the year. Authorities voiced their concern about regional risks, and stressed that effective consolidated supervision is essential for the health of regional financial groups with presence in Nicaragua. Staff advised officials to step up the efforts to better coordinate the work and information exchanges with banking regulators in the region. Staff also encouraged continued monitoring of the relatively volatile aid-related (large) deposits, which are concentrated in a few banks. In addition, staff welcomed the legal framework regulating microfinance activity passed by the National Assembly in June,⁴ and the norms requiring greater disclosure of balance-sheet information of large financial cooperatives and trust funds issued in early September.

C. Structural Policies

16. **The authorities agreed that despite the progress made under the ECF, the structural reform agenda remained challenging and should be a priority for the incoming government.** Macroeconomic stability was strengthened during the program and some important reforms were enacted, including the end-2009 tax reform and the recent regulation of microfinance activity. However, the authorities agreed that much of the reform agenda remains ahead of them, including (i) updating the cost and tariff structure of the electricity sector; (ii) aligning key parameters of the social security system; (iii) improving public financial management; and (iv) enhancing the effectiveness of poverty-reducing spending.

⁴ The framework establishes a new regulator for the sector, and defines microfinance customers' rights and obligations, as well as those of microfinance institutions. The law is expected to become operational in early 2012.

17. **Electricity sector.** The financial situation of the sector deteriorated during 2011, as sharp increases in oil prices combined with a tariff freeze created a gap between generation costs and tariffs of about 1½ percent of GDP (Box 3). The authorities explained that this gap will be covered with concessional funds from Venezuela; staff underscored that transfers of this magnitude are not sustainable and encouraged the authorities to realign tariffs with generation costs and focus subsidies on the poorest segments of society. Staff urged the authorities to continue discussions with key stakeholders to ensure the sector's financial sustainability.

Box 3. Nicaragua: Electricity Sector

In 2006 the situation of Nicaragua's electricity sector was dismal. Electricity shortages were frequent and unpredictable owing to (i) insufficient electricity generation capacity; (ii) large losses during distribution (total unbilled electricity usage was close to 35 percent); (iii) an inadequate legal framework to combat electricity theft; and (iv) accumulated arrears.

An agreement between the government and the private sector improved the framework for the sector. During 2007-08, and in the context of the current Fund program, the Nicaraguan authorities negotiated with the privately-owned electricity distribution company an *Electricity Sector Protocol* aiming at improving the sector's finances. Among other things, the protocol established that (i) electricity tariffs would reflect generation costs; (ii) the government would subsidize consumption below 150 kwh and that of poor neighborhoods; (iii) the distribution company would undertake an aggressive investment program to reduce non-technical losses, with the government capping the recognition of such losses to 13 percent of total electricity usage; and, (iv) the arrears between the distribution company and a number of public entities would be cleared. And, the government would assume a 16 percent participation in the distribution company.

Other improvements to the framework were also made (and some were part of Fund conditionality). A law establishing economic and penal sanctions for electricity theft was approved in 2008 and the protocol was broadened to include more clients in 2010. As a result of these changes, unbilled electricity by the distribution company (i.e., technical and non-technical losses) decreased from 35 percent of total usage to about 20 percent in 2010.

At the same time, electricity generation capacity was increased. Venezuela made investments in plants fueled with oil and several private projects using non-exhaustible resources began operations. The government is also undertaking investment in electricity transmission, mostly financed by international organizations (IDB, CABI and the World Bank).

In spite of the progress, large increases in world oil prices introduced a significant amount of stress in the sector. More than 2/3 of the country's electricity is still generated by fuel-based plants, and electricity tariffs have often been below generation costs. Although the resulting gap is being financed by concessional resources from Venezuela, the still large non-technical distribution losses are causing liquidity problems for electricity distribution. In particular, frozen electricity tariffs have caused a gap of about US\$100 million in 2011 at current oil prices, or 1.5 percent of GDP.

A viable electricity sector going forward will require updating the parameters established in the protocol. That will likely imply higher tariffs for consumers and a larger budgetary cost for the government. In addition, subsidies will need to be better targeted solely to the most vulnerable segments of society.

18. **Social security.** The authorities indicated that discussions with social partners on possible parametric changes to the system were underway (Box 2). The changes being considered included increasing contribution rates, delinking pensions from minimum wages, reducing replacement rates, and creating a second-pillar system. Staff stressed the importance of seeking consensus as rapidly as possible and of strengthening the management of INSS financial portfolio.

19. **Poverty Reduction.** Fund and World Bank staff discussed with the authorities the findings of the Poverty Reduction Strategy Paper (PRSP) update, recently published.⁵ The report shows that social indicators have improved markedly in Nicaragua in the second half of the past decade, particularly with significant declines in income inequality, poverty rates, and illiteracy rates. In addition to economic growth and increased demand for agricultural exports, the report stresses the role of government's social policies in improving social conditions. The report notes, though, that the overall improvement in social indicators masks some disparities, including between poverty rates in urban and rural areas. Indeed, despite significant reductions recently, extreme poverty in rural areas remains five times larger than in cities. Bank and Fund staff welcomed the clear improvement in social conditions but noted that further work is needed to ascertain the exact contribution of different factors (especially government policies) on the observed changes in social indicators.

Nicaragua: Poverty and Inequality		
	2005	2009
Incidence of poverty		
General ^{1/}	48.3	42.5
Extreme ^{2/}	17.2	14.6
Inequality		
Consumption Gini coefficient	0.41	0.37
Income Gini coefficient	0.51	0.46
Source: 2011 PRSP update.		
^{1/} Percent of people below the poverty line.		
^{2/} Percent of people below the extreme poverty line.		

Nicaragua: Key Social Indicators, 2007–10 ^{1/}				
	2007	2008	2009	2010
Net enrollment rate in primary education	86.5	87.2	87.1	87.5
Illiteracy rate of individuals 15 years old and older	20.2	7.5	3.3	3.0
Drinking water coverage (rural only)	56.3	58.7	59.4	68.6
Sewage coverage (rural only)	73.2	74.0	76.3	84.8
Source: 2011 PRSP update.				
^{1/} All data in percent of relevant population.				

20. **Public expenditure management.** A study about employment practices and different ways to raise public sector productivity (structural benchmark for September) is underway

⁵ The updated document is available at <http://www.imf.org/external/country/NIC/index.htm>.

and will serve to inform public sector management in the medium term. A final draft is expected before December.

21. **Management and transparency of aid flows.** Staff stressed the importance of continued monitoring of the size and use of these resources to avoid unwarranted macroeconomic volatility, including through the creation of contingent fiscal liabilities. In this context, staff advised the authorities to strengthen the report on aid flows, in particular regarding the uses of official cooperation flows.

IV. EXTERNAL FINANCING AND DEBT SUSTAINABILITY ANALYSIS UPDATE

22. **Budget financing.** External concessional resources will more than cover the overall fiscal deficit (after grants) projected for 2011 (Tables 4A and 4B), with the excess being used to amortize relatively expensive domestic debt. The program envisages official financing of US\$262 million; of which, budget support from the IDB together with the disbursements under the ECF represent US\$63 million.

23. **Debt relief.** The authorities are continuing negotiations to obtain debt relief on HIPC-equivalent terms from non-Paris Club bilateral creditors and for a pending claim (for US\$22.8 million) related to the commercial debt buy-back operation of October 2007. Debt to non-Paris Club bilateral creditors still pending relief stood at US\$1.6 billion (24 percent of GDP) by end-2010. Earlier this year, Libya agreed to grant debt relief for around US\$196 million (out of a total of US\$314 million owed to the country) but the relief still has not been formalized. Staff urged the authorities to continue making progress with non-Paris Club creditors.

24. **DSA Update.** As noted, staff discussed with the authorities the results of the DSA update (Annex I), which was produced under the assumption of continued fiscal restraint. Notwithstanding a recent reclassification of Nicaragua as a medium performer (from a strong performer in the previous DSA), the country maintains a moderate risk of external public debt distress, with vulnerabilities arising from worsening financing terms, lower-than-envisaged medium-term growth, or slower-than-expected external adjustment. The authorities broadly concurred with these conclusions.

V. STAFF APPRAISAL

25. **The economic recovery has gained steam but there are headwinds ahead.** Economic growth remained strong in the first half of 2011, despite the slowdown in global growth. However, the weaker external environment is expected to weigh in more strongly in 2012. Inflation is also expected to decline somewhat, while the international reserves position is projected to remain broadly stable, supported by FDI and grants.

26. **Performance under the program has been good.** All end-June performance criteria were met with margins and macro-financial stability was preserved. On the structural front, a law regulating the micro-finance sector was approved by the Assembly and the authorities introduced norms requiring greater balance-sheet transparency of financial cooperatives and trust funds. A study about employment practices and options to raise public sector productivity (structural benchmark) is underway and will be finalized before December.

27. **The weak external environment calls for continued fiscal prudence.** The weak growth outlook for the U.S. economy and other advanced countries does not bode well for Nicaraguan exports, despite the increased diversification achieved in the last few years. In addition, fiscal pressures on donor countries may have a negative effect on projected aid flows. This outlook validates the authorities' strategy of saving this year's revenue overperformance by paying down debt and of proposing moderate spending increases in the draft budget law for 2012.

28. **Reducing Nicaragua's high public debt while increasing the effectiveness of public sector spending remain key priorities.** Lower public debt ratios would free up financing for private investment and strengthen the public sector ability to mitigate the effects of adverse shocks. Additional tax and administrative reforms—including the gradual phasing out of relatively large tax exemptions and increasing public employment productivity—are also needed to strengthen the fiscal position. Given the significant long-term fiscal pressure from pension obligations, the new government should prioritize changing key parameters of the social security system.

29. **A prudent monetary policy has contributed to preserve macroeconomic stability.** Constrained by the economy's high degree of dollarization, monetary policy should continue geared at protecting the international reserves position and providing a nominal anchor to the economy, while helping smooth out transitory liquidity pressures.

30. **Banks' balance sheets are improving, but efforts at strengthening banking supervision should be sustained.** Staff welcomes the Superintendency of Banks' plans to undertake periodical stress tests. Moreover, the authorities should continue monitoring the deposits related to external aid flows and step up efforts to improve coordination and information exchanges with other regional supervisors. Staff welcomes the new regulatory framework for microfinance entities. The new law will contribute to give predictability to the sector and bodes well for more stable financing flows.

31. **The financial and regulatory framework of the electricity sector should be revamped.** The parameters established in the "Protocol" of 2008 should be updated to reflect higher long-term oil prices and lower-than-expected reduction in distribution losses. In addition, electricity tariffs have to be kept broadly aligned with costs, and subsidies would need to be better targeted.

32. **Recent progress in aid-flows reporting is welcome and efforts in this area should continue.** Staff welcomes the recent issuance of norms requiring greater disclosure of balance-sheet information of large financial cooperatives and trust funds. Prompt publication of these balance sheets should be a priority for the new government.

33. **Staff recommends the completion of the seventh review under the ECF arrangement and of the Financing Assurances Review.**

34. **It is proposed that the next Article IV consultation with Nicaragua be held on the standard 12-month cycle.**

Table 1a. Nicaragua: Quantitative Performance Criteria and Indicative Targets, 2010-11^{1/}

	2010		2011			
	Jan-Dec		Jan-Jun		Jan-Dec	
	Adj. Prog.	Prel.	Adj. Prog.	Prel.	Prog.	Proj.
Performance Criteria (Jan-Dec 2010, Jan-Jun 2011, indicative targets otherwise)						
	<i>(In millions of Córdoba)</i>					
1. Floor on combined public sector overall balance, after grants ^{2/}	-3,418	-1,982	-1,822	818	-2,896	-1,803
2. Floor on Social Security Institute (INSS) overall balance, after grants	1,415	1,492	982	1,040	1,400	1,431
3. Ceiling on change in net domestic assets of the central bank ^{3/}	1,560	-182	230	-982	2,348	1,098
Cumulative flows from end-June 2010 ^{3/}	2,549	807	1,037	-174	3,155	1,905
	<i>(In millions of US dollars)</i>					
4. Floor on change in net international reserves of the central bank ^{3/}	-35	105	-70	-5	-55	20
Cumulative flows from end-June 2010 ^{4/}	-45	95	25	90	40	115
5. Continuous ceiling on nonconcessional external debt contracted or guaranteed by the consolidated public sector	0	0	0	0	0	0
6. Continuous ceiling on the accumulation of new external arrears of the combined public sector	0	0	0	0	0	0
Indicative targets						
	<i>(In millions of Córdoba)</i>					
1. Ceiling on central government primary expenditure ^{5/}	29,953	30,439	16,954	16,639	35,460	35,696
2. Floor on poverty-related expenditures of the central government ^{6/}	18,368	18,107	9,645	9,839	21,103	21,064
3. Ceiling on monitorable wage bill	11,288	11,301	6,088	5,924	12,850	13,121
Memorandum items						
Stock of NIR (adjusted, US\$ millions)	776	917	847	911	862	937

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates/projections.

^{1/}Cumulative flows starting at the beginning of the calendar year. Definitions are specified in the TMU, including adjusters.

^{2/}Adjusted by any excess of project loans for up to US\$15 million in 2010 and US\$55 million in 2011. It is adjusted in 2011 by any use of US\$49.5 million of a grant to ENACAL received in 2009.

^{3/}Adjusted for deviations in budget support external loans compared to programmed levels in both in 2010 and 2011.

^{4/}The targets for NDA and NIR-Adjusted are defined as cumulative flows from June 2010.

^{5/}Adjusted by any shortfalls/excess in observed grants and project-loans with respect to programmed amounts.

^{6/}Adjusted any shortfalls/excess in external financing as specified in TMU.

Table 1b. Nicaragua: Structural Measures, 2010-11^{1/}

	Date		Status
Assembly approval of a regulatory framework for institutions operating in the microfinance industry	SB	End-July 2011	Done
Complete study assessing the scope for productivity gains and rationalizing government employment practices	SB	End-September 2011	In progress

^{1/}SB= Structural Benchmark.

Table 2. Nicaragua: Selected Social and Economic Indicators, 2008–12

I. Social and Demographic Indicators						
Main export products: coffee, sugar (ethanol), meat, gold.						
GDP per capita (current U.S. dollars, 2009)	1,082			Income shared by highest 10 percent		
Population (millions, 2009)	5.7			(in percent, 2005)		41.8
Life expectancy at birth in years (2009)	73			Poverty rate (in percent, 2009)		42.5
Infant mortality rate (per 1,000 live births, 2009)	21.8			Adult literacy rate (2005)		78.0
II. Economic Indicators						
	2008	2009	2010	2011	2012	
				6 th Rev. Prog. ^{1/}	Proj.	Proj.
Real sector						
				(In percent)		
GDP growth	2.8	-1.5	4.5	3.5	4.0	3.3
GDP deflator	15.0	3.9	6.0	9.2	9.1	6.8
Consumer price inflation						
End of period	13.8	0.9	9.2	8.6	8.0	7.5
Period average	19.8	3.7	5.5	8.7	8.3	8.8
External sector						
				(In US\$ millions)		
Current account	-1,570	-832	-969	-1,256	-1,112	-1,371
Exports of goods, f.o.b	2,530	2,390	3,157	3,677	3,966	4,345
Imports of goods, f.o.b.	-4,731	-3,929	-4,792	-5,625	-5,865	-6,451
Of which: oil	-963	-676	-751	-984	-1,029	-1,065
Capital and financial account ^{2/ 3/}	1,535	1,224	1,164	1,176	1,104	1,422
				(In percent of GDP)		
Current account	-24.6	-13.4	-14.8	-17.8	-15.7	-18.4
Exports of goods, f.o.b	39.7	38.5	48.2	52.2	56.0	58.4
Imports of goods, f.o.b.	-74.2	-63.2	-73.1	-79.8	-82.9	-86.8
Of which: oil	-15.1	-10.9	-11.5	-14.0	-14.5	-14.3
Capital and financial account ^{2/ 3/}	24.1	19.7	17.8	16.7	15.6	19.1
Fiscal sector						
Central government overall balance, after grants	-1.2	-2.8	-1.0	-1.1	-0.1	-0.4
Revenues	19.0	18.9	19.7	20.0	21.1	21.5
Expenditures ^{4/}	23.2	24.1	23.2	24.0	24.1	24.1
Grants ^{4/}	2.9	2.4	2.5	2.9	2.9	2.2
Rest of NFPS overall balance	0.4	0.9	0.4	0.0	-0.4	-0.8
Central bank balance	-0.7	-1.2	-0.9	-0.7	-0.6	-0.8
Combined public sector (CPS) overall balance	-1.5	-3.1	-1.4	-1.8	-1.1	-2.0
Financing	1.5	3.1	1.4	1.8	1.1	2.0
External	1.9	3.9	3.4	2.5	2.6	2.7
Domestic (including CB operating balance)	-0.3	-0.8	-1.9	-0.6	-1.4	-0.6
CPS overall balance, before grants	-4.6	-6.5	-4.0	-4.9	-4.3	-4.6
Public sector debt						
Total	74.8	80.1	78.5	78.2	75.0	75.2
Domestic	19.7	21.2	19.3	20.9	17.8	17.3
External ^{5/}	55.1	58.9	59.2	57.3	57.1	57.9
Memorandum items:						
GDP (US\$ million)	6,372	6,214	6,551	7,050	7,078	7,435
Gross reserves (US\$ m) ^{3/}	1,141	1,573	1,799	1,743	1,818	1,811
(in months of imports excl. maquilas)	2.9	4.9	4.7	3.9	4.0	3.6
Net international reserves ^{3/}	1,030	1,423	1,632	1,576	1,651	1,644
Net international reserves (adjusted) ^{6/}	710	811	917	862	937	926
SDR allocations	...	165	165	165	165	165
Observed reserves on foreign deposits	320	447	550	550	549	553
Short-term liabilities	111	150	167	167	167	167
Oil price (average, US\$/bbl)	97.0	61.8	79.0	107.2	103.2	100.0

Sources: Central Bank of Nicaragua; Ministry of Finance; World Bank, and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).^{2/}Figure for 2011 includes budget support that covers the financing gap.^{3/}Starting in 2009, figures include the SDR allocation for SDR105.1 million (US\$165 million) of September 2009.^{4/}Figures for 2010-11 include off-budget wage bonus.^{5/}Actual and projection are based on the 2011 DSA Update. Estimates up to 2010 correspond to the legal situation. The projections assumes no restructuring of the outstanding debt to non-Paris Club Bilaterals, currently under negotiations.^{6/}Program definition. Includes deposit insurance fund (FOGADE) and excludes the September 2009 SDR allocation and reserve requirements of commercial banks in foreign currency.

