INTERNATIONAL MONETARY FUND

IMF Country Report No. 12/256

NICARAGUA

2012 ARTICLE IV CONSULTATION

September, 2012

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2012 Article IV consultation with Nicaragua, the following documents have been released and are included in this package:

- **Staff report** for the 2012 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 11, 2012, 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 June 12, 2012. 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.
- **Informational Annex**
- **Public Information Notice** (PIN) summarizing the views of the Executive Board.
- **A statement by the Executive Director for Nicaragua**

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

Ex Post Assessment of Longer-Term Program Engagement
Selected Issues Paper

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

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INTERNATIONAL MONETARY FUND

NICARAGUA

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION

June 12, 2012

KEY ISSUES

Context. Nicaragua's performance on the growth and fiscal fronts in 2011 was better than anticipated in the last review of the ECF-supported program. President Ortega was re-elected in November. Municipal elections are scheduled for November 2012.

Near-term prospects and risks. Output growth is projected to moderate in 2012 as the global economy remains weak. Oil price increases are significant risks to the near-term outlook given Nicaragua's large oil import bill. Tax revenue collections are expected to remain strong but expenditure pressures are building up. Key fiscal risks for 2012 are higher electricity subsidies and other increases in current expenditures, including the absorption of the wage bonus (granted since 2010) into the wage bill.

Medium-term challenges and staff recommendations. Under current policies, economic growth may stabilize at about 4 percent, which would not result in large reductions in poverty. Attaining a much higher growth rate, sustained by large increases in productivity, is Nicaragua's overarching challenge. Reducing fiscal and external vulnerabilities is another significant challenge. Reforming the social security system, establishing a sustainable financial framework for the electricity sector, improving business conditions, and continuing the momentum in tax reforms would be critical to overcome these challenges. A growth-enhancing fiscal consolidation path (anchored on controlling current expenditure and broadening the tax base), a higher international reserves buffer, and a steady strategy to lower the dependence on oil imports are key staff recommendations.

Approved By
Miguel Savastano (WHD) and Dhaneshwar Ghura (SPR)

Discussions took place in Managua during May 2–May 11, 2012. The Team comprised M. Estevão (head), I. Samake, C. Johnson (all WHD), R. Fenochietto (FAD), J. Bersch (SPR) and G. Di Bella (Resident Representative). Staff met with the Vice President, the Economic Cabinet, the Superintendent of Banks, the Attorney General, the Comptroller General, the Minister of Energy, the Economic Commission of the National Assembly, other government representatives, the business community, labor unions, civil society organizations, and international donors. L. Consenza (OED) participated in policy meetings.

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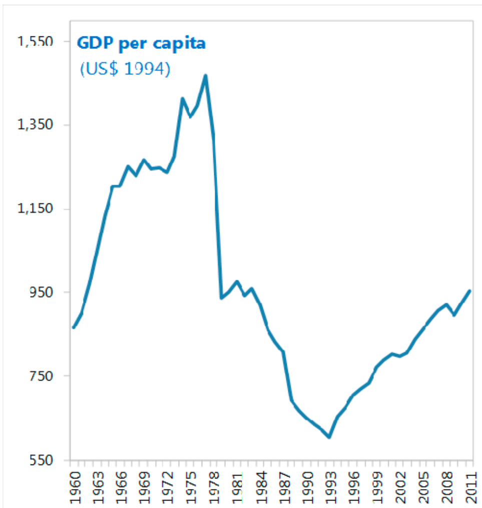
BOXES

BACKGROUND

1. Despite moderate growth since the mid 1990s, Nicaragua's per capita GDP is still well below its 1977 peak.

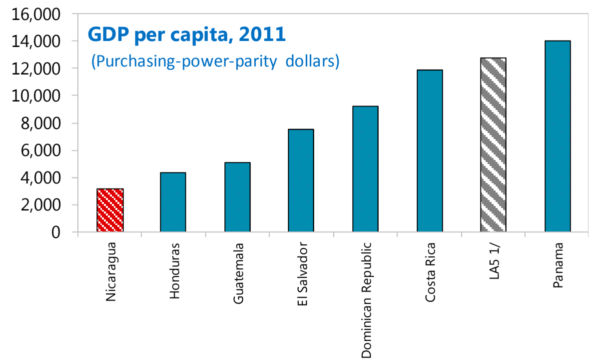


Sources: Nicaraguan authorities; and Fund staff calculations.

GDP per capita collapsed at the end of the 1970s and in the 1980s, as war and inadequate economic policies took their toll. Following a peaceful democratic transition in 1990, economic growth resumed, but at moderate rates. More recently, the Nicaraguan economy has shown signs of strength amid difficulties in advanced economies, as adequate macroeconomic policies (supported by the Fund), favorable export prices, and transfers from abroad helped maintain economic stability. The implementation of key structural reforms—including in tax policy, and in the electricity and financial sectors—also helped increase resilience.

2. Boosting growth to reduce widespread poverty remains Nicaragua's key challenge. Despite a steady growth performance in the last decade and increased spending in social and poverty-reducing policies,[1] Nicaragua remains one of the poorest countries in the Western Hemisphere. Poverty rates have declined from 48.3 percent of the population in 2005 to 42.5 percent in 2009—still well above the Latin American average (27 percent). Rural areas have seen the largest poverty declines, but 63 percent of their population remained below the poverty line in 2009. Extreme poverty declined by only 3 percentage points during the same period, resting at 15 percent of the population in 2009 (27 percent in rural areas).

[1]Poverty Reduction Strategy Paper (PRSP) update at http://www.imf.org/external/pubs/cat/longres.aspx?sk=25353.0



Sources: WEO; and Fund staff calculations.
1/Brazil, Chile, Colombia, Mexico, and Peru.

3. Economic and political vulnerabilities are non-negligible. External financial flows remain critical to finance very large trade and current account deficits. This makes resources from foreign donors and IFIs particularly important for Nicaragua's external viability. On the political front, President Ortega was reelected for another term in November 2011 amid critical reports on the electoral process by international observers; the President's party now has a comfortable majority in Congress and a strong influence on other decision bodies, including the judiciary. Most donors and international observers insist on the need of reforming the electoral system before the municipal elections, currently scheduled for November 2012.[2]

RECENT ECONOMIC DEVELOPMENTS

4. Economic performance in 2011 was stronger than previously envisaged (Figure 1). Real GDP grew 4.7 percent in 2011 (compared to a 4-percent projection at the time of the final review of the ECF arrangement).[3] Robust consumption and investment were the key growth drivers on the demand side, while construction and manufacturing performed strongly on the supply side. This said, supply-side indicators showed some deceleration in activity at the turn of the year. Inflationary pressures abated somewhat to 8 percent by end 2011, as world commodity prices eased. The exchange rate crawl remained at 5 percent per year.