Table 3a. Nicaragua: Operations of the Central Government, 2008–12
(in millions of Córdoba)

	2008	2009	2010	2011				2012
				June		Dec.		
				6 th Rev. Prog. ^{1/}	Act.	6 th Rev. Prog. ^{1/}	Proj.	Proj.
Total Revenue	23,468	23,859	27,575	15,451	17,041	31,600	33,453	37,611
Tax	21,730	22,175	25,530	14,343	15,790	29,254	31,038	34,893
Income and property	7,002	7,865	8,481	5,457	6,016	10,150	10,642	11,824
VAT	3,139	3,885	4,028	2,136	2,371	4,486	4,725	5,156
Excises	3,338	3,339	5,541	2,948	2,897	6,119	5,926	6,449
Other	8,251	7,086	7,480	3,802	4,507	8,499	9,745	11,463
Nontax and current transfers	1,739	1,684	2,045	1,109	1,251	2,346	2,415	2,719
Total Expenditure	28,578	30,424	32,430	17,910	17,712	37,955	38,192	42,257
Current expenditures ^{2/}	21,063	23,410	24,866	14,069	13,675	29,299	29,657	32,637
Wages and salaries ^{3/}	7,629	8,615	9,603	5,192	5,028	11,050	11,318	11,268
of which: bonus	0	0	670	462	525	1,002	1,238	0
Goods and services	4,831	4,652	4,863	3,154	2,974	6,477	6,372	7,280
Interest	1,447	1,711	1,991	1,163	1,074	2,495	2,495	2,785
of which: external	515	553	595	369	349	802	802	906
Current transfers ^{4/}	7,156	8,432	8,409	4,559	4,600	9,277	9,472	11,304
Capital Expenditures ^{2/}	7,417	6,977	7,564	3,841	4,037	8,656	8,535	9,620
Domestically financed	1,839	904	1,699	1,368	1,354	1,708	2,058	1,369
Externally financed	5,578	6,073	5,866	2,472	2,683	6,948	6,476	8,251
Net lending	98	37	0	0	0	0	0	0
Overall balance (before grants)	-5,110	-6,564	-4,855	-2,459	-671	-6,355	-4,739	-4,646
Grants ^{5/}	3,574	3,080	3,504	1,796	1,796	4,582	4,635	3,865
of which: Project-related ^{6/}	2,977	2,742	2,396	1,334	1,271	3,580	3,397	3,857
Primary balance (after grants)	-89	-1,774	639	500	2,198	722	2,391	2,004
Overall balance (after grants)	-1,537	-3,485	-1,351	-663	1,124	-1,773	-104	-781
Net Financing	1,537	3,485	1,351	663	-1,124	1,773	104	781
External	1,865	4,019	3,458	641	979	3,245	3,001	3,346
Amortizations	-735	-911	-922	-498	-433	-1,131	-1,131	-1,265
Disbursements	2,600	4,930	4,380	1,138	1,412	4,376	4,133	4,610
Project-related ^{6/}	2,600	3,331	3,470	1,138	1,412	3,368	3,125	3,553
BOP support	0	1,599	910	0	0	1,008	1,008	1,057
Domestic	-328	-535	-2,107	22	-2,104	-1,472	-2,897	-2,565
Central Bank	932	-824	-2,204	645	-1,989	-182	-182	-366
Commercial Banks	-147	-19	66	0	-199	0	0	0
Amortizations (gross)	-2,320	-2,313	-2,864	-1,852	-1,889	-3,006	-3,006	-4,174
Bonds issuance ^{7/}	867	2,414	2,555	2,128	2,001	2,800	2,451	2,867
Other ^{8/}	340	207	340	-899	-28	-1,084	-2,160	-892
Privatization	0	1	0	0	0	0	0	0
<u>Memorandum items:</u>								
Monitorable wage bill ^{9/}	9,119	10,153	11,301	6,088	5,924	12,850	13,121	12,933
Poverty related expenditure	16,468	17,024	18,107	9,542	9,839	21,103	21,064	24,166
Central Government primary spending ^{10/}	27,130	28,713	30,440	16,747	16,639	35,460	35,696	39,472
Election-related Spending	0	0	159	0	0	723	745	320

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}Starting in 2008, a portion of capital spending was reclassified to current spending, namely wages and goods and services.

^{3/}For 2010 and 2011, it includes an extra-budgetary wage bonus financed with Venezuela-related resources.

^{4/}Current transfers in 2009 includes payment of arrears to the electricity sector for US\$28 million.

^{5/}For 2010 and 2011, it includes an extra-budgetary grant from Venezuela to finance the wage bonus.

^{6/}In 2010 a project loan for US\$17 million was reclassified as a grant.

^{7/}It includes issuance of central government bonds to the social security institute (INSS).

^{8/}The program for 2011 includes a net reduction of debt of the consolidated public sector through the payment of outstanding obligations of state-owned enterprises in the electricity sector and in water and sewage provision. Information on the exact amount and type of debt being paid is still pending.

^{9/}It includes the wage bill of all decentralized agencies of the central government; and the extra-budgetary wage bonus.

^{10/}It includes the extra-budgetary wage bonus.

Table 3b. Nicaragua: Operations of the Central Government, 2008–12
(in percent of GDP)

	2008	2009	2010	2011		2012
				6 th Rev. Prog. ^{1/}	Proj.	Proj.
Total Revenue	19.0	18.9	19.7	20.0	21.1	21.5
Tax	17.6	17.5	18.2	18.5	19.6	19.9
Income and property	5.7	6.2	6.1	6.4	6.7	6.8
VAT	2.5	3.1	2.9	2.8	3.0	2.9
Excises	2.7	2.6	4.0	3.9	3.7	3.7
Other	6.7	5.6	5.3	5.4	6.1	6.5
Nontax and current transfers	1.4	1.3	1.5	1.5	1.5	1.6
Total Expenditure	23.2	24.1	23.2	24.0	24.1	24.1
Current expenditures ^{2/}	17.1	18.5	17.8	18.5	18.7	18.6
Wages and salaries ^{3/}	6.2	6.8	6.9	7.0	7.1	6.4
of which: bonus	0.0	0.0	0.5	0.6	0.8	0.0
Goods and services	3.9	3.7	3.5	4.1	4.0	4.2
Interest	1.2	1.4	1.4	1.6	1.6	1.6
of which: external	0.4	0.4	0.4	0.5	0.5	0.5
Current transfers ^{4/}	5.8	6.7	6.0	5.9	6.0	6.5
Capital Expenditures ^{2/}	6.0	5.5	5.4	5.5	5.4	5.5
Domestically financed	1.5	0.7	1.2	1.1	1.3	0.8
Externally financed	4.5	4.8	4.2	4.4	4.1	4.7
Net lending	0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (before grants)	-4.1	-5.2	-3.5	-4.0	-3.0	-2.7
Grants ^{5/}	2.9	2.4	2.5	2.9	2.9	2.2
of which: Project-related ^{4/}	2.4	2.2	1.7	2.3	2.1	2.2
Primary balance (after grants)	-0.1	-1.4	0.5	0.5	1.5	1.1
Overall balance (after grants)	-1.2	-2.8	-1.0	-1.1	-0.1	-0.4
Net Financing	1.2	2.8	1.0	1.1	0.1	0.4
External	1.5	3.2	2.5	2.1	1.9	1.9
Amortizations	-0.6	-0.7	-0.7	-0.7	-0.7	-0.7
Disbursements	2.1	3.9	3.1	2.8	2.6	2.6
Project-related ^{6/}	2.1	2.6	2.5	2.1	2.0	2.0
BOP support	0.0	1.3	0.7	0.6	0.6	0.6
Domestic	-0.3	-0.4	-1.5	-0.9	-1.8	-1.5
Central Bank	0.8	-0.7	-1.6	-0.1	-0.1	-0.2
Commercial Banks	-0.1	0.0	0.0	0.0	0.0	0.0
Amortizations (gross)	-1.9	-1.8	-2.0	-1.9	-1.9	-2.4
Bonds issuance ^{7/}	0.7	1.9	1.8	1.8	1.5	1.6
Other ^{8/}	0.3	0.2	0.2	-0.7	-1.4	-0.5
Privatization	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:						
Monitorable wage bill ^{9/}	7.4	8.0	8.1	8.1	8.3	7.4
Poverty related expenditure	13.3	13.5	12.9	13.3	13.3	13.8
Central Government primary spending ^{10/}	22.0	22.7	21.8	22.4	22.5	22.5
Election-related Spending	0.0	0.0	0.1	0.5	0.5	0.2

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}Starting in 2008, a portion of capital spending was reclassified to current spending, namely wages and goods and services.

^{3/}For 2010 and 2011, it includes an extra-budgetary wage bonus financed with Venezuela-related resources.

^{4/}Current transfers in 2009 includes payment of arrears to the electricity sector for US\$28 million.

^{5/}For 2010 and 2011, it includes an extra-budgetary grant from Venezuela to finance the wage bonus.

^{6/}In 2010 a project loan for US\$17 million was reclassified as a grant.

^{7/}It includes issuance of central government bonds to the social security institute (INSS).

^{8/}The program for 2011 includes a net reduction of debt of the consolidated public sector through the payment of outstanding obligations of state-owned enterprises in the electricity sector and in water and sewage provision. Information on the exact amount and type of debt being paid is still pending.

^{9/}It includes the wage bill of all decentralized agencies of the central government; and the extra-budgetary wage bonus.

^{10/}It includes the extra-budgetary wage bonus.

Table 4a. Nicaragua: Operations of the Combined Public Sector, 2008–12
(in millions of Córdoba)

	2008	2009	2010	2011				2012
				June		Dec.		
				6 th Rev. Prog. ^{1/}	Act.	6 th Rev. Prog. ^{1/}	Proj.	Proj.
Central government overall balance	-1,536	-3,485	-1,351	-663	1,124	-1,773	-104	-781
Revenue	23,468	23,859	27,575	15,451	17,041	31,600	33,453	37,611
Expenditure ^{2/}	28,578	30,424	32,430	17,910	17,712	37,955	38,192	42,257
Current	21,063	23,410	24,866	14,069	13,675	29,299	29,657	32,637
of which: interest	1,447	1,711	1,991	1,163	1,074	2,495	2,495	2,785
Capital and net lending ^{3/}	7,515	7,013	7,564	3,841	4,037	8,656	8,535	9,620
Grants ^{4/}	3,574	3,080	3,504	1,796	1,796	4,582	4,635	3,865
Social Security Institute (INSS) balance	1,536	784	1,492	982	1,040	1,400	1,431	881
Contributions and revenues	7,129	7,783	9,627	5,117	5,331	10,339	10,677	11,396
Payments and expenses	5,593	6,999	8,135	4,136	4,296	8,942	9,257	10,525
Grants	0	0	0	1	5	3	11	11
Managua municipality (ALMA) balance	-53	60	86	14	96	-23	-27	40
of which: Grants	15	31	23	7	0	14	14	47
Overall Public Enterprises balance^{5/}	-970	255	-960	-667	-965	-1,366	-2,109	-2,316
Revenue	3,994	4,035	3,972	2,348	1,949	4,718	4,160	4,614
Expenditure	5,223	5,048	5,085	3,227	3,030	6,387	6,558	7,420
Grants ^{5/}	259	1,268	154	212	116	303	290	491
Central Bank (BCN) operating balance	-848	-1,514	-1,249	-542	-477	-1,133	-994	-1,411
Overall CPS balance (after grants)	-1,872	-3,900	-1,982	-875	818	-2,896	-1,803	-3,586
Primary balance (after grants)	-405	-2,167	46	320	1,908	-340	723	-750
Total interest	1,467	1,733	2,028	1,196	1,090	2,555	2,526	2,836
Net Financing	1,872	3,900	1,982	875	-818	2,896	1,803	3,586
External	2,301	4,874	4,706	898	1,392	3,880	4,079	4,685
Amortizations	-754	-931	-940	-508	-427	-1,152	-1,158	-1,295
Disbursements ^{4/}	3,055	5,805	5,647	1,406	1,818	5,032	5,238	7,037
Domestic	-1,277	-2,488	-3,973	-565	-2,687	-2,118	-3,270	-2,510
Central Bank	786	-865	-780	1,456	1,456	-99	-99	-3,084
Commercial Banks	951	392	-2,243	664	664	957	957	-34
Amortizations (gross)	-1,823	-2,069	-1,828	-1,719	-1,719	-2,110	-2,110	-4,174
Bonds issuance ^{7/}	587	807	1,156	1,053	1,053	1,455	1,106	4,748
Others ^{8/}	-1,778	-753	-279	-2,017	-4,140	-2,321	-3,124	0
of which: Caruna ^{9/}	486	48	-681	-35	-35	146	146	0
Central Bank (BCN) operating balance	848	1,514	1,249	542	477	1,133	994	1,411
<u>Memorandum items:</u>								
Quasi-fiscal activities of ALBA ^{10/}	5,679	4,798	11,033	4,282	4,282	8,733	12,340	13,876
CPS primary balance (before grants)	-4,252	-6,545	-3,634	-1,695	516	-5,242	-4,228	-5,164
CPS overall balance (before grants)	-5,719	-8,278	-5,662	-2,891	-1,099	-7,798	-6,754	-7,989

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}For 2010 and 2011, it includes the extra-budgetary wage bonus financed with Venezuela-related resources.

^{3/}Starting in 2008, a portion of capital spending was reclassified to current spending, namely wages and goods and services.

^{4/}In 2010, a project-loan for US\$17 million was reclassified into a grant. For 2010 and 2011, it includes an extra-budgetary grant from Venezuela to finance the wage bonus.

^{5/}It includes the state-owned water, electricity generation, electricity transmission, and port companies, as well as the telecommunications regulatory agency.

^{6/}It includes a project grant for US\$49.5 million received in December 2009 by the state-owned water company.

^{7/}It nets out purchases of central government bonds by the social security institute (INSS).

^{8/}The program for 2011 includes a net reduction of debt of the consolidated public sector through the payment of outstanding obligations of state-owned enterprises in the electricity sector and in water and sewage provision. Information on the exact amount and type of debt being paid is still pending.

^{9/}In 2010, it includes payments of short-term bills by the central government and a debt net out by the state-owned electricity company.

^{10/}It includes all resources from the oil-colaboration scheme, some of which have not been spent and are deposited in the commercial banks.

Table 4b. Nicaragua: Operations of the Combined Public Sector, 2008–12
(in percent of GDP)

	2008	2009	2010	2011	2012
				6 th Rev. Prog. ^{1/}	Proj. Proj.
Central government overall balance	-1.2	-2.8	-1.0	-1.1	-0.4
Revenue	19.0	18.9	19.7	20.0	21.5
Expenditure ^{2/}	23.2	24.1	23.2	24.0	24.1
Current	17.1	18.5	17.8	18.5	18.6
of which: interest	1.2	1.4	1.4	1.6	1.6
Capital and net lending ^{3/}	6.1	5.5	5.4	5.5	5.5
Grants ^{4/}	2.9	2.4	2.5	2.9	2.2
Social Security Institute (INSS) balance	1.2	0.6	1.1	0.9	0.5
Contributions and revenues	5.8	6.2	6.9	6.5	6.5
Payments and expenses	4.5	5.5	5.8	5.7	6.0
Grants	0.0	0.0	0.0	0.0	0.0
Managua municipality (ALMA) balance	0.0	0.0	0.1	0.0	0.0
of which: Grants	0.0	0.0	0.0	0.0	0.0
Overall Public Enterprises balance^{5/}	-0.8	0.2	-0.7	-0.9	-1.3
Revenue	3.2	3.2	2.8	3.0	2.6
Expenditure	4.2	4.0	3.6	4.0	4.2
Grants ^{6/}	0.2	1.0	0.1	0.2	0.3
Central Bank (BCN) operating balance	-0.7	-1.2	-0.9	-0.7	-0.8
Overall CPS balance (after grants)	-1.5	-3.1	-1.4	-1.8	-2.0
Primary balance (after grants)	-0.3	-1.7	0.0	-0.2	-0.4
Total interest	1.2	1.4	1.4	1.6	1.6
Net Financing	1.5	3.1	1.4	1.8	2.0
External	1.9	3.9	3.4	2.5	2.7
Amortizations	-0.6	-0.7	-0.7	-0.7	-0.7
Disbursements ^{4/}	2.5	4.6	4.0	3.2	4.0
Domestic	-1.0	-2.0	-2.8	-1.3	-1.4
Central Bank	0.6	-0.7	-0.6	-0.1	-1.8
Commercial Banks	0.8	0.3	-1.6	0.6	0.0
Amortizations (gross)	-1.5	-1.6	-1.3	-1.3	-2.4
Bonds issuance ^{7/}	0.5	0.6	0.8	0.9	2.7
Others ^{8/}	-1.4	-0.6	-0.2	-1.5	0.0
of which: Caruna ^{9/}	0.4	0.0	-0.5	0.1	0.0
Central Bank (BCN) operating balance	0.7	1.2	0.9	0.7	0.8
Memorandum items:					
Quasi-fiscal activities of ALBA ^{10/}	4.6	3.8	7.9	5.5	7.9
CPS primary balance (before grants)	-3.4	-5.2	-2.6	-3.3	-2.9
CPS overall balance (before grants)	-4.6	-6.5	-4.0	-4.9	-4.6

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}For 2010 and 2011, it includes the extra-budgetary wage bonus financed with Venezuela-related resources.

^{3/}Starting in 2008, a portion of capital spending was reclassified to current spending, namely wages and goods and services.

^{4/}In 2010, a project-loan for US\$17 million was reclassified into a grant. For 2010 and 2011, it includes an extra-budgetary grant from Venezuela to finance the wage bonus.

^{5/}It includes the state-owned water, electricity generation, electricity transmission, and port companies, as well as the telecommunications regulatory agency.

^{6/}It includes a project grant for US\$49.5 million received in December 2009 by the state-owned water company.

^{7/}It nets out purchases of central government bonds by the social security institute (INSS).

^{8/}The program for 2011 includes a net reduction of debt of the consolidated public sector through the payment of outstanding obligations of state-owned enterprises in the electricity sector and in water and sewage provision. Information on the exact amount and type of debt being paid is still pending.

^{9/}In 2010, it includes payments of short-term bills by the central government and a debt net out by the state-owned electricity company.

^{10/}It includes all resources from the oil-collaboration scheme, some of which have not been spent and are deposited in the commercial banks.

Table 5. Nicaragua: Summary Accounts of the Central Bank, 2008–12
(Flows in millions of córdobas; unless otherwise indicated)

	2008	2009	2010	2011				2012
				June		Dec.		Dec.
				6 th Rev. Prog. ^{1/}	Prel.	6 th Rev. Prog. ^{1/}	Proj.	Proj.
Exchange rate (córdobas/US\$, period average)	19.4	20.3	21.4	22.4	22.4	22.4	22.4	23.6
Net international reserves (adjusted)^{2/}	-532	2,068	2,249	-1,568	-114	-1,233	449	-236
(In US\$ millions)	-27	102	105	-70	-5	-55	20	-10
Net domestic assets	494	-1,409	-181	230	-982	2,348	1,098	1,383
Net credit to public sector (NFPS) ^{3/}	3,230	-808	-2,204	645	-1,989	-182	-182	-366
Net credit to central government	932	-824	-2,204	645	-1,989	-182	-182	-366
Net credit to RNFPS	2,299	16	0	0	0	0	0	0
Net credit to the financial system	-694	-1,529	-198	-280	-175	-130	-1,287	-561
Operational losses	848	1,514	1,249	542	477	1,133	994	1,411
Central bank bonds (net)	-3,102	-875	708	-941	297	1,010	1,010	0
Medium- and long-term foreign liabilities	258	329	362	252	210	525	477	734
Other	-47	-38	-98	11	199	-9	86	164
Currency	-38	659	2,068	-1,339	-1,096	1,115	1,546	1,147
<u>Memorandum items:</u>								
Gross reserves (US\$ million, stock) ^{4/}	1,141	1,573	1,799	1,745	1,787	1,743	1,818	1,812
Net international reserves	1,030	1,423	1,632	1,567	1,632	1,576	1,651	1,644
Net international reserves (adjusted)^{2/}	710	811	917	847	911	862	937	926
SDR allocations	...	165	165	165	165	165	165	165
Reserves on foreign currency deposits	320	447	550	556	556	550	549	553
Short-term liabilities	111	150	167	178	154	167	167	167
Central Bank paper (stock)	7,321	8,626	9,118	10,288	9,049	8,540	8,637	8,131
<i>in percent of GDP</i>	<i>7.1</i>	<i>6.8</i>	<i>6.5</i>	<i>6.5</i>	<i>5.7</i>	<i>5.4</i>	<i>5.4</i>	<i>4.6</i>
Currency (stock)	5,499	6,157	8,225	6,886	7,129	9,339	9,771	10,918
<i>Year-on-year growth (percent)</i>	<i>-0.7</i>	<i>12.0</i>	<i>33.6</i>	<i>13.7</i>	<i>17.7</i>	<i>13.6</i>	<i>18.8</i>	<i>11.7</i>

Sources: Central Bank of Nicaragua; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}Program definition. Includes deposit insurance fund (FOGADE), and excludes 2009 SDR allocation and actual reserves of commercial banks in foreign currency.

^{3/}Includes only "Títulos Especiales de Inversión."

^{4/}Starting in 2009, figures include the SDR allocation for SDR105.1 million (US\$165 million) of September 2009.

Table 6. Nicaragua: Summary Accounts of Deposit Banks and the Financial System, 2008–12
(Flows in millions of córdobas; unless otherwise indicated)

	2008	2009	2010	2011				2012
				June		Dec.		Dec.
				6 th Rev.	Prel.	6 th Rev.	Proj.	Dec.
				Prog. ^{1/}		Prog. ^{1/}		Proj.
Commercial banks ^{2/}								
Net international reserves (adjusted)	2,330	5,770	3,273	673	2,417	1,794	4,488	2,697
(in US\$ millions)	117	284	153	30	108	80	200	115
Net domestic assets	868	-1,541	6,054	2,417	2,300	4,794	2,393	2,300
Net credit to nonfinancial public sector	-794	-692	1,713	-309	-1,601	1,270	-2,134	-761
Net credit to the financial system	-572	-1,488	-3,868	-499	-1,826	-1,287	-4,755	-3,989
Net credit to the private sector	5,142	-3,479	2,539	624	-1,060	6,052	2,269	3,335
Medium- and long-term foreign liabilities	-1,271	879	1,048	310	848	522	1,097	883
Other net assets	-1,637	3,239	4,623	2,291	5,939	-1,764	5,916	2,831
Liabilities	3,198	4,229	9,326	3,090	4,718	6,588	6,881	4,997
Financial sector ^{3/}								
Net international reserves (adjusted)^{4/}	1,741	7,838	5,522	-895	2,303	561	4,936	2,462
(in US\$ millions)	90	385	259	-40	103	25	220	105
Net domestic assets	1,362	-2,950	5,873	2,646	1,318	7,142	3,491	3,683
Net credit to nonfinancial public sector	2,436	-1,501	-491	336	-3,590	1,088	-2,316	-1,127
Net credit to the private sector	5,142	-3,479	2,539	624	-1,060	6,052	2,269	3,335
Medium- and long-term foreign liabilities	-1,012	1,207	1,409	563	1,058	1,048	1,574	1,618
Other net assets	-5,204	822	2,416	1,123	4,910	-1,046	1,964	-143
Of which: Other financial institutions	-1,282	-3,150	-4,814	-710	-710	-1,274	-1,274	-892
Liabilities to the private sector	3,104	4,888	11,395	1,751	3,621	7,703	8,427	6,145
<u>Memorandum items:</u>								
Credit to the private sector (percent of GDP)	37.6	33.9	32.4	29.1	28.4	32.5	30.0	29.1
Credit to the private sector (year-on-year, percent)	12.5	-7.5	5.9	10.7	8.9	13.3	5.0	7.0
Foreign currency deposits (percent of total)	68.5	71.8	73.1	73.1	73.5	73.2	73.4	73.4

Sources: Central Bank of Nicaragua; and Fund staff estimates and projections.

^{1/}Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{2/}Includes Financiera Nicaraguense.

^{3/}Includes Central Bank of Nicaragua.

^{4/}Program definition (for Central bank NIR Adjusted). Includes deposit insurance fund (FOGADE), and excludes the September 2009 SDR allocation and actual reserves of commercial banks in foreign currency.

Table 7. Nicaragua: Balance of Payments, 2008–16^{1/}
(In millions of U.S. dollars; unless otherwise indicated)

	2008	2009	2010	2011		2012	2013	2014	2015	2016
				6 th Rev. Prog. ^{2/}	Proj.			Proj.		
Current account	-1,570	-832	-969	-1,256	-1,112	-1,371	-1,415	-1,391	-1,408	-1,181
According to BPM5 ^{3/}	-1,517	-760	-947	-1,256	-1,112	-1,371	-1,415	-1,391	-1,408	-1,181
Trade balance	-2,201	-1,540	-1,636	-1,947	-1,899	-2,106	-2,103	-2,051	-2,022	-1,774
Exports, f.o.b.	2,530	2,390	3,157	3,677	3,966	4,345	4,618	4,899	5,193	5,503
Imports, f.o.b.	-4,731	-3,929	-4,792	-5,625	-5,865	-6,451	-6,721	-6,951	-7,214	-7,277
Of which: oil imports	-963	-676	-751	-984	-1,029	-1,065	-1,065	-1,048	-1,040	-793
Services	-269	-148	-222	-225	-124	-98	-108	-117	-126	-136
Receipts	460	496	472	535	578	656	686	718	755	795
Payments	-729	-644	-694	-760	-702	-754	-793	-835	-881	-931
Income	-240	-263	-284	-279	-260	-306	-367	-409	-469	-501
Credits	23	6	9	7	13	11	11	11	12	12
Debits	-263	-269	-293	-286	-273	-317	-378	-421	-481	-513
Of which: official interest	-36	-33	-31	-35	-36	-41	-44	-50	-78	-84
Transfers to the private sector	1,140	1,118	1,173	1,195	1,171	1,139	1,162	1,187	1,209	1,230
Of which: remittances	818	768	823	865	881	907	940	976	1,012	1,049
Capital account	1,535	1,224	1,164	1,114	1,042	1,357	1,435	1,405	1,456	1,359
Official	479	714	395	278	336	382	472	416	377	365
Official transfers	347	300	186	174	212	188	182	178	173	166
Of which: grants	347	300	186	174	212	188	182	178	173	166
Disbursements	219	330	285	180	199	283	374	337	317	324
Amortization	-75	-81	-71	-73	-73	-89	-84	-98	-113	-125
Other	-13	165	-5	-3	-3	0	0	0	0	0
Private	1,057	511	770	836	706	976	964	988	1,079	994
Foreign direct investment	626	434	508	658	741	803	692	726	760	796
Capital Transfers	52	99	17	3	4	0	0	0	0	0
Of which: ALBA collaboration	22	55	0	0	0	0	0	0	0	0
Financial system and other capital flows	379	-23	244	175	-39	173	271	262	319	198
Assets	-67	-211	-278	-149	-341	-156	-156	-156	-116	10
Medium- and long-term liabilities	527	196	460	272	360	273	437	428	444	197
Of which: ALBA collaboration ^{4/ 5/}	293	232	509	382	421	405	393	365	-83	-103
Other, including errors and omissions ^{6/}	-81	-8	62	52	-57	56	-9	-9	-9	-9
Overall balance	-35	392	195	-142	-71	-13	20	14	48	179
Change in external assets (- increase) ^{7/}	-38	-432	-226	56	-19	7	-95	-85	-55	-184
Exceptional financing	72	40	30	24	27	6	10	7	6	5
Financing gap^{8/}	...	...	...	62	63	65	65	65	...	...
IMF	...	...	...	17	18	...	...	...	...	...
World Bank	...	...	...	0	0	...	...	...	...	...
IDB	...	...	...	45	45	45	...	...	...	...
Bilaterals and other multilaterals	...	...	...	0	0	...	...	...	...	...
Memorandum items:										
Current account (in percent of GDP)	-24.6	-13.4	-14.8	-17.8	-15.7	-18.4	-17.9	-16.6	-15.8	-12.5
According to BPM5 ^{3/}	-23.8	-12.2	-14.5	-17.8	-15.7	-18.4	-17.9	-16.6	-15.8	-12.5
Excluding official interest	-23.2	-11.7	-14.0	-17.3	-15.2	-17.9	-17.3	-16.0	-15.0	-11.6
Non-oil, excluding interest	-8.1	-0.8	-2.5	-3.4	-0.7	-3.6	-3.9	-3.5	-3.3	-3.2
Alba-related flows (in percent of GDP)	7.2	7.1	7.9	6.6	7.8	7.9	5.0	4.4	0.0	-0.2
FDI	2.1	2.4	0.2	1.1	1.8	2.5	0.0	0.0	0.0	0.0
Oil collaboration	5.0	4.7	4.9	6.0	6.6	6.1	5.6	5.0	0.0	-0.2
Others ^{5/}	0.5	0.1	2.8	-0.6	-0.7	-0.6	-0.6	-0.6	0.0	0.0
Gross reserves ^{7/}	1,141	1,573	1,799	1,743	1,818	1,811	1,907	1,992	2,046	2,230
in months of imports excl. maquilas	2.9	4.9	4.7	3.9	4.0	3.6	3.7	3.7	3.7	4.0
Oil price (average, US\$/bbl)	97.0	61.8	79.0	107.2	103.2	100.0	99.5	97.5	96.5	95.5

Sources: Central Bank of Nicaragua; and Fund staff estimates and projections.

^{1/} Assuming that outstanding debt to non-Paris Club bilaterals is settled on HIPC-equivalent terms by the end of 2011. Debt service is measured on accrual basis. The presentation has been revised to reflect methodological changes in the classification of services and income and the measurement of NGO transfers.

^{2/} Staff Report for the Sixth Review under the ECF arrangement (EBS/11/56, April 13, 2011).

^{3/} Untied grants are recorded above the line.

^{4/} A portion of ALBA-related flows is being used to finance off-budget transport subsidies and wage bonuses in 2010 and 2011.

^{5/} 2010 includes a bilateral loan of US\$ 185 million to Alba-Caruna provided under different terms than the oil collaboration, i.e., 5 years maturity, 1 year grace period and 2 percent interest.

^{6/} Includes short-term credits for importing oil under ALBA.

^{7/} The one-off allocation of SDR 105.1 million (US\$165 million) in 2009 is reported in the official financial account, in accordance with BPM6.

^{8/} Includes expected IMF disbursements and budget support loans and grants for 2011. The financing gap estimated for 2012-14 is preliminary and its financing is mostly unidentified. Disbursements made in 2010 are included in official disbursements.

Table 8. Nicaragua: External Financing Requirements, 2008–16^{1/}

(In millions of U.S. dollars)

	2008	2009	2010	2011		2012	2013	2014	2015	2016
				6 th Rev. Prog. ^{2/}	Proj.			Proj.		
Gross financing requirements	-1,696	-1,181	-1,271	-1,276	-1,207	-1,452	-1,594	-1,574	-1,575	-1,489
Current account deficit (excluding official transfers)	-1,570	-832	-969	-1,256	-1,112	-1,371	-1,415	-1,391	-1,408	-1,181
Public debt amortization	-75	-81	-71	-73	-73	-89	-84	-98	-113	-125
GIR accumulation (-) ^{3/}	-38	-432	-226	56	-19	7	-95	-85	-55	-184
Other official ^{3/ 4/}	-13	165	-5	-3	-3	0	0	0	0	0
Gross financing sources	1,696	1,181	1,271	1,213	1,144	1,387	1,529	1,509	1,575	1,489
Foreign direct investment and capital transfers	678	534	525	661	744	803	692	726	760	796
Debt financing from private creditors, net	379	-23	244	175	-39	108	271	262	319	198
Official transfers	347	300	186	174	212	188	182	178	173	166
Of which: grants	347	300	186	174	212	188	182	178	173	166
Official disbursements (medium- and long-term loans)	219	330	285	180	199	283	374	337	317	324
Net Exceptional Financing	72	40	30	24	27	6	10	7	6	5
Financing gap	...	...	...	62	63	65	65	65	...	...
IMF	...	...	...	17	18	...	...	...	...	...
World Bank	...	...	...	0	0	...	...	...	...	...
IDB	...	...	...	45	45	45	...	...	...	...
Bilaterals and Other Multilaterals	...	...	...	0	0	...	...	...	...	...
Memorandum items:										
Official disbursements	219	330	285	242	262	348	439	402	317	324
Gross international reserves (GIR) ^{5/}	1,141	1,573	1,799	1,743	1,818	1,811	1,907	1,992	2,046	2,230
In months of imports of G&NFS excl. maquilas	2.9	4.9	4.7	3.9	4.0	3.6	3.7	3.7	3.7	4.0
Change GIR (+ = increase) ^{3/}	38	432	226	-56	19	-7	95	85	55	184

Sources: Central Bank of Nicaragua; and Fund staff estimates/projections.

^{1/}Assuming that outstanding debt to non-Paris Club bilaterals is settled on HIPC-equivalent terms in 2011. Debt service is measured on an accrual basis.^{2/}Staff Report for the Fourth and Fifth Reviews under the ECF arrangement (EBS/10/198, November 2, 2010).^{3/}2009 entry includes the allocation of SDR 105.1 million (US\$165 million) of September 2009.^{4/}Includes public external assets.^{5/}Starting in 2009, figures include the SDR allocation for SDR105.1 million (US\$165 million) of September 2009.