5. The fiscal outturn was substantially stronger than anticipated in September 2011. At the central government level, the over performance was explained by larger-than-projected restraint in current spending and public investment as a ratio to GDP. As a result,

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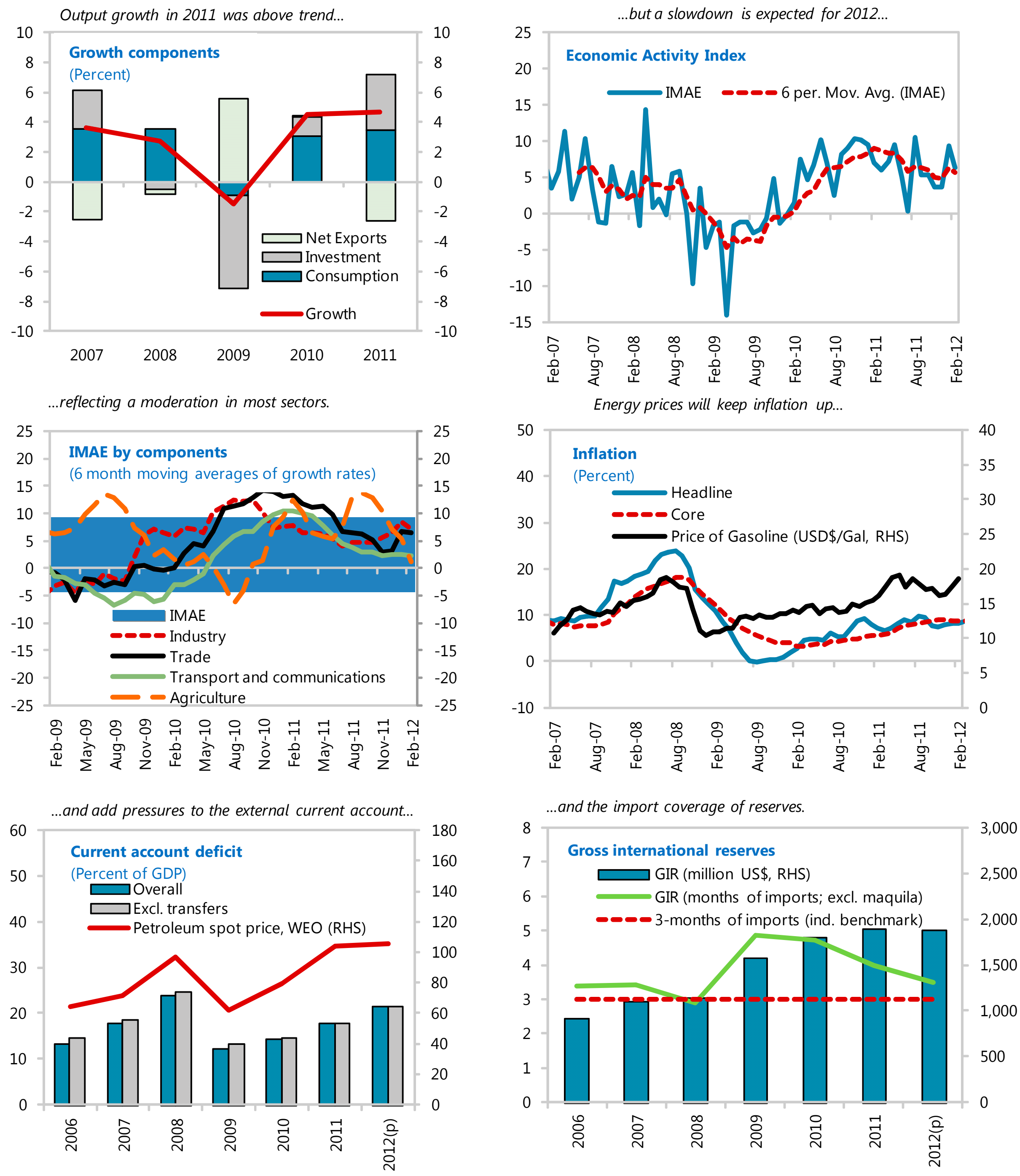
[2] Budget support from traditional donors and the World Bank was suspended following reports of irregularities in the 2008 municipal elections.

[3] IMF Country Report No. 11/322 (http://www.imf.org/external/pubs/cat/longres.aspx?sk=25352.0).

Figure 1. Nicaragua: Recent Economic Developments



Sources: Nicaraguan authorities; and Fund staff estimates and projections.

the central government posted a surplus of 0.6 percent of GDP—0.7 percentage-point of GDP above the projection in the last review (Figure 2). The bulk of the central government surplus was used to pay down debts of the state-owned electricity generation company, ENEL. Elsewhere in the public sector, better-than-projected revenues of state-owned enterprises and a lower operational deficit of the central bank also contributed to eliminate the deficit of the consolidated public sector (CPS) for the first time since 2007.

Nicaragua's Public Sector Balance, 2011

(Percent of GDP)

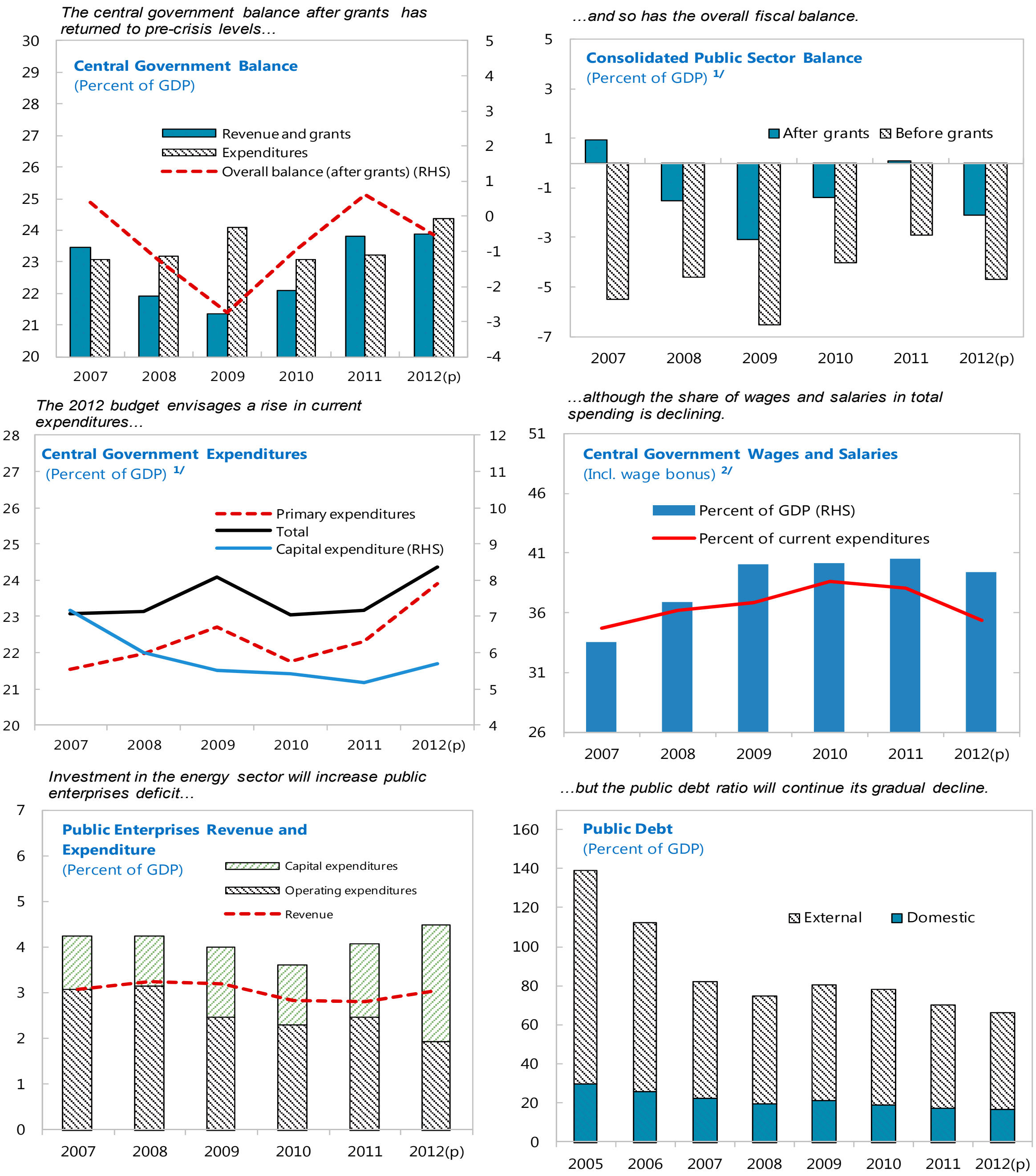
	ECF 7th Review [1/]	Outturn
Central government	-0.1	0.6
Revenue	21.1	21.1
Expenditure	24.1	23.2
Current	18.7	18.1
Capital	5.4	5.1
Grants	2.9	2.7
Social Security Institute	0.9	0.9
Managua Municipality	0.0	-0.1
Public Enterprises	-1.3	-1.0
Central Bank Operating	-0.6	-0.4
Consolidated Public Sector (after grants)	-1.1	0.1