Table 9. Nicaragua: Nonfinancial Public Sector Gross Financing Requirements, 2008–12

	2008	2009	2010	2011	2012
				Proj.	
(In US\$ millions)					
a. NFPS primary deficit (before grants)	176	247	111	144	159
CG and public enterprises	255	286	181	208	196
INSS	-79	-39	-70	-64	-37
b. Debt service obligations	208	232	224	259	353
External	65	72	73	89	94
Interest	27	28	29	36.9	39
Amortization	38	45	44	52	55
Domestic	143	159	151	170	259
Interest	49	58	66	76	81
Amortization	94	102	85	94	177
c. Gross financing needs (a+b)	384	479	336	403	512
d. Financing sources	384	479	336	403	512
External	356	451	436	455	486
Project	325	355	342	355	441
Grants	167	148	120	166	187
Loans	158	207	223	189	254
Budget support	32	97	94	100	45
Grants ^{1/}	32	18	52	55	0
Loans ^{2/}	0	79	43	45	45
Domestic	27	28	-100	-52	26
Central Bank	41	-43	-36	-4	-131
Commercial banks	49	69	-105	43	-1
Other	-63	1	41	-90	158
(In percent of GDP)					
a. NFPS primary deficit (before grants)	2.8	4.0	1.7	2.0	2.1
CG and public enterprises	4.1	4.7	2.8	2.9	2.6
INSS	-1.3	-0.6	-1.1	-0.9	-0.5
b. Debt service obligations	3.3	3.8	3.4	3.7	4.7
External	1.0	1.2	1.1	1.3	1.3
Interest	0.4	0.4	0.4	0.5	0.5
Amortization	0.6	0.7	0.7	0.7	0.7
Domestic	2.3	2.6	2.3	2.4	3.5
Interest	0.8	0.9	1.0	1.1	1.1
Amortization	1.5	1.7	1.3	1.3	2.4
c. Gross financing needs (a+b)	6.1	7.8	5.1	5.7	6.9
d. Financing sources	6.1	7.8	5.1	5.7	6.9
External	5.7	7.3	6.7	6.4	6.5
Project	5.2	5.8	5.2	5.0	5.9
Grants	2.7	2.4	1.8	2.3	2.5
Loans	2.5	3.4	3.4	2.7	3.4
Budget support	0.5	1.6	1.4	1.4	0.6
Grants ^{1/}	0.5	0.3	0.8	0.8	0.0
Loans ^{2/}	0.0	1.3	0.7	0.6	0.6
Domestic	0.4	0.5	-1.5	-0.7	0.3
Central Bank	0.6	-0.7	-0.6	-0.1	-1.8
Commercial banks	0.8	1.1	-1.6	0.6	0.0
Other	-1.0	0.0	0.6	-1.3	2.1

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates and projections.

^{1/}Figures for 2010 and 2011 include grant from Venezuela to finance an extra-budgetary wage bonus.

^{2/}Figures for 2010 and 2011 assume disbursement of IDB budget support loan for US\$43 million and US\$45 million respectively.

Table 10. Nicaragua: Indicators of Capacity to Repay the Fund, 2011–16

	2011	2012	2013	2014	2015	2016
Fund obligations based on existing and prospective credit						
In millions of SDRs	0.0	8.7	11.1	14.7	19.4	21.1
In millions of U.S. dollars	0.0	13.8	17.6	23.3	30.7	33.3
In percent of exports of goods and nonfactor services	0.0	0.3	0.3	0.4	0.5	0.5
In percent of external public debt service	0.0	10.7	13.7	15.8	16.1	16.0
In percent of quota	0.0	6.7	8.5	11.3	14.9	16.2
In percent of gross international reserves	0.0	0.8	0.9	1.2	1.5	1.5
Fund credit outstanding						
In millions of SDRs	118.4	110.0	99.3	84.9	65.7	44.8
In millions of U.S. dollars	188.1	175.3	157.8	134.6	104.0	70.8
In percent of exports of goods and nonfactor services	4.1	3.5	3.0	2.4	1.7	1.1
In percent of external public debt service	173.3	135.0	123.0	91.2	54.5	33.9
In percent of quota	91.1	84.6	76.4	65.3	50.5	34.5
In percent of gross international reserves	10.3	9.7	8.3	6.8	5.1	3.2
Memorandum items						
Exports of goods and services (millions of U.S. dollars)	4,544	5,002	5,304	5,617	5,947	6,298
External public debt service (millions of U.S. dollars)	109	130	128	148	191	209
Quota (millions of SDRs)	130	130	130	130	130	130
Quota (millions of U.S. dollars)	207	207	207	206	206	205
Gross international reserves (millions of U.S. dollars) ^{1/}	1,818	1,811	1,907	1,992	2,046	2,230
SDR per U.S. dollars (period average)	0.6	0.6	0.6	0.6	0.6	0.6

Source: Fund staff calculations.

^{1/}Includes new SDR allocation in 2009.

Table 11. Nicaragua: Schedule of Disbursements Under the ECF Arrangement

Date	Proposed Schedule		Conditions	Status
	In millions of SDRs	In percent of quota ^{1/}		
Oct. 5, 2007	11.90	9.2	Board approval of PRGF arrangement	Completed
Sep. 10, 2008 ^{2/}	18.40	14.2	Observance of end-Dec 2007 performance criteria and completion of first review	Completed
Nov. 2, 2009 ^{3/}	23.80	18.3	Observance of end-Jun and end-Dec 2008 performance criteria and completion of second and third reviews.	Completed
Nov. 19, 2010 ^{4/}	12.80	9.8	Observance of end-Dec 2009 and end-Jun 2010 performance criteria and completion of fourth and fifth reviews.	Completed
Apr. 29, 2011	5.55	4.3	Observance of end-Dec 2010 performance criteria and completion of sixth review	Completed
Oct. 24, 2011	5.55	4.3	Observance of end-Jun 2011 performance criteria and completion of seventh review	
Total	78.00	60.0		

Sources: IMF, Finance Department and Fund staff estimates and projections.

^{1/}Nicaragua's quota is SDR 130 million.

^{2/}Includes augmentation of 5 percent of quota approved in September 2008.

^{3/}Includes disbursement for completion of second and third reviews, each for SDR 11.9 million.

^{4/}Original program contemplated 6 reviews.

Table 12. Nicaragua: Financial Soundness Indicators, 2008–11
(In percent, unless otherwise indicated)

	2008	2009		2010		2011	
		Jun	Dec	Jun	Dec	Mar	Jun
Capital adequacy							
Regulatory capital to risk-weighted assets	15.3	16.7	16.5	16.4	16.6	15.0	15.7
Regulatory Tier 1 capital to risk-weighted assets ^{1/}	9.0	10.0	10.9	11.8	11.1	9.9	10.0
Asset quality							
Nonperforming loans to total gross loans	3.0	3.0	3.3	3.5	3.0	3.1	2.9
Nonperforming loans to total gross loans ^{2/}	6.7	8.3	10.9	11.0	8.0	7.7	7.4
Nonperforming loans net of provisions to capital	17.2	25.3	33.4	30.7	20.3	17.5	14.8
Earnings and profitability							
Return on assets	1.8	1.4	0.5	0.0	1.0	1.2	1.4
Return on equity	18.1	13.3	4.8	-0.1	10.8	12.7	14.5
Interest margin to assets	9.1	8.7	8.7	7.8	7.0	6.8	6.2
Liquidity							
Liquid assets to total assets	21.2	24.5	29.5	31.5	28.7	29.1	31.1
Liquid assets to total short-term liabilities	118.0	137.7	139.4	121.0	120.8	122.3	143.6
Exposure to FX risk							
Net open position in foreign exchange to capital	94.7	90.8	81.4	86.6	99.4	120.6	n.a.
Number of institutions^{3/}	10	10	9	9	8	8	8
Total assets (in millions of cordobas)	71,791	75,538	79,754	91,508	91,681	97,979	102,429
Bank concentration							
Number of banks accounting for at least							
25 percent of total assets	1	1	1	1	2	2	2
75 percent of total assets	9	9	8	8	6	6	6
Total assets (in percent of GDP)							
Private commercial	58.2	60.4	63.8	68.6	68.7	61.8	65.2
Of which: Foreign banks ^{3/}	25.7	26.3	29.1	27.8	26.3	23.6	24.2
Bank deposits (percentage of GDP)							
Private commercial	39.6	41.3	45.2	50.8	52.8	47.8	51.4
Of which: Foreign banks ^{3/}	17.7	18.4	20.0	19.7	20.0	17.9	18.8
Dollarization and maturity structure							
Banking system assets as percentage of GDP	58.2	60.4	63.8	68.6	68.7	61.8	65.2
Assets in foreign currency							
as percentage of banking system assets	69.5	68.0	70.2	68.9	72.0	73.2	73.2

Sources: Superintendency of Banks; and Central Bank of Nicaragua.

^{1/}In 2006 a regulatory change narrowed the definition of Tier 1 capital.

^{2/}NPLs including restructured and reprogrammed loans.

^{3/}In 2009, HSBC (with deposits less than one percent of total deposits) closed its operations in Nicaragua. In July 2010 Banex closed its operations in Nicaragua.



Attachment I: Letter of Intent

GOVERNMENT OF NICARAGUA

October 3, 2011

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C.

Dear Ms. Lagarde:

1. The performance of the Nicaraguan economy has been satisfactory during 2011. All quantitative performance criteria for June 2011 under the Extended Credit Facility (ECF) have been met, and progress has been made in implementing the supplementary agenda, both of which have contributed to foster macroeconomic stability. For the remainder of the year, the Government of Reconciliation and National Unity (GRUN) will continue to implement prudent macroeconomic policies, with particular attention to the potential impact on the economy of the observed economic slowdown in the advanced economies and the continuing high level of international commodity prices.

Macroeconomic Framework for 2011-2012

2. After growing at a rate of 4.5 percent in 2010, gross domestic product (GDP) will continue to recover in 2011 at a projected rate of around 4 percent. Inflation is expected to hover at the lower end of the 8 to 9 percent range, primarily reflecting pressures on international prices for agricultural and energy products. In line with the decline in the terms of trade and a higher level of economic activity, the external current account deficit will increase in 2011, from 14.8 percent of GDP in 2010 to 15.7 percent of GDP this year. The revised growth outlook in the advanced economies suggests that GDP growth will slow in 2012, to a figure of between 3 and 3.5 percent, while inflation is also expected to decline to a range between 7 and 8 percent. It is expected that the external current account deficit will stand at around 18.4 percent of GDP in 2012.

Fiscal policy

3. The government will continue to implement a prudent and sustainable fiscal policy, and to that end will send to the National Assembly an amendment to the 2011 General Budget of the Republic (GBR) consistent with a central government deficit after grants of approximately 0.1 percent of GDP, which represents a 1 percentage-point improvement over the program agreed in the context of the sixth review of the ECF. This result will be achieved owing to improvements in tax revenues, reflecting the higher level of economic activity, and changes in income tax withholding for commercial banks, as well as a prudent execution of government expenditure. The increased resources will be used to pay down public debt, with priority being given to debt associated with the electricity sector. The payment of this debt will be included in a budget amendment to be approved by the National Assembly in 2011. In line with the improved central government deficit, the consolidated public sector deficit will also be smaller than expected in the last review and will reach about 1.1 percent of GDP in 2011. In addition, in mid-October the government will send to the National Assembly the GBR for 2012, which will be consistent with a deficit after grants of 0.4 percent of GDP. The monitorable wage bill as a share of GDP will remain broadly constant, while poverty-reducing expenditure will continue to be protected as a share of GDP. The surplus of the Nicaraguan social security institute (INSS) will stand at 0.5 percent of GDP, while the deficit of the consolidated public sector (CPS) will total around 2 percent of GDP.

4. In October 2011, the government published a report assessing the implementation of the National Human Development Plan during the period 2009–10 on the basis of poverty surveys financed jointly by the World Bank (WB) and the Inter-American Development Bank (IDB), that have been made available to both institutions. At the same time, the government is negotiating a new program with the IDB that will aim to strengthen the efficiency and effectiveness of social programs, particularly in the areas of health, education and family protection.

5. As part of its efforts to strengthen the tax system, the government has continued to explore ways of reducing the number of exemptions and deductions and establishing a regulation on transfer prices, for which it has received assistance from the IMF. In the area of pensions, the study containing a range of options for improving the financial position of the pension system has been presented to a tripartite forum including workers, employers and the government. Moreover, the INSS has published the composition of its financial assets in its 2010 Annual Report, a practice that it plans to continue in the future. Additionally, improvements to the investment rules are planned to ensure that portfolio management is in line with international best practices; specifically, a draft for new investment regulations will be prepared during the last quarter of 2011.

Monetary and financial policy

6. Monetary policy will remain focused on ensuring adequate international reserve coverage, containing inflation, and maintaining appropriate levels of liquidity in the money markets, in an international context characterized by the weaker economic situation of

advanced countries. Net international reserves (NIR-adjusted) are expected to be higher than programmed, and to increase by approximately US\$20 million in 2011, as a result of the higher-than-expected increase in the demand for base money, which will be followed by a slight decline next year. The rate of crawl of the exchange rate will be maintained at 5 percent in 2012. The Central Bank has continued its institutional strengthening. In this context, its capitalization will be continued and further steps will be taken toward its formalization. As well, and in line with IMF recommendations, a manual setting out the principles for the preparation of the Central Bank's financial statements in accordance with International Financial Reporting Standards (IFRS) has been adopted.

7. The banking system shows signs of improvement. Financial and solvency indicators for July 2011 suggest that progress has been made with the restructuring of their credit portfolios, which has led to an improvement in their profitability. It is expected that the improvement in the banks' balance sheets will result in a gradual increase in bank lending. The monetary and financial authorities will continue to monitor the quality of credit portfolios and deposit trends. At the same time, they will step up their efforts to cooperate with other supervisors in the region, to ensure timely information flows on the performance of financial groups with a presence in Nicaragua. As well, the Superintendence of Banks and Other Financial Institutions plans to start implementing the stress test methodology on a pilot basis in late 2011, with technical assistance from the IMF. The government will continue to ensure that the legislative framework promotes the sound development of credit markets, maintaining the current policy of market-based determination of interest rates.

External Financing

8. Concessional resources are important for the financing of the government's economic program. It is expected that the IDB will make disbursements of budgetary assistance in the amount of US\$45 million in 2011 and a similar amount in 2012. Concessional resources will continue to be allocated to financing social programs and investment in infrastructure, including the electrification of rural areas and disadvantaged neighborhoods. Nonconcessional borrowing will continue to be strictly controlled, while efforts will be made to obtain new concessional resources. To improve public debt management, the Central Bank and the Ministry of Finance will jointly prepare an annual Debt Sustainability Analysis that will enable them to assess the fiscal space in the medium-term. In the context of the Heavily Indebted Poor Countries (HIPC) Initiative, further efforts will be made to restructure the external debt pending relief.

Supplementary agenda

9. **Electricity sector.** The government recognizes the strategic importance of the energy sector and is committed to maintaining its financial viability. The difference between the average cost of electricity generation and the tariffs in effect in 2011 will result in a financing shortfall of approximately US\$100 million, which is being financed with concessional resources from Venezuela. These resources will be repaid as efforts to transform the country's energy matrix result in average generation costs that are lower than applicable tariffs. The government acknowledges that subsidies will have to be refocused

and the parameters governing the electricity sector will need to be revised starting in 2012, and it is working with stakeholders to ensure the normal functioning of the sector. To this end, the government will work so that the electricity tariffs normalize payment flows, and that investments in the sector help reduce technical and non-technical losses, while increasing service coverage. The central government will continue to guarantee through the budget the payment of its own electricity consumption, and the subsidies for customers paying social tariffs, pensioners, and disadvantaged neighborhoods, and will ensure that public companies that consume large amounts of electricity pay their electricity bills on a timely basis.

10. **Water and sewage.** Following some delays in the implementation of its investment program, the public water and sewage company (ENACAL) is investing in infrastructure in cooperation with the World Bank, the IDB, and the Spanish Cooperation Agency, which will enable it to improve its service and reduce the levels of unbilled water. To this end, ENACAL plans to install 20,000 new meters in the city of Managua by end-2011 with the twofold aim of improving billing and reducing technical losses. At the same time, ENACAL is devising a multiannual plan for the sector that will set targets for reducing unbilled water, among other objectives, with a view to improving the financial viability of providing this service.

11. **Enhanced monitoring of external aid flows.** The Central Bank will publish by mid-October the seventh report on foreign aid, including detailed information on the use of such aid in the first half of 2011. The government will continue to ensure that the use of foreign aid does not generate fiscal contingent liabilities or sharp fluctuations in the level of bank deposits, and will consult with the Fund to ensure that the use of such aid is in line with the economic program.

12. **Strengthening of the public administration.** A series of steps is being taken to improve financial public management. Specifically, (i) with financial and technical assistance from the IDB, the government is conducting a study that will assess the budgeting of permanent and temporary positions in the central government and that will include options for its improvement (*structural benchmark*); the government has discussed preliminary findings of the study with the IMF technical team and expects to complete it by November 2011; (ii) further progress has been made in strengthening tax and customs administration based on a work plan implemented with assistance from the Regional Technical Assistance Center (CAPTAC-DR); moreover, the IMF will provide technical assistance to support the efforts to modernize the General Directorate of Taxes (DGI); (iii) the Office of the Comptroller General of the Republic (CGR) published the audit of the 2009 GBR during the third quarter of 2011, and the draft budget for 2012 includes an allocation that will enable the CGR to do a similar audit of the 2010 GBR during the first half of 2012; the government will step up its efforts to ensure that public enterprises publish their audited financial statements; (iv) efforts have been ongoing to improve liquidity and public debt management; in this regard, the central government floating debt is expected to be reduced significantly in 2011, and the coupon on new public debt issuance will be adjusted to reflect market financing costs.

13. **Microfinance sector and cooperatives.** To strengthen supervision, transparency and efficiency in the microfinance sector, the National Assembly approved in June 2011 the Law for the Promotion and Regulation of Microfinance Institutions, which is applicable to entities operating in the sector (*structural benchmark*). The new oversight agency for the microfinance sector (CONAMI) will begin operations in the first quarter of 2012, and the necessary financial resources for this will be included in the GBR. In addition, the oversight agency for cooperatives (INFOCOOP) issued regulations in August 2011 that set the standards for the preparation of the financial statements of savings and loan cooperatives, which will be published.

14. In view of the progress made in implementing the ECF and the framework presented for the remaining policies, we hereby request approval of the seventh review and the eighth disbursement of the ECF in the amount of SDR5.55 million. Table 1 shows quantitative performance criteria through June 2011 and projections for the remainder of the year. Structural benchmarks through end-2011 are shown in Table 2. The government believes that the policies described in this letter are sufficient to meet the objectives of our economic program and we stand ready to take additional measures that may be needed for this purpose. In addition, we will consult with Fund staff regarding any measures that could have a potential impact on the program.

Sincerely yours,

/s

Antenor Rosales Bolaños
President
Central Bank of Nicaragua

/s

Alberto Guevara Obregón
Minister
Ministry of Finance and Public Credit

Table 1. Nicaragua: Quantitative Performance Criteria and Indicative Targets, 2010-11 1/

	2010		2011			
	Jan-Dec		Jan-Jun		Jan-Dec	
	Adj. Prog.	Prel.	Adj. Prog.	Prel.	Prog.	Proj.
Performance Criteria (Jan-Dec 2010, Jan-Jun 2011, indicative targets otherwise)						
	<i>(In millions of Córdoba)</i>					
1. Floor on combined public sector overall balance, after grants 2/	-3,418	-1,982	-1,822	818	-2,896	-1,803
2. Floor on Social Security Institute (INSS) overall balance, after grants	1,415	1,492	982	1,040	1,400	1,431
3. Ceiling on change in net domestic assets of the central bank 3/	1,560	-182	230	-982	2,348	1,098
Cumulative flows from end-June 2010 4/	2,549	807	1,037	-174	3,155	1,905
	<i>(In millions of US dollars)</i>					
4. Floor on change in net international reserves of the central bank 3/	-35	105	-70	-5	-55	20
Cumulative flows from end-June 2010 4/	-45	95	25	90	40	115
5. Continuous ceiling on nonconcessional external debt contracted or guaranteed by the consolidated public sector	0	0	0	0	0	0
6. Continuous ceiling on the accumulation of new external arrears of the combined public sector	0	0	0	0	0	0
Indicative targets						
	<i>(In millions of Córdoba)</i>					
1. Ceiling on central government primary expenditure 5/	29,953	30,439	16,954	16,639	35,460	35,696
2. Floor on poverty-related expenditures of the central government 6/	18,368	18,107	9,645	9,839	21,103	21,064
3. Ceiling on monitorable wage bill	11,288	11,301	6,088	5,924	12,850	13,121
Memorandum items						
Stock of NIR (adjusted, US\$ millions)	776	916	847	911	862	937

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates/projections.

- 1/ Cumulative flows starting at the beginning of the calendar year. Definitions are specified in the TMU, including adjusters.
2/ Adjusted by any excess of project loans for up to US\$15 million in 2010 and US\$55 million in 2011. It is adjusted in 2011 by any use of US\$49.5 million of a grant to ENACAL received in 2009.
3/ Adjusted by shortfalls/excess in budget support external loans compared to programmed levels in both 2010 and 2011.
4/ The targets for NDA and NIR-Adjusted are defined as cumulative flows from June 2010.
5/ Adjusted by any shortfalls/excess in observed grants and project-loans with respect to programmed amounts.
6/ Adjusted for shortfalls/excess in external financing as specified in TMU.

Table 2. Nicaragua. Structural Benchmarks, 2011 1/

		Date	Status
Assembly approval of a regulatory framework for institutions operating in the microfinance industry	SB	End-July 2011	Done
Complete study assessing the scope of productivity gains and rationalizing government employment practices	SB	End-September 2011	In Progress

1/ SB=Structural Benchmark.

Attachment II: Nicaragua—Changes to the Technical Memorandum of Understanding October 3, 2011

All aspects of the Technical Memoranda of Understanding (EBS/07/103, Supplement I; EBS/08/101, Supplement I; EBS/09/157, Supplement I; and EBS/10/198, Annex II; EBS/11/56, Annex II) issued on September 4, 2007, August 28, 2008, October 21, 2009, November 2, 2010, and April 8, 2011, respectively, remain valid, except for the revisions incorporated in the October 3, 2011 letter of intent, and those indicated below.

A. Definitions

1. The monitorable wage bill for 2010-11 includes transfers of US\$31.3 million and US\$44.7 million (of which US\$20.6 million through June 2011) financed through a grant from the Venezuelan cooperation arrangement.¹

B. Quantitative Targets

2. The program targets for the quantitative performance criteria for end-June 2011, as well as projections for end-December 2011, are detailed in Table 1.

TMU Table 1. Nicaragua: Quantitative Performance Criteria and Indicative Targets, 2010-11 ^{1/}

	2010		2011			
	Jan-Dec		Jan-Jun		Jan-Dec	
	Adj.		Adj.			
	Prog.	Prel.	Prog.	Prel.	Prog.	Proj.
Performance Criteria (Jan-Dec 2010, Jan-Jun 2011, indicative targets otherwise)						
	<i>(In millions of Córdobas)</i>					
1. Floor on combined public sector overall balance, after grants 2/	-3,418	-1,982	-1,822	818	-2,896	-1,803
2. Floor on Social Security Institute (INSS) overall balance, after grants	1,415	1,492	982	1,040	1,400	1,431
3. Ceiling on change in net domestic assets of the central bank 3/	1,560	-182	230	-982	2,348	1,098
Cumulative flows from end-June 2010 4/	2,549	807	1,037	-174	3,155	1,905
	<i>(In millions of US dollars)</i>					
4. Floor on change in net international reserves of the central bank 3/	-35	105	-70	-5	-55	20
Cumulative flows from end-June 2010 4/	-45	95	25	90	40	115
5. Continuous ceiling on nonconcessional external debt contracted or guaranteed by the consolidated public sector	0	0	0	0	0	0
6. Continuous ceiling on the accumulation of new external arrears of the combined public sector	0	0	0	0	0	0
Indicative targets						
	<i>(In millions of Córdobas)</i>					
1. Ceiling on central government primary expenditure 5/	29,953	30,439	16,954	16,639	35,460	35,696
2. Floor on poverty-related expenditures of the central government 6/	18,368	18,107	9,645	9,839	21,103	21,064
3. Ceiling on monitorable wage bill	11,288	11,301	6,088	5,924	12,850	13,121
Memorandum items						
Stock of NIR (adjusted, US\$ millions)	776	916	847	911	862	937

Sources: Central Bank of Nicaragua; Ministry of Finance; and Fund staff estimates/projections.

1/ Cumulative flows starting at the beginning of the calendar year. Definitions are specified in the TMU, including adjusters.

2/ Adjusted by any excess of project loans for up to US\$15 million in 2010 and US\$55 million in 2011. It is adjusted in 2011 by any use of US\$49.5 million of a grant to ENACAL received in 2009.

3/ Adjusted by shortfalls/excess in budget support external loans compared to programmed levels in both 2010 and 2011.

4/ The targets for NDA and NIR-Adjusted are defined as cumulative flows from June 2010.

5/ Adjusted by any shortfalls/excess in observed grants and project-loans with respect to programmed amounts.

6/ Adjusted for shortfalls/excess in external financing as specified in TMU.

¹ An analogous treatment will be given to the primary expenditure of the Central Government.

C. Adjustors

3. The adjustors related to the external financing will be applied to the updated projections in Table 2.

TMU Table 2. Programmed External Financing 2010-11
(in millions of US\$)

	External loans	Budget support loans 1/	Project- related loans	of which, Project related loans to CG	External grants 2/	of which, Grants to CG	Budget support grants	Project- related grants	Total financing	Budget support	Project- related
	(a=b+c)	(b)	(c)	(c')	(d=e+f)	(d')	(e)	(f)	(g=a+d)	(h=b+e)	(i=c+f)
Cumulative from January 2010											
Q1-10	35	0	35	26	16	15	1	15	50	1	50
Q2-10	94	0	94	74	44	40	1	44	138	1	137
Q3-10	123	0	123	96	89	83	22	67	212	22	190
Q4-10	266	43	223	162	142	134	22	120	408	65	343
Cumulative from January 2011											
Q1-11	29	0	29	22	18	16	1	17	46	1	46
Q2-11	81	0	81	63	63	57	1	62	144	1	143
Q3-11	149	0	149	109	115	105	1	114	264	1	262
Q4-11	234	45	189	140	166	152	1	165	400	46	354

1/ Excludes IMF.

2/ Excludes extra-budgetary grants to finance wage bonus

4. The indicative target on poverty-reducing spending will be adjusted *downwards* for any shortfalls of external financing related to the poverty programs specified in Table 3. Similarly, the indicative target on poverty-reducing spending will be adjusted *upwards* for any excess of external financing related to the poverty programs specified in Table 3.

TMU Table 3. Nicaragua: Central Government Poverty Spending and Financing, 2010-11
(in C\$ millions)

	2010		2011			
	Jan.-Dec.		Jan.- Jun.		Jan.-Dec.	
	Prog.	Prel.	Adj. Prog.	Prel.	Prog.	Proj.
Poverty Spending	18,919	18,107	9,645	9,839	21,103	21,064
Domestic Financing	10,632	10,371	5,869	6,063	11,900	12,203
External Financing	8,287	7,737	3,776	3,776	9,203	8,861
Grants	2,563	2,294	584	584	2,976	2,789
Loans	2,898	2,642	1,856	1,856	3,000	3,236
Debt Relief	2,826	2,801	1,336	1,336	3,228	2,835

Source: Ministry of Finance and Public Credit.

D. Supplementary Agenda

5. **Study on Central Government employment.** The Ministry of Finance and Public Credit discussed with Fund staff preliminary findings of the study in line with the terms broadly described in Country Report No. 11/144. The final report will be ready before December 2011.

E. Provision of Information and Monitoring

6. **Continued production and publication of reports.** The information described in Section F of Annex II of Country Report No. 10/376 will continue to be provided according to the terms described therein. In particular, the reports described in paragraphs 18, 19, and 21 will continue to be published electronically. The Report on External Aid flows will continue to be published semi-annually in electronic form.

7. **Analysis of the effectiveness of public social spending.** With the aim of measuring the quality of public spending, the Office of Economic Studies at the Ministry of Finance and Public Credit (MFPC) discussed with Fund staff preliminary results on a forthcoming report on the redistributive impact of public expenditures and of aggregate indicators to measure the effectiveness and efficiency of public spending, in line with Country Report No. 11/144. The final version of the study will be available before December 2011.

Annex I: Update of Debt Sustainability Analysis¹

October 6, 2011

*Based on the joint Low-Income Country Debt Sustainability Framework of the World Bank and the IMF, Nicaragua's Debt Sustainability Analysis (DSA) has been updated to reflect developments in the period following the global financial crisis. Nicaragua maintains a **moderate risk** of external public debt distress, with vulnerabilities arising from worsening financing terms and a historical scenario that indicates significant risks should growth and the envisaged external adjustment not materialize. Total external debt (public and private) continues to appear sustainable in the medium term. Nicaragua was recently reclassified as a medium performer.*

I. ASSUMPTIONS AND DEVELOPMENTS IN TOTAL DEBT

1. **Assumptions.** Key macroeconomic assumptions were revised in the context of the seventh review of Nicaragua's ECF taking into account developments through mid-2011. Over the medium term, the baseline scenario envisages an external adjustment driven by a diversification of energy consumption away from imported oil to domestically generated renewable energy and continued fiscal prudence. Box 1 summarizes the key assumptions.
2. **External debt restructuring.** After reaching the completion point in 2004, Nicaragua received substantial debt relief under the HIPC and MDRI initiatives. Some progress has been made since then in formalizing debt relief from non-Paris Club creditors and in restructuring private commercial debt. At end-2010, the debt to non-Paris Club bilateral creditors pending relief stood at US\$1.6 billion (24 percent of GDP and 40 percent of outstanding external debt).

II. EXTERNAL PUBLIC DEBT SUSTAINABILITY

3. **Under the baseline scenario all external public debt indicators remain below the policy-dependent thresholds.** Nicaragua was recently reclassified as a medium performer in terms of policies and institutional quality,² which lowers the debt-burden thresholds relevant for the DSA.³ Notwithstanding this change, all external debt indicators remain below the indicative

¹ This appendix was prepared in the context of the 7th review of the ECF arrangement that took place during August–September, 2011. It updates the last full joint Bank-Fund DSA conducted in June 2010 (SM/10/156, Supplement 1). A post-mortem of the June 2010 DSA is not included given that its assumptions and conclusions are broadly unchanged.

² Policy and institutional quality is measured using a three-year moving average of the World Bank's Country Policy and Institutional Assessment Index (CPIA) which has fallen for two consecutive years, crossing the threshold between the medium and strong performance categories. Nicaragua's 2010 CPIA results reflect governance concerns. The country sustains strong performances on macroeconomic, fiscal and social indicators.

³ This reclassification reduces, among other things, the threshold for the PV of external public debt-to-GDP from 50 to 40 percent.

risk thresholds for debt distress and are expected to improve over the 20-year projection period (Table 1 and Figure 1).

Box 1. Assumptions in the Baseline Scenario

Real economic activity has recovered and real GDP is projected to grow at 4 percent in 2011. Activity is projected to slow to 3.3 percent in 2012 owing to weak external demand, before recovering to its long-term growth rate (4 percent).

The (non-interest) external current account deficit is expected to narrow gradually, from an average of 15 percent of GDP during 2005-10, to an average deficit of about 6 percent of GDP during 2026-2031, as a result of lower oil dependency as large renewable energy projects start operating.

Non-Paris Club bilateral debt is assumed to be settled on HIPC-equivalent terms by end-2011. Such restructuring would generate debt relief of about 13 percent of GDP in 2011.

Official external assistance (loans and grants to the public sector) is expected to decline from an average of 8 percent of GDP during 2006–10 to around 1 percent during 2026–31. Net official external borrowing (in concessional terms) is projected to average 3 percent of GDP during 2011-15, falling gradually over the medium term.

The deficit of the consolidated public sector (CPS) is projected to decline gradually in the coming years as the central government balance improves and the central bank reduces its operating deficit. The CPS deficit is expected to increase again in the medium term as the surpluses posted by the *Instituto Nacional de Seguridad Social* (INSS) are followed by increasing deficits (under a no reform scenario).

4. **External public debt service flows are expected to remain manageable.** External public debt service ratios are expected to remain well below the relevant thresholds reflecting the high concessionality of existing and prospective public external debt. Highly concessional borrowing is projected to decline gradually over the medium- and long-term as Nicaragua gains access to borrowing under commercial terms (see Figure 1).⁴ The present value (PV) of public external debt stays at around 34 percent of GDP until 2015 and gradually declines in the following years.

5. **Standard stress tests reveal some vulnerabilities.** The "historical scenario" corresponds to a situation where the envisaged large investments in the energy sector and infrastructure do not result in a sustained increase in output growth or a decline in oil imports, and assumes that the public sector borrows to avoid an external financing gap. Under such circumstances, the non-interest current account deficit remains at its 2001–10 average level of about 15 percent of GDP, and the PV of the external-debt-to-GDP ratio increases without bound, breaching the 40 percent of GDP threshold by 2014. All debt service ratios, however, remain well below the distress thresholds. Under the standardized bound test of a "terms shock"⁵ in 2012, the PV of the

⁴ The temporary decline of the grant element in 2012-14 reflects the slightly lower concessionality of the large financing provided for the country's energy program.

⁵ The terms shock assumes that the interest rate on new borrowing is 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

external-debt-to-GDP ratio marginally breaches the 40 percent of GDP threshold during most of the projection period, gradually declining by the end of the horizon. The breach under the exchange rate shock is also protracted but front-loaded, reaching 47 percent in 2012 and falling below the threshold in 2021.

6. **Private external debt at end-2010 stood at US\$2.9 billion (44 percent of GDP).**⁶ Non-financial institutions account for almost one half of this debt, while the concessional financing provided by Venezuela under the auspices of the *Alternativa Bolivariana de las Americas* (ALBA), and channeled through a private cooperative, represent almost 40 percent. The remainder corresponds to debt of non-public financial institutions.

IV. PUBLIC DEBT SUSTAINABILITY

7. **The public debt to GDP ratio is projected to decline over the medium term.** The PV of public debt is estimated to remain stable at about 50 percent of GDP through 2014 and then to fall (to 26 percent by 2031) as a result of continued fiscal consolidation and GDP growth in line with potential. Total debt service remains below 25 percent of total revenue throughout the projection period. Continued external financing on concessional terms allows for the reduction of market-based, expensive, domestic debt. By the end of the projection horizon, pressures from the social security system begin to arise, even under the baseline assumption of fiscal discipline.

8. **Nicaragua's public domestic debt is denominated in foreign currency, and thus particularly sensitive to exchange rate shocks.** The stress tests indicate that a one-time 30 percent depreciation in 2012 would increase the PV of public debt-to-GDP and the PV of public debt-to-revenues by about 20 and 100 percentage points, respectively; the debt service-to-revenue ratio would also deteriorate significantly, reaching one-third in 2015 and falling afterwards.

V. CONCLUSION

9. **Nicaragua faces a moderate risk of external public debt distress.** No indicative policy-dependent threshold is breached under the baseline scenario. However, the historical scenario underscores the importance of reducing oil dependency and maintaining strong exports. Moreover, despite the assumed continued fiscal restraint, the pressures arising from the social security system start affecting the public debt dynamics noticeably towards the end of the projection period, illustrating the importance of a fundamental reform of the INSS.

10. **The authorities were in broad agreement with these conclusions and with the thrust of the analysis and the main results.** In particular, they agreed that it is imperative to strengthen the pension system and to continue transforming the country's energy matrix over the medium

⁶ This estimate is considerably larger than the one reported in the previous DSA (US\$1.7 billion as of end - 2009). The difference can be accounted for by improvements in the methodology and increases in the coverage for private external debt.

term. However, the authorities considered that the medium-term growth rate used in the analysis was too low. They questioned the realism of assuming that only public sector borrowing would be used to avoid an external financing gap in the “historical” scenario.