[1/] IMF Country Report No. 11/322

6. **Even though the external current account deficit widened, larger capital inflows produced a small surplus in the balance of payments** (Figure 3). The large increase in oil prices and imports raised Nicaragua's oil bill to almost 17 percent of GDP, from about 11 percent in 2010. Thus, despite the strong growth in exports (28 percent year-on-year in U.S. dollar terms) and remittances (11 percent), the current account deficit increased to 18 percent of GDP in 2011. Sizable FDI inflows and assistance from Venezuela in the context of the *Alianza Bolivariana para los Pueblos de Nuestra America* (ALBA) more than offset this increase and the overall balance of payments posted a small surplus.

7. **Monetary policy was geared at strengthening the international reserve position in 2011**. During 2011, the central bank continued to adhere to its crawling-peg system, which, in the context of a stronger-than-expected fiscal outturn and demand for base money, allowed an increase in net international reserves and a decline in central bank's short-term debt. In addition, changes in the levels and the computation of minimum reserve requirements on bank deposits in early 2011 helped to keep reserve demand stable.

Figure 2. Nicaragua: Selected Fiscal Indicators



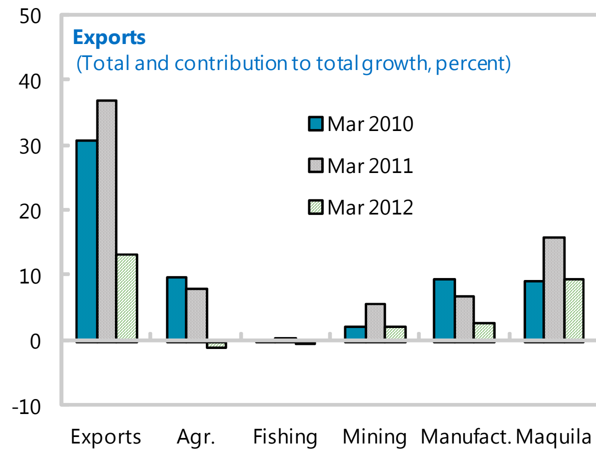
Sources: Nicaraguan Authorities; and Fund staff estimates and projections.

1/ Includes the wage bonus of 2010-2012.

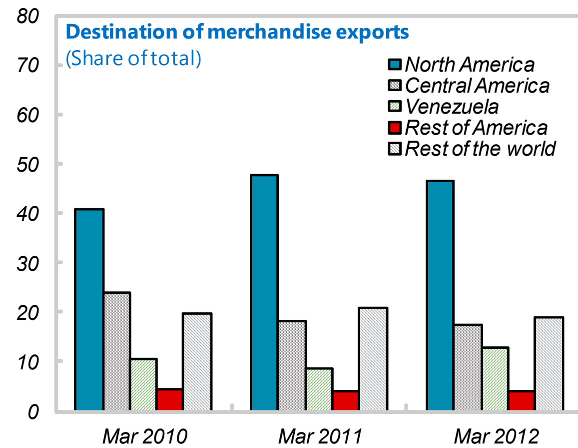
2/ The series reflect a transfer of salaries of teachers and service from municipalities to the central government budget that took place in 2007.

Figure 3. Nicaragua: External Sector Developments

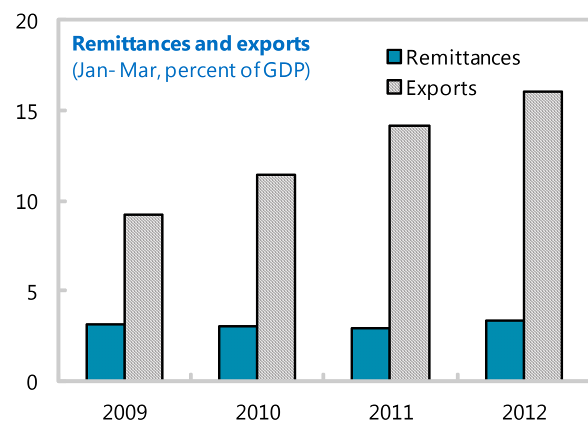
Export growth is slowing...



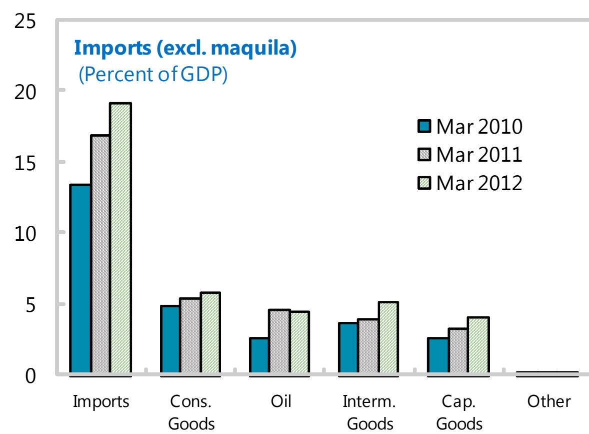
…and the United States continues to be the main destination for exports.



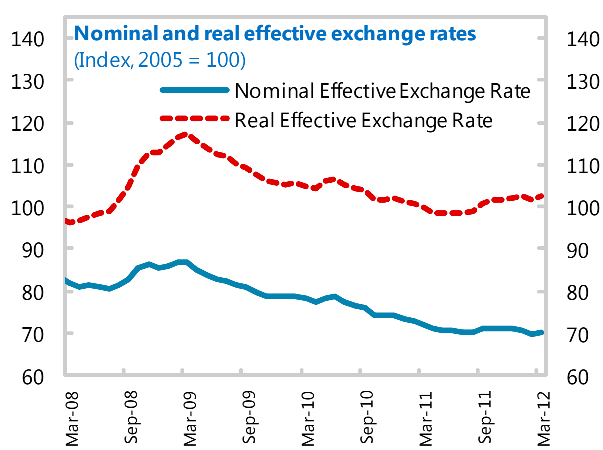
Remittances have remained stable...



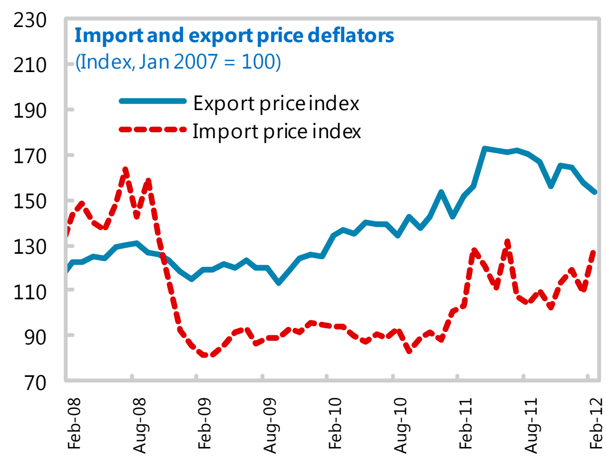
...while imports growth remains strong.



The real exchange rate remains broadly stable...



...while the terms of trade have deteriorated recently.



Sources: Nicaraguan authorities; and Fund staff calculations.

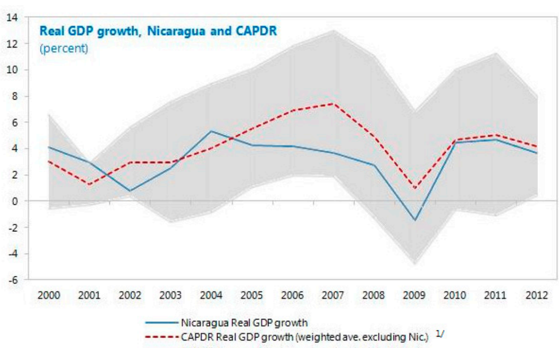
8. **Banks' balance sheets continued to strengthen while credit growth picked up** (Figure 4). Nonperforming loans ratios declined as banks' profitability improved and deposits (in local and foreign currency) continued to rise. At the same time, bank lending, especially to trade and agriculture, picked up significantly towards the end of the year.

Nicaragua: Selected Financial Indicators, 2009–11			
	Dec-09	Dec-10	Dec-11
Banks' Liquidity coverage 1/	1.8	1.5	2.3
Banks' deposits			
In foreign currency 2/	72.8	73.3	70.6
Annual change 3/	16.2	23.6	17.4
Credit to the private sector 4/	-7.5	5.9	15.6
NPLs 5/	3.3	3.0	2.2
NPLs 6/	10.9	8.0	5.9

Sources: Superintendency of Banks; and Central Bank fo Nicaragua.
1/ Ratio observed-required reserves.
2/ Percent of total deposits.
3/ By end of period, in percent.
4/ Annual change.
5/ Percent of total loans.
6/ Percent of total loans, includes restructured and reprogrammed loans in the numerator.

OUTLOOK AND RISKS

9. **On the back of weak global economic activity, the Nicaraguan economy is projected to grow by slightly less than 4 percent in 2012** (Table 1).

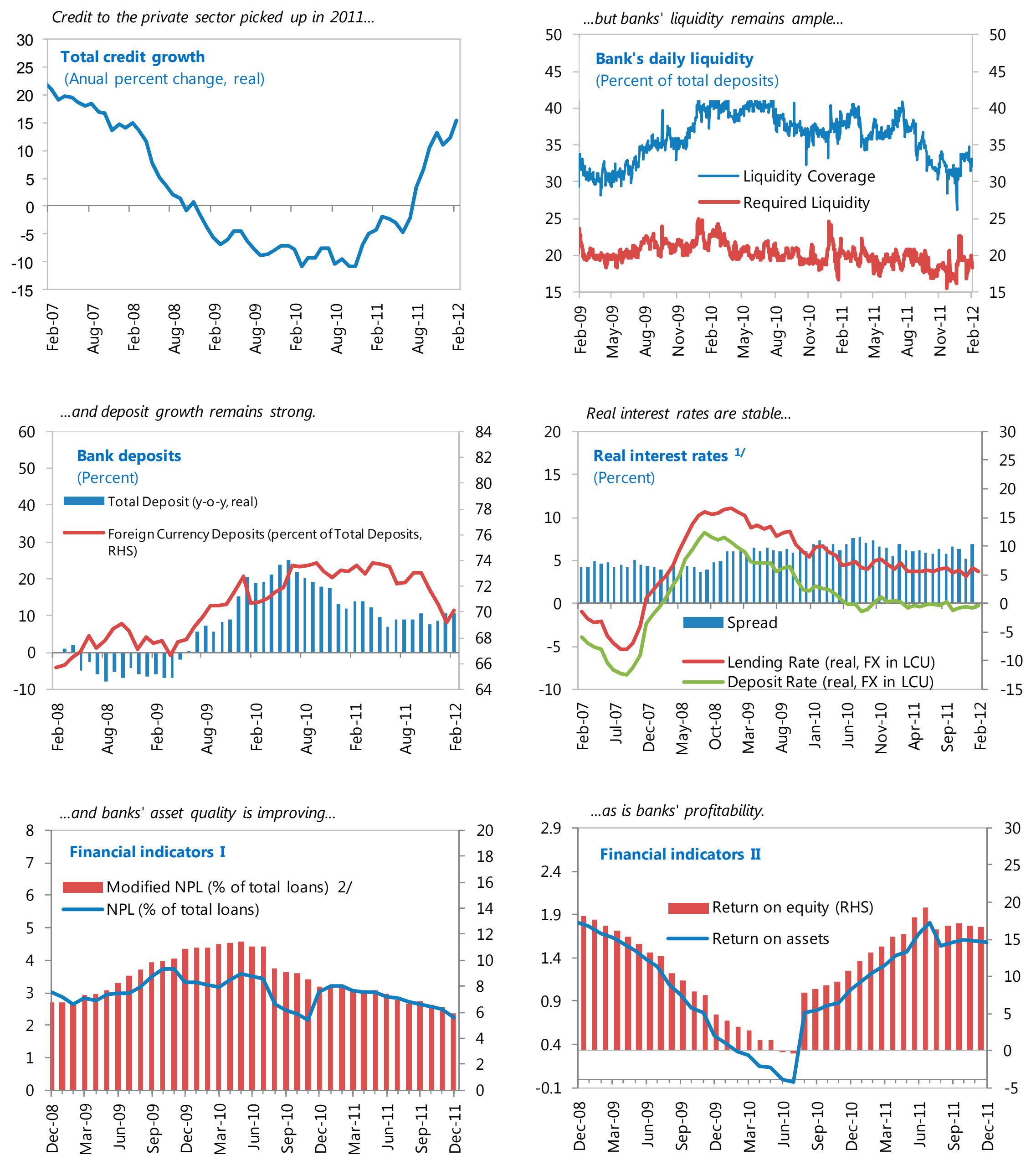


Source: Fund staff calculations.
1/CAPDR refers to Central America, Panama and the Dominican Republic.

Inflation is expected to rise to about 9 percent, reflecting first and second-round effects of higher world oil prices, electricity tariffs, and minimum wages. Weaker external demand and export prices are expected to moderate export growth and, together with a larger oil bill, worsen the external current account balance. Capital inflows are set to increase but the overall balance is expected to record a small deficit.