Table 1: Nicaragua: External Debt Sustainability Framework, Baseline Scenario, 2008-2031 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average	Standard Deviation	Projections						2011-2031		
	2008	2009	2010			2011	2012	2013	2014	2015	2016	Average	2021	2031
External debt (nominal) 1/	88.9	98.2	104.5			93.3	96.1	99.6	101.8	103.4	101.7		88.7	57.1
o/w public and publicly guaranteed (PPG)	56.5	60.4	60.6			45.2	46.3	47.2	47.3	46.9	46.4		42.6	32.6
Change in external debt	-1.7	9.3	6.3			-11.3	2.8	3.5	2.2	1.5	-1.6		-3.0	-2.4
Identified net debt-creating flows	4.7	8.7	2.0			1.4	4.7	5.6	4.2	3.5	0.2		-1.2	-1.5
Non-interest current account deficit	24.0	11.1	12.8	14.8	3.7	13.4	15.5	15.3	13.9	12.7	9.2		6.8	6.3
Deficit in balance of goods and services	38.8	27.2	28.4			28.6	29.6	28.0	25.9	24.2	20.3		15.7	12.1
Exports	46.9	46.4	55.4			64.2	67.3	67.1	67.0	66.9	66.9		66.6	66.2
Imports	85.7	73.6	83.7			92.8	96.9	95.1	92.9	91.1	87.2		82.3	78.3
Net current transfers (negative = inflow)	-24.2	-24.4	-21.0	-23.1	2.2	-19.6	-17.8	-17.0	-16.3	-15.6	-14.8		-11.2	-7.6
o/w official	-5.5	-4.8	-2.8			-3.0	-2.5	-2.3	-2.1	-1.9	-1.8		-0.9	-0.2
Other current account flows (negative = net inflow)	9.4	8.4	5.4			4.4	3.7	4.4	4.3	4.1	3.7		2.3	1.8
Net FDI (negative = inflow)	-9.8	-7.0	-7.8	-6.2	1.6	-10.5	-10.8	-8.8	-8.7	-8.6	-8.5		-8.0	-7.5
Endogenous debt dynamics 2/	-9.4	4.6	-3.0			-1.5	0.0	-1.0	-1.0	-0.6	-0.5		0.0	-0.3
Contribution from nominal interest rate	0.6	2.3	2.0			2.3	2.9	2.6	2.7	3.2	3.4		3.4	1.9
Contribution from real GDP growth	-2.2	1.3	-4.2			-3.9	-2.9	-3.6	-3.8	-3.8	-3.9		-3.5	-2.3
Contribution from price and exchange rate changes	-7.9	0.9	-0.9			...	...	...	...	...	...		...	...
Residual (3-4) 3/	-6.4	0.6	4.3			-12.7	-1.9	-2.1	-2.0	-2.0	-1.8		-1.8	-0.9
o/w exceptional financing	-1.1	-0.6	-0.5			-13.7	-0.1	-0.1	-0.1	-0.1	-0.1		0.0	0.0
PV of external debt 4/	...	...	77.7			81.3	83.7	86.9	88.9	90.1	88.2		74.6	44.8
In percent of exports	...	...	140.4			126.6	124.4	129.4	132.7	134.6	131.9		111.9	67.7
PV of PPG external debt	...	...	33.8			33.2	33.9	34.5	34.4	33.7	32.9		28.4	20.2
In percent of exports	...	...	61.1			51.7	50.4	51.4	51.4	50.3	49.2		42.7	30.6
In percent of government revenues	...	...	171.6			157.6	157.8	160.0	159.8	155.6	151.6		128.1	89.7
Debt service-to-exports ratio (in percent)	20.4	18.8	16.2			11.8	12.5	9.6	9.7	11.1	11.4		12.6	9.9
PPG debt service-to-exports ratio (in percent)	3.9	4.1	2.7			2.1	2.3	2.4	2.6	3.2	3.3		3.1	2.7
PPG debt service-to-revenue ratio (in percent)	9.6	10.2	7.5			6.4	7.3	7.5	8.2	9.9	10.2		9.3	8.0
Total gross financing need (Millions of U.S. dollars)	1982.6	1224.4	1308.5			1160.4	1388.8	1438.2	1397.9	1441.7	1201.6		1324.5	1608.1
Non-interest current account deficit that stabilizes debt ratio	25.7	1.8	6.5			24.7	12.7	11.8	11.7	11.2	10.8		9.8	8.7
Key macroeconomic assumptions														
Real GDP growth (in percent)	2.8	-1.5	4.5	2.9	2.0	4.0	3.3	4.0	4.0	4.0	4.0	3.9	4.0	4.0
GDP deflator in US dollar terms (change in percent)	9.5	-1.0	0.9	2.3	3.5	3.9	1.7	2.2	2.0	1.9	1.9	2.3	1.9	0.9
Effective interest rate (percent) 5/	0.8	2.5	2.2	1.7	0.7	2.4	3.3	2.9	2.9	3.3	3.5	3.0	4.0	3.4
Growth of exports of G&S (US dollar terms, in percent)	10.4	-3.5	25.7	13.1	10.4	25.2	10.1	6.0	5.9	5.9	5.9	9.8	5.9	5.0
Growth of imports of G&S (US dollar terms, in percent)	17.7	-16.2	20.0	10.5	11.8	19.7	9.7	4.3	3.6	4.0	1.4	7.1	5.0	5.3
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	47.3	42.0	38.3	40.6	42.3	40.4	41.8	38.2	19.3
Government revenues (excluding grants, in percent of GDP)	19.0	18.9	19.7			21.1	21.5	21.6	21.6	21.7	21.7		22.2	22.6
Aid flows (in Millions of US dollars) 7/	404.0	481.6	449.3			345.5	333.1	327.9	329.2	329.0	317.7		275.8	110.9
o/w Grants	184.5	151.4	164.1			206.7	164.1	159.1	154.6	150.1	143.0		91.4	19.3
o/w Concessional loans	219.5	330.2	285.2			138.8	169.0	168.8	174.6	178.9	174.7		184.4	91.7
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			4.7	4.1	3.8	3.5	3.2	2.9		1.8	0.4
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			70.5	61.4	56.7	59.3	60.9	58.6		50.9	23.4
Memorandum items:														
Nominal GDP (Millions of US dollars)	6372.2	6213.8	6551.5			7077.6	7435.4	7902.2	8383.5	8884.9	9416.3		12589.8	22185.4
Nominal dollar GDP growth	12.5	-2.5	5.4			8.0	5.1	6.3	6.1	6.0	6.0	6.2	6.0	5.0
PV of PPG external debt (in Millions of US dollars)			2162.4			2294.2	2459.8	2660.4	2818.9	2923.0	3023.6		3495.4	4360.8
(PVt-PVt-1)/GDPt-1 (in percent)						2.0	2.3	2.7	2.0	1.2	1.1	1.9	0.8	0.3
Gross workers' remittances (Millions of US dollars)	818.1	768.4	822.8			880.6	907.0	939.6	975.9	1012.1	1049.0		1245.2	1639.7
PV of PPG external debt (in percent of GDP + remittances)	...	...	30.0			29.5	30.2	30.8	30.9	30.3	29.6		25.9	18.8
PV of PPG external debt (in percent of exports + remittances)	...	...	49.8			43.3	42.6	43.7	43.8	43.0	42.2		37.2	27.5
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.2			1.8	2.0	2.1	2.2	2.7	2.8		2.7	2.5

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt. Historical estimates of debt have been revised (upwards) by the Central Bank of Nicaragua. The projections assume that outstanding debt to non-Paris Club bilateral creditors is settled on HIPC-equivalent terms by end-2011.

2/ Derived as $[r - g - \rho(1+g)] / (1+g+p+gp)$ times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2a.Nicaragua: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2011-2031
(In percent)

	Projections							
	2011	2012	2013	2014	2015	2016	2021	2031
PV of debt-to GDP ratio								
Baseline	33	34	34	34	34	33	28	20
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	33	36	38	41	44	49	78	136
A2. New public sector loans on less favorable terms in 2011-2031 2/	33	35	37	39	39	40	41	40
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	33	34	35	35	35	34	29	20
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	33	37	42	42	41	40	34	24
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	33	34	36	36	35	34	29	20
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	33	36	36	36	35	35	30	21
B5. Combination of B1-B4 using one-half standard deviation shocks	33	36	39	38	38	37	32	22
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	33	47	48	48	47	45	39	27
PV of debt-to-exports ratio								
Baseline	52	50	51	51	50	49	43	31
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	52	54	57	61	65	73	117	205
A2. New public sector loans on less favorable terms in 2011-2031 2/	52	52	55	58	59	59	62	60
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	52	49	50	50	49	48	41	29
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	52	58	69	69	67	66	57	40
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	52	49	50	50	49	48	41	29
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	52	53	54	54	53	52	45	31
B5. Combination of B1-B4 using one-half standard deviation shocks	52	54	54	54	53	52	45	31
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	52	49	50	50	49	48	41	29
PV of debt-to-revenue ratio								
Baseline	158	158	160	160	156	152	128	90
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	158	168	178	190	202	226	352	601
A2. New public sector loans on less favorable terms in 2011-2031 2/	158	162	172	179	181	183	186	176
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	158	158	165	164	160	155	131	90
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	158	170	195	193	188	183	154	107
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	158	158	166	166	161	157	132	91
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	158	166	169	168	163	159	134	92
B5. Combination of B1-B4 using one-half standard deviation shocks	158	170	179	178	173	169	142	98
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	158	218	221	221	215	209	176	121

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 2b.Nicaragua: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2011-2031 (continued)
(In percent)

	Projections							
	2011	2012	2013	2014	2015	2016	2021	2031
Debt service-to-exports ratio								
Baseline	2	2	2	3	3	3	3	3
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	2	2	3	3	4	4	5	8
A2. New public sector loans on less favorable terms in 2011-2031 2/	2	2	2	3	3	4	3	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	2	2	2	3	3	3	3	3
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	2	2	3	3	4	4	4	4
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	2	2	2	3	3	3	3	3
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	2	2	3	3	3	3	3	3
B5. Combination of B1-B4 using one-half standard deviation shocks	2	2	3	3	3	3	3	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	2	2	2	3	3	3	3	3
Debt service-to-revenue ratio								
Baseline	6	7	8	8	10	10	9	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	6	7	8	9	11	12	16	24
A2. New public sector loans on less favorable terms in 2011-2031 2/	6	7	7	8	11	11	10	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	6	7	8	9	10	11	10	8
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	6	7	8	9	11	11	10	10
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	6	7	8	9	11	11	10	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	6	7	8	9	10	11	10	9
B5. Combination of B1-B4 using one-half standard deviation shocks	6	7	8	9	11	11	10	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	6	10	11	12	14	15	13	11
<i>Memorandum item:</i>								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	23	23	23	23	23	23	23	23

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3. Nicaragua: Public Sector Debt Sustainability Framework, Baseline Scenario, 2008-2031
(In percent of GDP, unless otherwise indicated)

	Actual			Average	s/ Standard Deviation	Estimate						Projections				
	2008	2009	2010			2011	2012	2013	2014	2015	2016	2011-16 Average	2021	2031	2017-31 Average	
Public sector debt 1/ o/w foreign-currency denominated	74.3	80.0	81.8			63.4	64.0	63.7	63.3	61.6	59.8		51.2	38.4		
	74.3	80.0	81.8			63.4	64.0	63.7	63.3	61.6	59.8		51.2	38.4		
Change in public sector debt	-7.3	5.7	1.8			-18.3	0.6	-0.3	-0.4	-1.7	-1.8		-1.7	-0.4		
Identified debt-creating flows	-7.8	3.9	-2.5			-18.1	-0.5	-1.6	-2.0	-1.9	-1.9		-1.5	0.5		
Primary deficit	0.1	1.4	0.1	-0.6	1.7	-0.4	0.4	0.2	0.2	-1.1	-0.4	-0.2	0.0	1.1	0.2	
Revenue and grants	21.9	21.3	22.2			24.0	23.7	23.6	23.4	23.3	23.2		22.9	22.6		
of which: grants	2.9	2.4	2.5			2.9	2.2	2.0	1.8	1.7	1.5		0.7	0.1		
Primary (noninterest) expenditure	22.0	22.7	22.3			23.6	24.1	23.8	23.6	22.3	22.8		22.9	23.7		
Automatic debt dynamics	-7.6	3.6	-2.7			-4.5	-1.4	-2.2	-2.1	-0.8	-1.5		-1.4	-0.6		
Contribution from interest rate/growth differential	-2.4	2.0	-2.9			-3.2	-1.0	-1.5	-1.4	-0.4	-1.2		-1.2	-0.8		
of which: contribution from average real interest rate	-0.2	0.9	0.5			-0.1	1.1	1.0	1.0	2.0	1.2		0.8	0.7		
of which: contribution from real GDP growth	-2.2	1.1	-3.4			-3.1	-2.0	-2.5	-2.4	-2.4	-2.4		-2.0	-1.5		
Contribution from real exchange rate depreciation	-5.3	1.6	0.2			-1.3	-0.5	-0.8	-0.7	-0.4	-0.3		...	...
Other identified debt-creating flows	-0.2	-1.1	0.2			-13.2	0.5	0.4	-0.1	-0.1	-0.1		0.0	0.0		
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
Recognition of implicit or contingent liabilities	0.3	0.7	0.6			0.6	0.5	0.5	0.0	0.0	0.0		0.0	0.0		
Debt relief (HIPC and other)	-0.5	-1.7	-0.5			-13.7	-0.1	-0.1	-0.1	-0.1	-0.1		0.0	0.0		
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
Residual, including asset changes	0.5	1.8	4.4			-0.3	1.1	1.3	1.6	0.2	0.2		-0.2	-0.9		
Other Sustainability Indicators																
PV of public sector debt	...	...	55.0			51.5	51.6	51.0	50.4	48.4	46.3		37.0	26.1	
o/w foreign-currency denominated	...	...	55.0			51.5	51.6	51.0	50.4	48.4	46.3		37.0	26.1	
o/w external	...	...	33.8			33.2	33.9	34.5	34.4	33.7	32.9		28.4	20.2	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...
Gross financing need 2/	6.0	7.5	6.6			7.5	8.9	7.9	6.7	6.5	6.0		4.3	3.8		
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	247.6			214.5	217.8	216.3	215.6	207.2	199.4		161.4	115.1	
PV of public sector debt-to-revenue ratio (in percent)	...	...	279.0			244.3	240.2	236.5	234.0	223.4	213.4		166.7	115.6	
o/w external 3/	...	...	171.6			157.6	157.8	160.0	159.8	155.6	151.6		128.1	89.7	
Debt service-to-revenue and grants ratio (in percent) 4/	23.6	22.7	19.8			15.6	21.6	20.9	18.4	24.7	21.7		16.7	11.9		
Debt service-to-revenue ratio (in percent) 4/	27.2	25.7	22.3			17.8	23.8	22.8	19.9	26.7	23.2		17.2	11.9		
Primary deficit that stabilizes the debt-to-GDP ratio	7.4	-4.3	-1.8			18.0	-0.1	0.5	0.6	0.6	1.4		1.7	1.5		
Key macroeconomic and fiscal assumptions																
Real GDP growth (in percent)	2.8	-1.5	4.5	2.9	2.0	4.0	3.3	4.0	4.0	4.0	4.0	3.9	4.0	4.0	4.0	
Average nominal interest rate on forex debt (in percent)	2.0	2.2	1.8	2.3	0.6	2.1	2.7	2.6	2.6	4.6	3.5	3.0	3.2	3.3	3.4	
Average real interest rate on domestic debt (in percent)	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Real exchange rate depreciation (in percent, + indicates depreciation)	-6.7	2.1	0.2	0.0	3.0	-1.7	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	15.0	3.9	6.0	7.8	3.4	9.1	6.8	7.3	7.1	7.0	7.0	7.4	7.0	7.0	7.0	
Growth of real primary spending (deflated by GDP deflator, in percent)	0.1	0.0	0.0	0.0	0.1	0.1	0.1	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	
Grant element of new external borrowing (in percent)	...	...	...	...	...	47.3	42.0	38.3	40.6	42.3	40.4	41.8	38.2	19.3	

Sources: Country authorities; and staff estimates and projections.