10. **Risks to Nicaragua's economic outlook are tilted to the downside**. The effects of a further escalation of the euro area crisis on global growth and on donor countries' aid budgets would impact adversely the Nicaraguan economy, particularly given some donors' renewed concerns about governance in the country. Possible pressures on oil prices from heightened geopolitical uncertainty would

Figure 4. Nicaragua: Monetary and Financial Sector Developments



Sources: Nicaragua authorities; and Fund Staff calculations.
1/ Interest rates in foreign currency expressed in local currency.
2/ NPLs including restructured and reprogrammed loans.

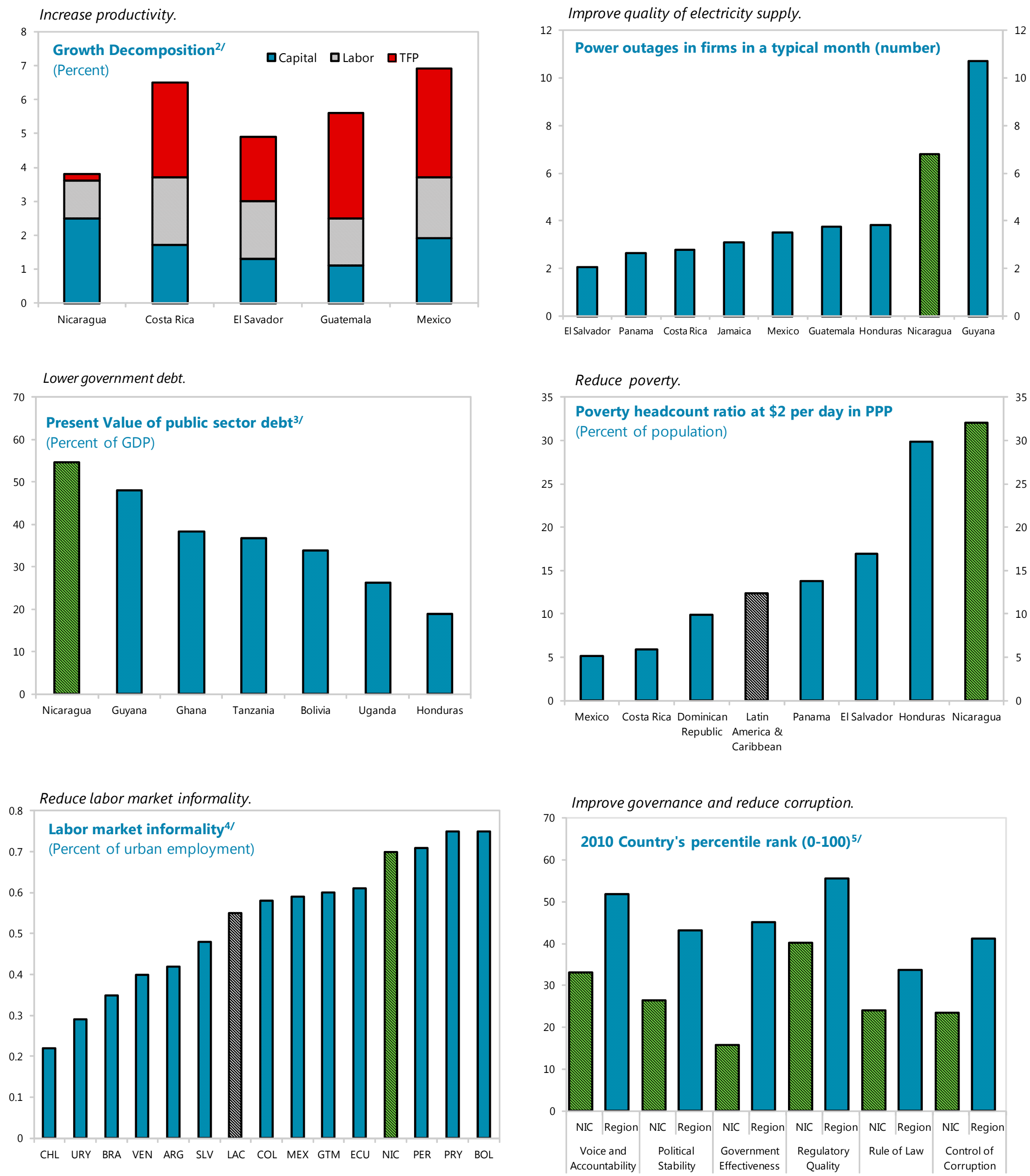
also have a severe impact on the external accounts. In addition, the magnitude and nature of the oil-collaboration flows from Venezuela could be affected following that country's presidential elections in October 2012.

11. **Over the medium term, large external current account deficits will remain a key source of vulnerability**. Recent staff work gives support to the view that Nicaragua's potential output growth rate is about 4 percent a year under current policies (Selected Issues Paper, Chapter 1). Given the high oil dependency of the Nicaraguan economy, this scenario implies large current account deficits in the medium term, as planned investment projects to move Nicaragua's energy matrix towards renewable fuel sources will mature slowly (Table 6). Sizable external inflows, including FDI, will be necessary to finance those deficits and to keep broadly adequate international reserve buffers. Assuming the oil cooperation scheme with Venezuela does not change significantly, the ratio of international reserves to imports is expected to decline slowly until savings from oil-substituting investments are large enough to reverse this trend, which would happen well after 5 years.

POLICY DISCUSSION

12. **Discussions focused on policies and reforms to contain fiscal and external vulnerabilities, boost medium-term growth, and reduce poverty** (Figure 5). The main recommendations of the previous Article IV Consultation (June 2010) included: (i) securing public debt sustainability by addressing pressures from the social security system and further broadening the tax base; (ii) reforming the financial framework for the energy sector; (iii) strengthening governance, including by providing greater oversight to the micro-finance sector and enhancing the accountability of public institutions; and (iv) continuing to improve bank supervision and regulation, in particular risk-based and consolidated cross-border supervision. Since then, reform options for the pension and tax systems have been discussed with key stakeholders. In addition, the authorities enacted a law regulating the micro-finance sector,

Figure 5. Nicaragua: Medium-Term Challenges[1/]



Sources: World Development Indicators; World Bank Governance Indicators; and Fund staff calculations.

[1/] Latest data available as of 2009-2010.

[2/] Average 1998-2006, Table 4 in Harberger, A., 2007, *The Nicaraguan Economy: Situation and Prospects*, manuscript.

[3/] Latest available figures from the countries' debt sustainability analysis exercise.

[4/] Perry, G, O. Arias, and, P. Fajnzylber, 2010, *Informality, Exit and Exclusion*: World Bank, Washington, DC.

[5/] Region: Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras and Panama.

worked on guidelines to improve the administration of civil servants, and initiated bank stress testing. However, little has been done to reform the financial framework for the electricity sector, address critical governance problems, and reduce budget rigidities. Discussions during the 2012 consultation revolved around similar themes, with a focus on how to move toward reform implementation in all key areas. A baseline medium-term macroeconomic framework prepared by the staff served as the basis for those discussions (Table 7).

A. Near-Term Policies

13. It was agreed that the overall public sector balance would deteriorate in 2012. At the central government level, revenues are expected to increase by 0.4 percent of GDP on the back of improvements in tax administration and a one-off court-mandated payment of overdue taxes by a large private sector company (0.2 percent of GDP). However, the central government balance will switch to a deficit of ½ percent of GDP reflecting higher expenditures on subsidies to electricity consumption (0.6 percent of GDP), on the government's own electricity bill, and on public investment. In addition, the staff's projection assumes that the wage bonus (so far financed by foreign grants) will be absorbed by the budget in the second half of the year (0.3 percent of GDP). Elsewhere in the public sector, lower income from investments of the social security institute is projected to reduce the social security surplus; higher spending in infrastructure and electricity will raise the deficit of state-owned enterprises; and the central bank operating balance will worsen.

14. Staff noted that there are significant risks to the 2012 fiscal outlook. The authorities judged the risks to be balanced and indicated that they are preparing a 5-year fiscal plan reflecting the new government priorities. Changes to current budget allocations are still uncertain, but pressures for higher spending from the education, health and law enforcement sectors are significant. Ongoing negotiations to ensure the medium-term solvency of the electricity sector also may require higher-than-projected government transfers. Staff strongly recommended keeping the central government deficit at or below ½ percent of GDP in 2012, in particular by controlling spending on goods and services. The authorities agreed and indicated that the supplementary budget that they will prepare by the middle of the year will be consistent with a small central government deficit in 2012.

15. Staff noted that monetary policy has contributed to protect the external position but cautioned about a fast weakening of reserve coverage. It was noted that Nicaragua's crawling-peg regime had been successful at keeping inflation rates at levels similar to those in other countries of the region and avoided large losses of international reserves.[5] Moreover, the country's price competitiveness has improved (Selected Issues Paper, Chapter 2). Staff noted, though, that the projected decline in reserve coverage for 2012 is a reason for concern going forward.

B. Medium-Term Challenges

Boosting output growth to reduce poverty

16. Staff noted that without a decisive reform effort, Nicaragua's output growth is likely to remain dependent on low-productivity activities, which would be insufficient to reduce poverty significantly. With population expected to grow by 1½ percent a year through 2020, a real GDP growth rate of 4 percent would raise income per capita by only 2½ percent a year, which would translate into very slow poverty reduction. Moreover, Nicaragua's growth performance has been underpinned by relatively robust investment rates but low productivity—a feature also noted by the authorities—suggesting there is room for improving growth outturns (Selected Issues Paper, Chapter 1).

17. Staff argued that stronger institutions would yield productivity gains. Indicators suggest that Nicaragua lags behind its peers in terms of government accountability and effectiveness, regulatory quality, the rule of law, and the control of corruption (Figure 5 and Selected Issues Paper, Chapter 2). Key domestic stakeholders shared this assessment. The authorities agreed that there is room for improvement in a number of areas, but stressed that the sharp increase in FDI observed in recent years is a sign of improved business

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[4]The crawling peg system has been in place since the mid-1990s. As fiscal consolidation evolved and the economy stabilized, the rate of crawl was progressively reduced.

conditions and harbinger of future productivity gains. On the issue of accountability, the President and the Vice-President of the Council of Comptrollers pointed to difficulties in bringing cases against misuse of public resources to completion in the judicial system. On the issue of property rights, the Attorney General reported good progress toward regularizing land titles. Staff noted that decisive action to improve government accountability and effectiveness, punish the misuse of public resources, and strengthen property rights would improve perceptions about the quality of governance in the country, with positive effects on investment and growth.

18. Staff stressed that reforming the financial framework for the electricity sector is crucial for unleashing higher growth. Oil-based power plants produce about 70 percent of Nicaragua's electricity, and tariffs to final consumers have been trailing fast-rising oil costs. Even after a 9-percent tariff increase in January 2012, staff estimates that a further 16 percent increase would be needed to close the gap with marginal costs. Staff argued that developing a tariff-setting framework that ensures the solvency of the electricity sector was critical to boost output growth. Such a framework would have to take into account medium-term costs, electricity losses during distribution, and transfers to poorer households (Selected Issues Paper, Chapter 3). The authorities noted that negotiations with all stakeholders were underway, and they were confident that a multi-year framework for the sector would be agreed soon.

19. High labor and product market informality and low labor force skills are steep obstacles to productivity growth. Only about 25 percent of the Nicaraguan labor force is part of the social security system and the economy is populated by many small, low-productivity firms (Box 1). Those firms have little incentives (or means) to either grow or leave the informal sector, hence hindering economic growth. Staff welcomed the recent improvements in electronic filing of taxes and business licensing procedures, which will increase incentives to join the formal sector. In addition, it argued that creating more flexible social security schemes for segments of the workforce (with lower contribution rates but also lower benefits), could increase incentives to formal labor agreements. Low education levels and reported mismatches between university-level graduates and the needs of the marketplace also hurt productivity. Staff stressed that enhancing the coverage and quality of education would involve allocating more resources to primary, secondary, and technical education.

Box 1. Informality in Nicaragua's Labor Market

Labor market informality is quite high in Nicaragua but follows a pattern observed in all Latin America. One definition of an informal worker is someone who does not contribute to the social security system. Data from the 2010 Permanent Household Survey show that informal workers in Nicaragua are prevalent (i) in smaller firms or in firms without formal book keeping; (ii) among the self-employed; and (iii) in rural areas (Figure 6). Informal labor arrangements also are more prevalent among women and younger workers. While these patterns are present in other Latin American countries, in Nicaragua informal employment accounts for more than 70 percent of urban employment—much higher than the 54 percent average in the Latin American region (Perry et al, 2010).[1]

Low income per capita is likely a key reason for the high proportion of informal workers in Nicaragua. Academic work has typified informality as either a "barrier" or a "choice" for workers. According to the "barrier" interpretation, informal workers are excluded from government benefits and the modern economy, either as a result of labor market segmentation or burdensome regulations (de Soto, 2000).[2] According to the "choice" hypothesis, workers choose to exit or not enter into formal arrangements following a cost-benefit analysis about the quality of government services and benefits, and the extent of institutional enforcement (Perry et al, 2010). Because an informal worker costs less to a firm, employers accept informality when the chances of detection are low. Both factors seem to be present in Nicaragua, as enforcement capacity is relatively weak, and the quality of government benefits is low. The high incidence of informality in Nicaragua is also consistent with its standing as the second-poorest country in the Western Hemisphere.

Large levels of informality result in low productivity and create policy challenges. For instance, informality can be a barrier to firm growth, as employers try to avoid detection, thus preventing the full realization of economies of scale. Moreover, informality creates dual labor markets and a less equitable society. As in other places, reducing informality in Nicaragua should be a long-term goal and would require, inter alia, revamping the benefits of belonging to the formal workforce, reducing costs of doing business (including by simplifying the tax system), facilitating compliance and strengthening enforcement, enhancing government effectiveness and legitimacy, enforcing property rights, and improving the quality of education .

1/ Perry, G, O. Arias, and, P. Fajnzylber, 2010, *Informality, Exit and Exclusion*: World Bank, Washington, DC.

2/ De Soto, H., 2000, *The Mystery of Capital*: Basic Books, New York.