1/ Public debt refers to the gross debt of the Consolidated Public Sector. The projections assume that the outstanding debt to non-Paris Club bilateral creditors is settled on HIPC-equivalent terms by end-2011.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4. Nicaragua: Sensitivity Analysis for Key Indicators of Public Debt 2011-2031

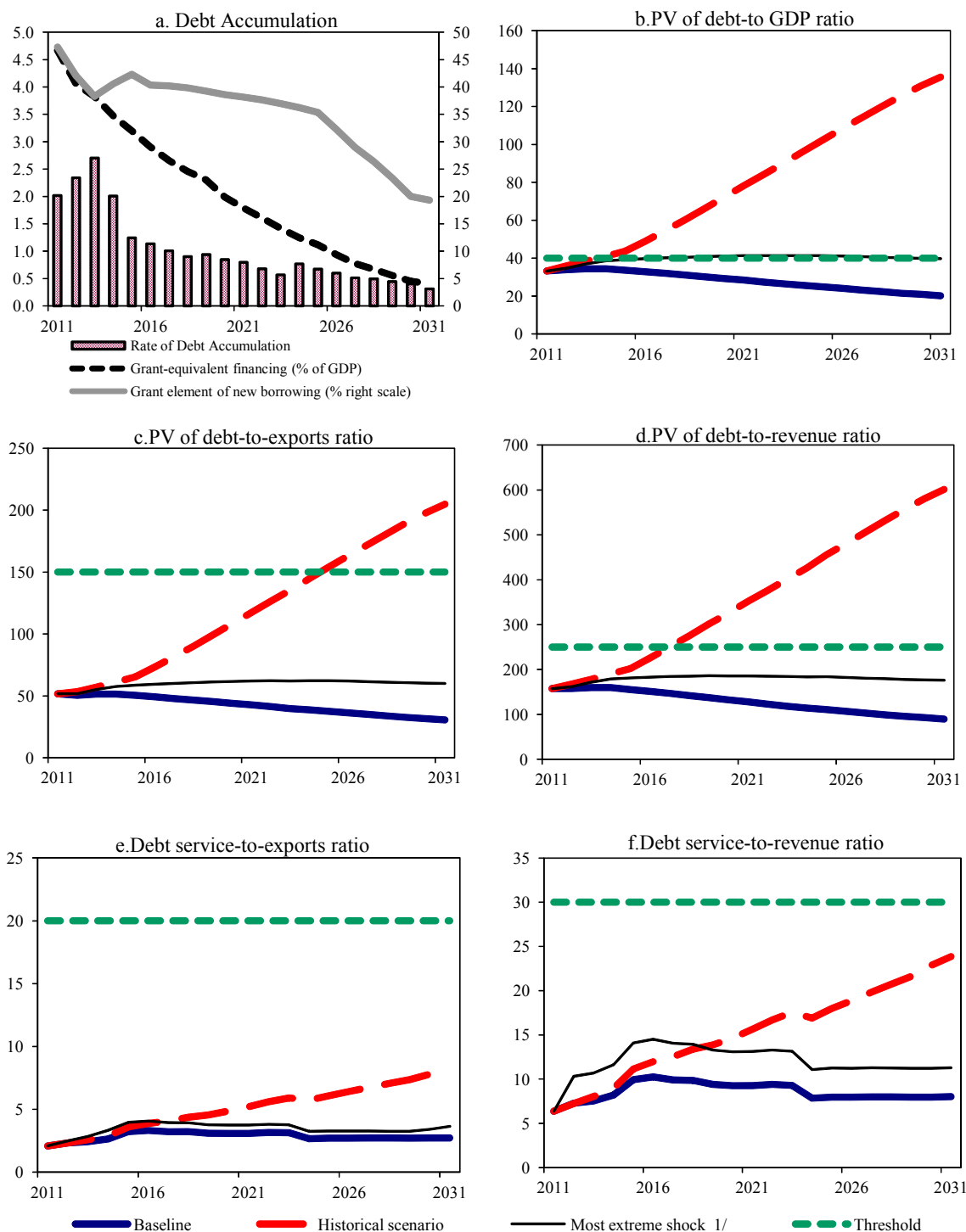
	Projections							
	2011	2012	2013	2014	2015	2016	2021	2031
PV of Debt-to-GDP Ratio								
Baseline	51	52	51	50	48	46	37	26
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	51	51	50	49	48	46	37	17
A2. Primary balance is unchanged from 2011	51	51	50	48	47	45	35	16
A3. Permanently lower GDP growth 1/	51	52	52	52	50	49	44	48
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	51	53	55	56	55	54	50	48
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	51	52	53	52	50	48	38	27
B3. Combination of B1-B2 using one half standard deviation shocks	51	52	53	53	51	50	44	39
B4. One-time 30 percent real depreciation in 2012	51	75	73	72	70	68	58	50
B5. 10 percent of GDP increase in other debt-creating flows in 2012	51	62	61	60	58	56	46	33
PV of Debt-to-Revenue Ratio 2/								
Baseline	215	218	216	216	207	199	161	115
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	215	214	211	209	205	199	159	76
A2. Primary balance is unchanged from 2011	215	214	210	207	202	194	151	73
A3. Permanently lower GDP growth 1/	215	219	219	221	215	209	190	210
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	215	225	234	239	235	232	216	212
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	215	221	223	222	214	206	168	120
B3. Combination of B1-B2 using one half standard deviation shocks	215	220	222	225	220	215	191	172
B4. One-time 30 percent real depreciation in 2012	215	317	311	308	299	291	252	219
B5. 10 percent of GDP increase in other debt-creating flows in 2012	215	260	258	257	248	240	199	147
Debt Service-to-Revenue Ratio 2/								
Baseline	16	22	21	18	25	22	17	12
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	16	22	21	18	25	22	18	11
A2. Primary balance is unchanged from 2011	16	22	21	18	24	21	16	10
A3. Permanently lower GDP growth 1/	16	22	21	19	25	22	18	17
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	16	22	22	20	26	23	19	18
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	16	22	21	19	25	22	17	12
B3. Combination of B1-B2 using one half standard deviation shocks	16	22	22	19	26	23	18	15
B4. One-time 30 percent real depreciation in 2012	16	24	26	24	33	29	24	22
B5. 10 percent of GDP increase in other debt-creating flows in 2012	16	22	23	20	26	23	18	15

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

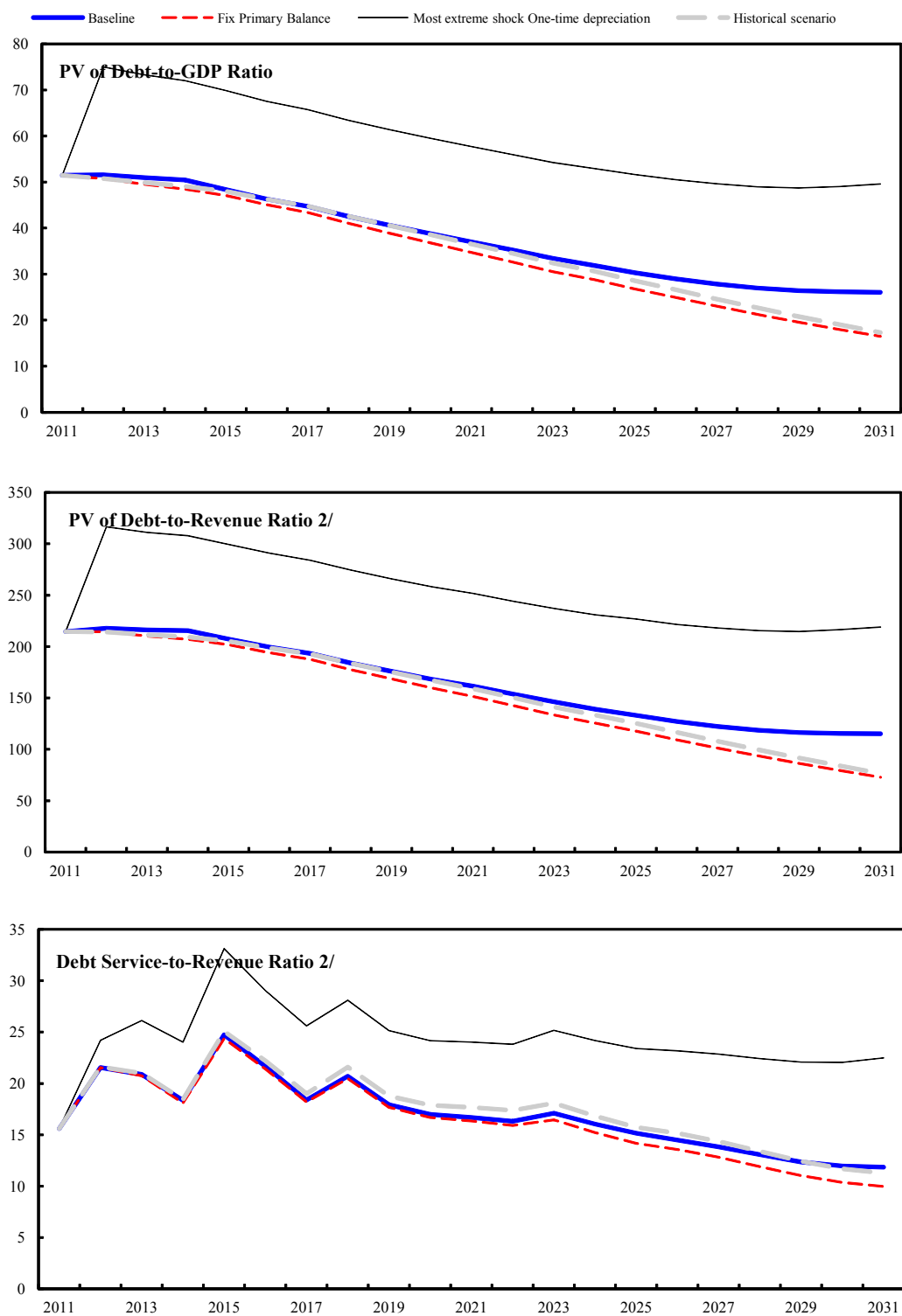
Figure 1. Nicaragua: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2011-2031 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2021. In figure b. it corresponds to a Terms shock; in c. to a Terms shock; in d. to a Terms shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Figure 2. Nicaragua: Indicators of Public Debt Under Alternative Scenarios, 2011-2031 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2021.

2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND

NICARAGUA

**Seventh Review Under the Extended Credit Facility and Financing Assurances Review—
Informational Annex**

Prepared by the Western Hemisphere Department

October 6, 2011

	Contents	Page
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Annex I–Relations with the Fund
(As of August 31, 2011)

I. Membership Status: Joined: March 14, 1946;

Article VIII

II. General Resources Account:	SDR Million	%Quota
<u>Quota</u>	130.00	100.00
<u>Fund holdings of currency (Exchange Rate)</u>	130.01	100.01
<u>Reserve Tranche Position</u>	0.00	0.00

III. SDR Department:	SDR Million	%Allocation
<u>Net cumulative allocation</u>	124.54	100.00
<u>Holdings</u>	108.95	87.48

IV. Outstanding Purchases and Loans:	SDR Million	%Quota
ECF Arrangements	112.84	86.80

V. Latest Financial Arrangements:

<u>Type</u>	<u>Date of Arrangement</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
ECF ^{1/}	Oct 05, 2007	Dec 04, 2011	78.00	72.45
ECF ^{1/}	Dec 13, 2002	Dec 12, 2006	97.50	97.50
ECF ^{1/}	Mar 18, 1998	Mar 17, 2002	148.96	115.32

^{1/} Formerly PRGF.

VI. Projected Payments to Fund ^{2/}

(SDR Million; based on existing use of resources and present holdings of SDRs):

	<u>Forthcoming</u>				
	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Principal		8.36	10.74	14.42	19.18
Charges/Interest	<u>0.02</u>	<u>0.33</u>	<u>0.31</u>	<u>0.28</u>	<u>0.24</u>
Total	<u>0.02</u>	<u>8.69</u>	<u>11.04</u>	<u>14.69</u>	<u>19.41</u>

^{2/} When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

VII. Implementation of HIPC Initiative:

	<u>Enhanced Framework</u>
I. Commitment of HIPC assistance	
Decision point date	Dec 2000
Assistance committed	
by all creditors (US\$ Million) ^{1/}	3,308.00
Of which: IMF assistance (US\$ million)	82.20
(SDR equivalent in millions)	63.54

Completion point date	Jan 2004
II. Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	63.54
Interim assistance	2.55
Completion point balance	60.99
Additional disbursement of interest income ^{2/}	7.62
Total disbursements	71.16

^{1/} Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

^{2/} Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI):

I.	MDRI-eligible debt (SDR Million) ^{1/}	140.48
	Financed by: MDRI Trust	91.79
	Remaining HIPC resources	48.70
II.	Debt Relief by Facility (SDR Million)	

<u>Delivery</u> <u>Date</u>	<u>Eligible Debt</u>		
	<u>GRA</u>	<u>PRGT</u>	<u>Total</u>
January 2006	N/A	140.48	140.48

^{1/} The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

IX. Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

Decision point - point at which the IMF and the World Bank determine whether a country qualifies for assistance under the HIPC Initiative and decide on the amount of assistance to be committed.

Interim assistance - amount disbursed to a country during the period between decision and completion points, up to 20 percent annually and 60 percent in total of the assistance committed at the decision point (or 25 percent and 75 percent, respectively, in exceptional circumstances).

Completion point - point at which a country receives the remaining balance of its assistance committed at the decision point, together with an additional disbursement of interest income as defined in footnote 2 above. The timing of the completion point is linked to the implementation of pre-agreed key structural reforms (i.e., floating completion point).

X. EXCHANGE RATE ARRANGEMENTS:

In December 1995, the Monetary Board of the central bank approved the unification of the exchange rate system effective January 1, 1996. With the unification of the exchange rate, all previous exchange restrictions on payments and transfers for current international transactions and multiple currency practices were eliminated. The central bank buys/sells any amount of foreign currency from/to financial institutions at the official exchange rate, and implements a crawling peg system. Since December 2004, the monthly crawl has been set at an annual rate of 5 percent. As of October 5, 2011, the exchange rate in the official market was C\$22.7110 per U.S. dollar.

XI. ARTICLE IV CONSULTATION:

The last consultation was completed by the Executive Board on July 9, 2010, (SM/10/156). It is expected that the next Article IV consultation with Nicaragua will be held on a standard 24-month cycle subject to the provisions of the decision on consultation cycles approved by the Board on July 15, 2002.

XII. FSAP PARTICIPATION:

An FSAP update was completed in October 2009, and the Financial System Stability Assessment report for Nicaragua was issued on April 28, 2010.

XIII. TECHNICAL ASSISTANCE:

Nicaragua has received substantial technical assistance. The schedule below details assistance provided since 2007.

Dept.	Purpose	Time of Delivery
FAD	Tax Policy (revision of the tax system)	August 2011
FAD	Public Financial Management (Performance budgeting)	April 2011
FAD	Customs Revenue Administration (CAPTAC, follow-up)	March 2011
FAD	Revenue administration (CAPTAC, follow-up)	November 2010
FAD	Customs Revenue administration (CAPTAC)	September 2010
FAD	Revenue administration (CAPTAC, follow-up)	September 2010
FAD	Revenue Administration Audit (CAPTAC)	May 2010
FAD	Follow-up on pension reform	April 2010
FAD	Public financial management (performance budgeting)	April 2010
FAD	Revenue administration (CAPTAC, follow-up)	February 2010
FAD	Revenue administration assessment (CAPTAC)	November 2009
FAD	Public Financial Management (joint with WB)	May 2009
FAD	Public Financial Management (Diagnostic mission)	March 2007
MCM	Risk-based Supervision	July 2011
MCM	Risk-based Supervision	May 2011
MCM	Financial Sector Supervision	March 2011
MCM		February 2011

MCM	Training on stress-testing	October 2010
MCM	Financial sector supervision	October 2010
MCM	Risk-based Supervision	August 2010
MCM	Monetary policy- Liquidity forecasting	August 2010
MCM	Risk-based Supervision	April 2010
MCM	Risk-based Supervision	April 2010
MCM	MTDS follow up	March 2010
MCM	Financial sector supervision	January 2010
MCM	Risk-based Supervision	December 2009
MCM	Risk-based Supervision	November 2009
MCM	Risk-based Supervision	October 2009
MCM	FSAP update mission	September 2009
MCM	Risk-based Supervision	August 2009
MCM	Pre-FSAP mission	July 2008
MCM	Medium-term debt strategy	April 2008
MCM	Central Bank Independence and Recapitalization	September 2007
MCM	Regional Project of Harmonization of Monetary and Financial Statistics in Central America and the Dominican Republic	March 2007
STA	Government finance statistics	October 2011
STA	Balance of payments statistics	October 2011
STA	Government finance statistics	April 2011
STA	Balance of payments statistics	February 2011
STA	National accounts	January 2011
STA	Government finance statistics	October 2010
STA	Balance of payments statistics	October 2010
STA	Producer price index	September 2010
STA	International Investment Position	March 2010
STA	Government finance statistics	February 2010
STA	Balance of payments, international investment position	April 2009
STA	Producer price index	December 2008
STA	Monetary statistics	April 2008
STA	National accounts	January 2008
STA	Producer price index	September 2007
STA	Monetary statistics	February 2007

XIV. RESIDENT REPRESENTATIVE:

Mr. Gabriel Di Bella assumed the position of Resident Representative in Nicaragua in February 2010.

Annex II– Nicaragua: Bank-Fund Country Level Joint Managerial Action Plan, 2010-11¹

Products	Mission timing	Expected delivery
A. Mutual information on relevant work programs		
The Fund work program		
Strategy: The IMF-supported program entails macroeconomic policies anchored on containing expenditures, paving the way for fiscal consolidation, and protecting the external position. It also includes measures to improve the monitoring and reporting on the sources and uses of foreign aid flows. Technical assistance will focus on tax administration, improving financial regulation and oversight, and on improvements in statistics.		
Sixth Review	End-February 2011	Board discussion in April 2011
Seventh Review	September 2011	Board discussion in October 2011
FAD TA: Revenue administration (general assessment)	October 2011	Aide-memoire at the end of the mission
MCM TA: Risk-based Supervision	Sept 19, and Nov. 2011	TA report at the end of the final mission
MCM TA: Monetary and Foreign Exchange	Oct. and Dec. 2011	TA report at the end of the final mission
MCM TA: Payment System and Modernization	Oct. and Nov. 2011	TA report at the end of the final mission
MCM TA: Bank Supervision and Regulation	November 2011	TA report at the end of the final mission
MCM TA: Cash Management	December 2011	TA report at the end of the final mission
STA: SDDS Assessment	November 2011	Aide-memoire at the end of the mission
STA: CAPTAC Export and Import Price Index and Producer Price	December 2011	TA report at the end of the final mission
The World Bank program		
Strategy: The Bank's operations and analytical activities under the Country Assistance Strategy 2008-2012 will aim at stimulating productivity and competitiveness, developing human capital (improving social equity and opportunity) and strengthening governance and accountability. Additionally, to complement fiscal consolidation and improved public financial management, the Bank will support the government in removing bottlenecks to inclusive growth and development.		
A. Lending		
A.1. Support to the Education Sector Project II	September , 2011	Board presentation by December 2011
A.2. Rural Roads Infrastructure Improvement Project	September , 2011	Board presentation by February 2012

¹ The Fund and the World Bank teams agreed to maintain regular monthly communication and exchange of information and to set a more structured semi-annual discussion in the context of the JMAP.