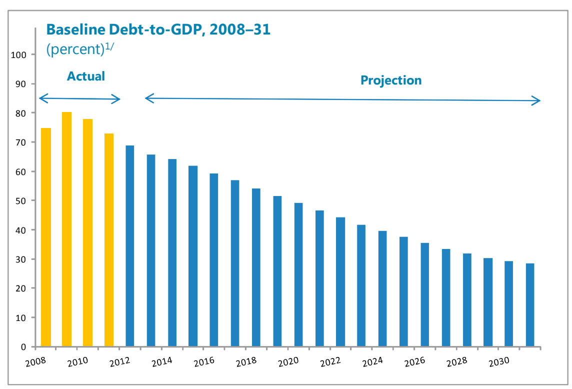
Figure 6. Nicaragua: Labor Market Informality, 2010Q4
(Ratio of total employment)

Sources: Nicaraguan Statistical Institute (INIDE); and Fund staff calculations.

Staying the course of fiscal consolidation

20. It was agreed that medium-term fiscal consolidation is crucial to create policy space to mitigate the adverse effects of shocks. Staff discussed a scenario where the central government deficit declines to about 0.2 percent of GDP in the medium term, even after assuming that the wage bonus would be fully funded by the public budget. Central government investment is projected to edge up to 5.9 percent of GDP by 2016 to underpin the 4 percent growth projection. The projected tax revenue path reflects ongoing tax administration efforts to improve revenue collections. Overall, the assumed adjustment strategy (based on controlling current spending and improving tax administration without raising marginal taxes) would have limited negative effects on growth (Selected Issues Paper, Chapter 4). Outside the central government, the consolidation projection assumes gradual reductions in the deficit of state-owned enterprises and the central bank, while the social security system would put continued pressure on the fiscal accounts.

21. Steady fiscal consolidation into the next decade would reduce public debt ratios. Nicaragua's public debt dynamics have not changed significantly with respect to the recently published debt-sustainability analysis (DSA).[5] That analysis concluded that Nicaragua's external debt appeared sustainable in the medium term and that the external public debt faced a moderate risk of distress, with vulnerabilities arising from worsening financing terms and lower growth. The authorities are continuing negotiations to obtain debt relief on HIPC-equivalent terms from non-Paris club creditors and for a pending claim (US$22.8 million) related to the commercial debt buy-back operation of October 2007, but a conclusion is still not on the horizon. At end-2011 there was about US$ 1.6 billion (24 percent of GDP) of unsettled debt with non-Paris club creditors.



Sources: Central Bank of Nicaragua; and Fund staff estimates and baseline projections.
1/ Based on the 2011 DSA Update and Staff current macroeconomic framework. Estimate up to 2010 correspond to the legal situation.

22. Staff noted that the fiscal risks in the baseline scenario were significant. To mitigate these risks, staff emphasized the importance of exercising strict

[5] IMF Country Report No. 11/322 (http://www.imf.org/external/pubs/cat/longres.aspx?sk=25352.0).

discipline in public enterprises and other public sector entities. Staff also noted that the size of municipal legislatures had greatly expanded, implying potential pressures on central government transfers. The authorities indicated that transfers to municipalities are capped by law at 10 percent of total tax revenues, out of which only 30 percent can be used for current spending. Staff stressed the fiscal risks associated with a possible sudden interruption in the oil-cooperation flows from Venezuela, given the social costs of ending the programs funded by them. The authorities remarked that the history of cooperation between the two countries did not justify considering this a serious risk.[6]

23. Further improvements in the tax system could generate additional revenues (Box 2). Staff advised the authorities to use the momentum created by the 2009 reform to make the tax system more equitable and efficient, in particular by eliminating remaining VAT exemptions. The authorities confirmed their intention of continuing negotiations with unions and private sector employers toward a new set of reforms by the end of the year. Staff advised the authorities to use the direct tax system to protect vulnerable segments of society from a possible de facto increase in indirect taxes.

24. Staff urged the authorities to reform the public pension system. It noted that in staff's medium-term baseline, the pension system would start recording deficits in 2015 and its trust fund would be depleted by 2021. Moreover, as discussed in the November 2011 DSA, cumulative deficits in the pension system would put the public debt in an unsustainable path in the longer term. Staff emphasized that the benefits of reform would be higher the earlier it starts, and urged the authorities to implement it in 2012 based on the information of the comprehensive 2009 actuarial report. Concretely, staff recommended, inter alia, gradually raising the minimum retirement age, aligning pension benefits to the amount and length of contribution time for minimum pension recipients, and increasing contribution rates moderately (Selected Issues Paper, Chapter 5). Staff suggested that changes should be consistent with reducing the lure of informality. Even though the authorities agreed with the need to reform the pension system, they did not commit to any measure, emphasizing instead the importance of reaching a national consensus on key parametric changes.

[6] The stock of debt resulting from the Venezuelan oil cooperation flows was contracted by a private sector cooperative (CARUNA). The authorities and CARUNA representatives noted that there are no government guarantees on this debt. According to CARUNA representatives, if their ability to service these loans is in jeopardy, CARUNA's investment strategy would be reevaluated.

Box 2. The Benefits of a New Tax Reform

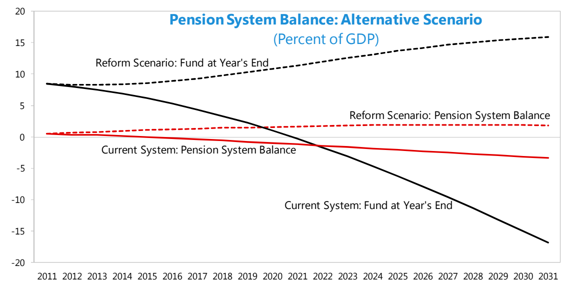
Recent reforms have improved the efficiency and equity of the tax system, and raised revenues. In November 2009, the Nicaraguan government sent to Congress a project of tax reform aiming at reducing exemptions and modernizing the tax system (through the introduction of a dual income tax system and rules to deal with transfer pricing and thin capitalization). The portion of the project that was approved, included the elimination of exemptions to excises, the broadening of the income tax base, and the introduction of a 1 percent minimum income tax on gross income. The reform was expected to increase tax revenues by over 1 percent of GDP. However, its greatest virtue was to improve the efficiency and equity of the tax system by eliminating exemptions without increasing tax rates.

Despite this progress, the Nicaraguan tax system continues to be plagued by a large number of loopholes, particularly in value-added (VAT) and corporate income (CIT) taxes. The continued granting of exemptions and tax preferences has narrowed both tax bases. Tax expenditures (which measure in a point in time how much revenue would be collected if all exemptions, benefits, and loopholes were eliminated) were estimated at 7.6 percent of GDP in 2010—one of the highest in Latin America.

The authorities are considering a new tax reform. The reform would aim at streamlining exemptions, simplifying the tax system, and protecting the CIT base. The authorities plan to consult with different stakeholders before sending a proposal to Congress.

The key components of this new reform would yield important revenue gains. Tax revenues could increase by about 0.4 percent of GDP if exemptions of VAT on goods and services are reduced (including domestic airline tickets—which are taxed in most countries in the region—the consumption of potable water over a threshold, clothing, meat, fruits, and other foodstuff). Transfers through the direct tax system could alleviate the impact on the poor from ending some of these exemptions.