B. Technical assistance and Analytical Work.		
B.2. Innovations for Rural Women's Economic Empowerment	TBD	Delivery to client by May 2012
B.3. Country Economic Memorandum	August 15-19, 2011	Delivery to client by March 2011
B.4. Nicaragua Agriculture Public Expenditure Review	August 29 – September 1, 2011	Delivery to client by June 2012
B.5. Nicaragua: Consumer Protection # 10136	August, 2011	Delivery to client by November 2012

Annex III—Relations with the Inter-American Development Bank

(As of September 30, 2011)

Statement of IDB Loans

(In millions of U.S. dollars)

Year	Purpose	Amount
2007	National transmission investments to support SIEPAC	12.5
	Electricity Sector Support Program I	32.7
	Hospital Infrastructure	20.0
	Social Housing II	15.0
2008	Electricity Sector Support Program II	40.2
	Rural Sector	20.0
	Fiscal Management and Social Expenditure Reform I	20.0
2009	Storm-water Drainage and Development Management Sub-Watershed III Managua	13.0
	Urban Welfare Program for Children in Extreme Poverty	15.0
	Electricity Sector Support Program III	20.0
	Supplementary Road Infrastructure for Competitiveness Program	43.5
	Global Multi-sector Credit Program	20.0
	Fiscal Management and Social Expenditure Reform II	40.5
	Foreign Trade Support Program	10.0
	Agricorp (Non-sovereign)	30.5
2010	National Sustainable Electrification and Renewable Energy Program	30.5
	San Jacinto-Tizate Geothermal Power Project	40.0
	Environmental Program for Disaster Risk and Climate Change	10.0
	Proposal for an additional financing of cost overruns	4.5
	Public Sector Financial Management System Modernization Project	10.0
	Support to Transportation Sector I	20.2
	National Program of Tourism	10.0
	Support to the Improvement of the Fiscal Management and Social	42.5
	Potable Water Program for Managua	30.0
	Comprehensive Child Care Program - PAININ Stage IV	12.5
2011 ¹	Improving Family and Community Health in Highly Vulnerable Municipalities	20.0
	National Sustainable Electrification and Renewable Energy Program	22.0
	Integral Housing Improvement Program	20.0
	<i>Improving Social Protection and Health expenditures and Public Management (pending approval)</i>	45.0
	<i>Lease to Own: Access to Social Housing for the Majority in Nicaragua (Non- sovereign pending approval)</i>	

¹ Carry-over of US\$64.2 million for 2012

IDB Loan Commitments and Disbursements

As of September 30, 2011, there were 33 projects in the IDB's current sovereign loan portfolio with a total commitment of US\$721.8 million, and an undisbursed balance of US\$385.8 million. Basic infrastructure (roads and energy) accounts for over half the portfolio. Nicaragua is one of four IDB borrowing member countries to receive highly-concessional loans from the Fund for Special Operations (FSO). Nicaragua receives a lending blend of 50 percent from the FSO and 50 percent from the Ordinary Capital. The annual sovereign lending envelop depends on the availability of FSO funding as well as an allocation formula that encompasses policy performance, project performance, per capita income and population. The allocation for Nicaragua was US\$80.2 million per annum in 2007 and 2008. In early 2009, the overall FSO

funding for the four low-income countries was increased as a counter-cyclical response to the global economic crisis, and Nicaragua's allocation increased to US\$162.0 million for 2009 and US\$170.2 million for 2010. For 2011, the FSO allocation increased to US\$171.2 million.

Technical Assistance

As of September 30, 2011, there were 35 non-reimbursable technical cooperations (for the public sector) in execution with an approved commitment of US\$16.8 million and an available balance of US\$7.5 million. The Multilateral Investment Fund has: (i) 20 non-reimbursable technical cooperations (including regional operations) in execution with an available balance of US\$6.6 millions; and (ii) 3 loans in execution from the Social Entrepreneurship Program with an approved commitment of US\$1.6 million and an available balance of US\$1.2 million.

Recent Agreements

The current country strategy with Nicaragua was approved by the Board in February 2009. A new country strategy for the period 2012-2017 is expected to be approved next year.

Annex IV—Statistical Issues
(As of September 30, 2011)

I. Assessment of Data Adequacy for Surveillance

General: Data provision has some shortcomings, but is broadly adequate for surveillance. Most affected areas are government financing statistics and monetary statistics.

National accounts:

National accounts are compiled in accordance with the United Nations *System of National Accounts (SNA93)*. GDP estimates with 1994 as the base year are available up to the fourth quarter of 2010. Annual surveys for agriculture, mining, manufacturing, domestic trade, and services are regularly collected to estimate GDP by the production approach.

The revised GDP estimate for 1994 resulted in a 67.1 percent higher level of economic activity than measured by the previous 1994 estimate. On average, the revised GDP series was 70 percent higher than the old series for the period 1994-1999. Per capita GDP in dollar terms increased from \$478 to \$779 for 2000. This downward bias of Nicaraguan GDP estimates was distributed across the value added of all economic activities and expenditure components, except for changes in inventories, since they were overestimated in the previous series. The impact of the revision on the GDP growth rate was around one and a half percentage points from 1994 to 1997 and one third of a percentage point for 1998 and 1999, when the old series was discontinued.

STA provided technical assistance in quarterly national accounts to the Central Bank of Nicaragua in June 2005 and January 2008. Quarterly GDP series at current and at constant prices with 1994 as the base year were published in October 2008. The Central Bank of Nicaragua (BCN) is currently in the process of changing the base year of the national accounts to 2006 in accordance with the methodology of the *System of National Accounts 2008*. In January 2011, CAPTAC-DR provided assistance on the production of quarterly national accounts harmonized with the annual accounts using 2006 as the new base year. The project had some delays, but the estimates for the new base year are expected to be ready soon. Production accounts, supply and use table, and the majority of accounts for other institutional sectors have been compiled with 2006 as the base year. Preliminary estimates for the period 2006-2008 are expected to be released in November 2011.

Price statistics:

The consumer price index (CPI), with expenditure weights derived from a (1998/99) household expenditure survey, was introduced in 2001. The CPI covers Managua and eight other cities and is published monthly. Expenditures (weights) and prices in rural areas are excluded. The base year of the CPI was updated from 1994 to 1999, reflecting the improvement in the varieties of basket, the number of respondents reporting prices, and the number of prices collected per month. The CPI is calculated on the geometric average and imputations for missing prices are made. However, the base, basket, and weights of the CPI need updating.

The producer price index (PPI) (July 2006=100) covers a sample of small and medium-size establishments, as well as goods for processing establishments in the tax-free zones (i.e., “la maquila”). Compilation of a PPI began in 1999, and its public release started in May 2004.

Historical data are available from 1992. STA provided technical assistance for improving the PPI in January 2006, September 2007, December 2008, and September 2010. The September 2010 mission helped authorities develop a work plan for expanding the coverage to the service sector.

Government finance statistics (GFS). The fiscal ROSC mission in 2002 and the data ROSC mission in 2005 both found serious weaknesses in fiscal data. In general, government finance statistics are not fully aligned with international standards. The transactional coverage of GFS is still partial in comparison with the *GFSM 2001* requirements. Coverage and sectorization issues can be partially explained by the Public Administration Law, which excludes the judicial and legislative branches from the data coverage of the central administration. The fiscal data also present large discrepancies between the overall balance compiled by the Ministry of Finance and Public Credit (MHCP) and the financing data compiled by the BCN. Therefore, stronger collaboration is needed between the MHCP and the BCN to derive more accurate and timely estimates of external and domestic financing of the nonfinancial public sector. A 2004 GFS mission recommended that the envisaged Integrated System of Financial Management be made to support the compilation of GFS data and gradual migration to the *GFSM 2001*. These recommendations were reiterated by the FAD/STA mission in June 2006. An STA mission conducted in February 2010 found that the authorities are making significant progress in implementing the *GFSM 2001* methodology but some issues are still pending. The MHCP disseminates government finance statistics (GFS) covering only the central administration, and compiles annual GFS for the nonfinancial public sector (NFPS) for internal use and for reporting to the Western Hemisphere Department. The BCN reports budgetary central government data, albeit with considerable delay, for publication in the International Financial Statistics. In 2006 the MHCP reported GFS data for publication in the *GFS Yearbook*.

Monetary finance statistics: Monetary statistics are, in general, consistent with the *Monetary and Financial Statistics Manual (MFSM)*, 2000. Further improvements in the sectorization of accounts of the ODCs would improve the usefulness of the data, particularly for assessing net credit to central government. Reconciliation with fiscal data also poses problems due to differences in institutional coverage and basis for recording. In April 2008, STA provided technical assistance to help harmonize monetary and financial statistics in the Central American region. A standardized report form (SRFs) for credit cooperatives and insurance companies was compiled based on their accounting records for December 2007.

External sector statistics: Balance of payments statistics broadly follow the concepts and definitions set out in the fifth edition of the *Balance of Payments Manual (BPM5)*, within the limits set by the availability of information sources.

Resident institutional units are defined in conformity with *BPM5*'s concepts of economic territory, residency, and center of economic interest. However, coverage of the private sector is incomplete, in both the current and financial accounts. There are major coverage weaknesses in areas such as services, compensation of border employees, and financial transactions. In February 2007, a STA mission found that the downsizing of staff at the BCN and additional workload unrelated to compiling external sector statistics, have resulted in limited progress in implementing previous STA recommendations.

With few exceptions, all data are provided on a quarterly basis. Monthly updates on exports and imports and condensed BOP tables are available from the BCN website, with varying lags. Debt data are updated continuously at the BCN and are regularly available but coverage needs

improvement—particularly for the external debt of public enterprises, banks, and the nonfinancial private sector. STA provided technical assistance for improving the balance of payments and the international investment position in April 2009 and April 2010. In October 2010, CAPTAC provided technical assistance for improving the compilation of services statistics in the goods and services account of the balance of payments. A one-week TA mission on international investment position statistics also visited Managua in March 2010. A ROSC on the balance of payments was conducted in 2005.

II. Data Standards and Quality

Nicaragua has participated in the General Data Dissemination System (GDDS) since February 2005, but metadata and plans for improvements have not been updated since January 2005.

Data ROSC published in December 2005.

Nicaragua: Table of Common Indicators Required for Surveillance
(As of October 3, 2011)

	Date of latest observation	Date received	Frequency of Data ⁷	Frequency of Reporting ⁷	Frequency of Publication ⁷	Memo Items:	
						Data Quality – Methodological soundness ⁸	Data Quality – Accuracy and reliability ⁹
Exchange Rates	8/08/2011	8/08/2011	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	8/08/2011	8/08/2011	D	D	D		
Reserve/Base Money	8/08/2011	8/08/2011	D	D	D	O, LO, LO, LO	LO, O, LO, LO, LO
Broad Money	8/08/2011	8/08/2011	D	D	D		
Central Bank Balance Sheet	8/08/2011	8/08/2011	M	M	M		
Consolidated Balance Sheet of the Banking System	8/08/2011	8/08/2011	M	M	M		
Interest Rates ²	8/08/2011	8/08/2011	W	W	W		
Consumer Price Index	8/08/2011	8/08/2011	M	M	M	O, LO, LO, LO	LO, LO, LO, O, LO
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	8/08/2011	8/08/2011	M	M	M	LO, LNO, LNO, LO	O, O, O, O, LO
Revenue, Expenditure, Balance and Composition of Financing ³ – Central Government	8/08/2011	8/08/2011	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt ⁵	8/08/2011	8/08/2011	Q	Q	Q		
External Current Account Balance	8/08/2011	8/08/2011	Q	Q	Q	LO, LO, LNO, LO	LO, O, LO, LO, LO
Exports and Imports of Goods and Services	8/08/2011	8/08/2011	M	M	M		
GDP/GNP	Q3/2010	3/2011	Q	Q	Q	O, O, O, LO	LO, O, LO, O, LNO
Gross External Debt	8/08/2011	8/08/2011	M	M	M		
International Investment Position ⁶	9/29/11	9/29/11	A	A	A		

¹Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

²Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

³Foreign, domestic bank, and domestic nonbank financing.

⁴The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

⁵Including currency and maturity composition.

⁶Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁷Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).

⁸Reflects the assessment provided in the data ROSC published on December 8, 2005, and based on the findings of the mission that took place during January 11-26, 2005) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).

⁹Same as footnote 7, except referring to international standards concerning source data, assessment and validation of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.



Press Release No. 11/377
FOR IMMEDIATE RELEASE
October 21, 2011

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Seventh and Final Review of Nicaragua's Extended Credit Facility and Approves US\$8.74 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the seventh and final review of Nicaragua's economic performance under its Extended Credit Facility (ECF) arrangement, and the financing assurances review. Completion of the review allows for the final disbursement to Nicaragua of an amount equivalent to SDR 5.55 million (about US\$8.74 million). Total disbursements so far had been of SDR 72.45 million (about US\$114.1 million).

Program performance was satisfactory. All quantitative performance criteria for end-June 2011 were met with margins, and the structural agenda is broadly on track.

The Executive Board approved a three-year ECF (formerly known as the Poverty Reduction and Growth Facility) in the amount of SDR 71.5 million (about US\$111 million) in October 2007 (see [Press Release No. 07/224](#)). In September 2008, the Board increased financial support under the program by SDR 6.5 million (about US\$10 million) to help Nicaragua cope with the natural disasters of 2007 (see [Press Release No. 08/204](#)). In November 2010, the Executive Board approved an extension of the arrangement through December 4, 2011.

Following the Executive Board discussion on Nicaragua, Mr. Min Zhu, Deputy Managing Director and Acting Chair, issued the following statement:

"The Nicaraguan economy grew strongly in the first half of 2011 despite deteriorating global conditions. Growth continues to be broad based. Inflows of foreign investment and official borrowing are expected to more-than-finance the still-high external current account deficit and contribute to reserve accumulation in 2011. The authorities' policies aim to enhance the resilience of the economy against downside risks.

"Further fiscal consolidation to reduce public indebtedness remains a key priority, with a focus on restraining government current spending (especially the wage bill), sustaining gains in revenue mobilization, and strengthening the financial position of the energy sector. The authorities' decision to use the revenue overperformance expected for this year to pay down government debt is appropriate. Efforts have been intensified to create space for investment and well-targeted assistance to the poor. Key structural reforms in the fiscal area include enhancing tax administration, broadening the tax base, and reforming the pension system and the civil service.

“The Nicaraguan banking system remains generally sound. Banks are well capitalized, profitability continues to improve, and liquidity buffers remain ample. The authorities intend to step up their efforts to improve coordination and information exchanges with other regional supervisors, and to monitor volatile aid-related deposits.

“Important steps have been taken to advance the structural reform agenda, including the approval of a law regulating the micro-finance sector and the introduction of norms requiring greater disclosure by financial cooperatives and trust funds. Significant progress has been made in managing and reporting aid flows, and continued improvements in this area would help foster confidence, facilitate macroeconomic management, and mobilize donor support,” Mr. Zhu said.

**Statement by Carlos Perez-Verdia, Executive Director for Nicaragua
and Mr. Luis Cosenza Jimenez, Senior Advisor
October 21, 2011**

We would like to thank Staff for their balanced report of the seventh, and final, review of Nicaragua's ECF and for their constructive dialogue with our authorities. We concur with the report's main messages and would like to emphasize the following points:

Program Performance: All quantitative performance criteria and structural benchmarks for end-June were met. As the report states, the revenue target was exceeded (the tax collections to GDP ratio is currently estimated to be 19.5 percent), the deficit of the central government is projected now to be only 0.1 percent of GDP at end 2011 and the consolidated public sector deficit will be reduced to 1.1 percent. The additional revenue (that resulted from the 2009 tax reform illustrated in Box 1 of the Staff Report) will be used to reduce internal debt, with particular attention paid to the financing needs of the electricity sector. Growth is currently estimated to be 4 percent in 2011 and 3.3 percent in 2012 (however, the index of monthly economic activity shows an average annual growth rate of 6.8 percent as of July, and the quarterly GDP posted a growth rate of 5.2 percent for the second quarter of 2011). FDI and capital transfers have increased and remittances have grown at about 10 percent in nominal terms. Remarkably, these goals have been achieved in the context of a deteriorating international environment.

Monetary Policy: The authorities will continue to build an adequate reserves level, to contain inflation and ensure liquidity in the financial system. The rate of crawl of the exchange rate will be maintained at 5 percent. The authorities have taken measures to strengthen the Central Bank and its financial statements will be prepared in line with international standards. As the report mentions, the banking system is sound and the authorities plan to perform stress testing on a pilot basis in late 2011. Finally, during the last three months, including September, net credit to the private sector has been positive.

Other Actions: The authorities recognize that further efforts are needed to rationalize fiscal exemptions and deductions and to enact new regulations on transfer prices. They have enhanced transparency and accountability, and as part of that effort they have recently updated the report on the use of external aid. The authorities submitted to Congress a budget for 2012 that will result in a deficit of 0.4 percent of GDP for the central government and 2 percent for the consolidated public sector. Although important steps have been taken to improve the situation of the electricity sector, as detailed in Box 3 of the Staff Report, other issues that affect the electricity sector will be addressed in 2012. In order to strengthen public administration a technical study on staffing and productivity in the public sector is underway. Finally, additional debt relief will be sought in the context of the HIPC initiative.

Other Developments: A new law was enacted to strengthen the microfinance sector. In addition, assessments undertaken recently show that Nicaragua has achieved a substantial

reduction of poverty and inequality. Furthermore, there have been marked improvements in literacy, primary school enrollment, potable water and sewerage coverage. Growth has indeed been inclusive.

Future Events: Presidential elections will take place at the end of the year and a new Administration will take office in January of 2012. Although the ECF is coming to an end, the authorities will continue to engage the Fund in a constructive and frank dialogue. As an important element of this dialogue, Article IV consultations will take place in 2012.

Finally, it is our opinion that the ECF has been instrumental in supporting Nicaragua's macroeconomic stability and inclusive growth. Based on the satisfactory performance under the program, on behalf of the government of Nicaragua we request that the Fund proceed with the eighth disbursement under the ECF arrangement.