Additional measures could include (i) ending the differential tax treatment of interest income for companies; (ii) increasing withholding rates on payments to nonresidents; (iii) raising the personal income tax minimum exemption; (iv) introducing rules to address transfer pricing and thin capitalization; and (v) gradually lowering sectoral tax incentives. Authorities also could start taxing dividends from companies operating in free trade zones and exempted activities (as it is done in other countries of the region) to allow revenue-neutral reductions in current CIT rates. The tax system could also be simplified by replacing the very complex scheme for small businesses and reducing the number of goods and services subject to excises.



Source: Fund staff calculations.

Strengthening the international reserves position

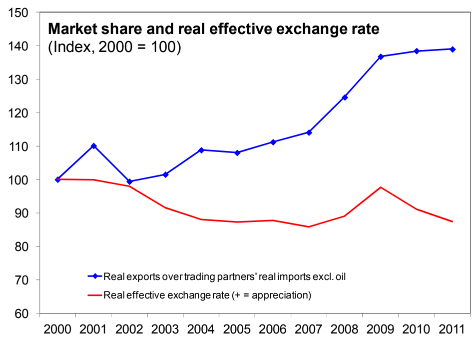
25. Staff argued that Nicaragua's balance of payments remained a key source of vulnerability. Staff noted that even if oil prices and concessional flows remain broadly in line with its baseline assumptions, the ratio of international reserves to imports would trend down, although the real exchange rate would be broadly appropriate (Box 3 and Selected Issues Paper, Chapter 2). However, if concessional flows were substantially lower and/or oil prices significantly higher, Nicaragua's balance of payments would be under severe pressure. The authorities recognized the vulnerability of the Nicaraguan economy to increases in oil prices but they did not see risks of a large decline in concessional inflows. At the same time, they agreed that a higher reserve coverage accompanied by structural reforms aimed at reducing the economy's dependency on oil imports and concessional flows should be the cornerstone of a strategy to ensure medium-term external sustainability. Staff noted that recurring increases in public sector wages and minimum wages could undermine competitiveness and compromise external sustainability.

Alternative scenario

26. A scenario where reforms in the tax system, social security, and the financial framework for the electricity sector resulted in higher growth rates and lower fiscal and external vulnerabilities was discussed with the authorities. The scenario assumed that the additional revenues from the tax reforms currently under discussion would be channeled to public investment to boost growth. Electricity sector reform would lower central government transfers (thus, reducing the fiscal deficit) and raise incentives for oil-saving investment in the sector (hence, mitigating external risks). The social security reform would eliminate the main source of long-term fiscal pressure, and deepen considerably the medium-term fiscal adjustment. The scenario would generate higher medium-term growth of about ½ percentage point. Staff argued that a larger increase in growth rates would necessitate institutional reforms including improving

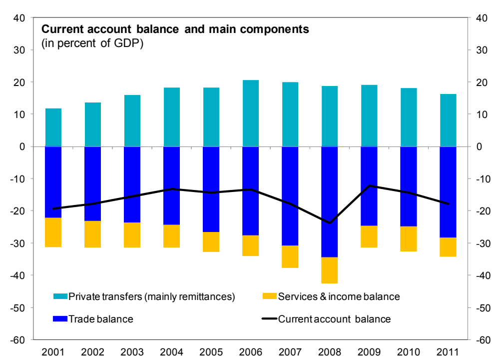
Box 3. Exchange Rate Assessment and External Competitiveness

Nicaragua's external competitiveness has improved steadily since the early 2000s. Nicaraguan exports have increased as a share of trading partners' non-oil imports. In addition, the



share of maquila exports in the U.S. market has risen significantly—largely a result of the sector's dynamism.

Despite these competitiveness gains, Nicaragua has continued to post large current account deficits. In large part, those deficits are the result of the country's extreme dependency on oil imports. Over the medium term, the projected increase in

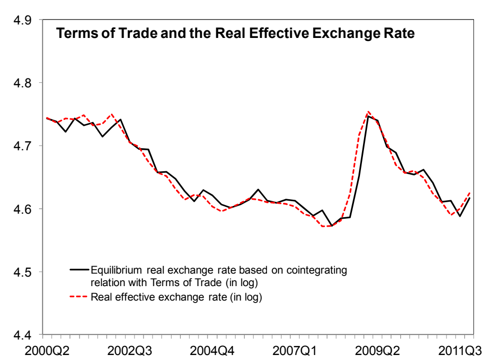


alternative sources of energy is expected to reduce oil imports and gradually lower the external current account deficit. Until these improvements in energy generation materialize, dependence on external financing poses a risk to Nicaragua's balance of payments. The high degree of dollarization of Nicaragua's banking system is an additional risk.

Non-price competitiveness indicators are not that favorable. Nicaragua ranks at the bottom half of assessed countries in surveys of the cost of doing business and other structural conditions, and its score are generally lower than those of its neighbors. However, the country's ranking in some key aspects has improved recently (Selected Issues Paper, Chapter 2).

Under the staff's baseline assumptions for oil prices and official assistance flows, Nicaragua's real exchange rate seems broadly in line with fundamentals (Selected Issues Paper, Chapter 2). The macroeconomic balance approach suggests an overvaluation of about 3 percent, while the external sustainability approach suggests that a depreciation of about 5 percent would be needed to stabilize the net foreign asset position of the country at its current, relatively high, negative level. These estimates need to be treated with caution as the staff's baseline projects substantial structural changes beyond the time horizon considered in the standard CGER methodology.

Real exchange rate movements are highly correlated with terms-of-trade fluctuations. Estimation of a simple cointegrating relationship between the two variables suggests that the real exchange rate is broadly in line with this fundamental.



the quality of government services and institutions. The authorities agreed with using some of the additional resources from reforms to increase capital spending, while controlling current spending and deepening the fiscal adjustment.

Containing financial sector vulnerabilities

27. Staff noted that Nicaragua's financial system remains resilient but pockets of vulnerability had to be addressed. Nicaraguan banks have large liquidity buffers and—according to recent stress tests conducted jointly with Fund staff—hold sufficient capital to withstand unexpected declines in loan quality. However, deposits linked to Venezuela's assistance programs are increasingly large and potentially volatile. The authorities noted that these dollar deposits are matched by liquid investments abroad, and pose little risk to the system. Staff welcomed the close coordination between the central bank and the superintendency of banks in conducting and evaluating stress tests, as well as in the context of the Committee for Crisis Resolution. Staff also welcomed the new on-site bank monitoring system and encouraged coordination across Central American bank supervisors to strengthen the supervision of domestic banks with a regional presence.

28. There has been progress in financial regulation and supervision. The new supervisory agency for micro-financial institutions has received budget resources to start operations and large financial cooperatives are expected to report their balance sheets on a comparable basis in the second half of 2012. Also, the authorities are discussing with key stakeholders a draft law creating a Financial Intelligence Unit (FIU), which would be in charge of preventing and combating anti-money laundering and the financing of terrorism (AML/CFT). Staff welcomed the initiative and the broad debate on the subject, but advised the authorities to use this opportunity to improve the AML/CFT framework in line with the Financial Action Task Force (FATF) standards, and the recommendations of the 2009 Caribbean Financial Action Task Force (CFATF) mutual evaluation report.

29. Staff recommended improving the infrastructure for monetary operations and the payments system, which would help deepening Nicaragua's inter-bank market. Staff welcomed recent improvements in liquidity projections and the planned transition to weekly (from monthly) cash-flow transactions, in the context of an enhanced coordination between the central bank and the ministry of finance. Plans to improve the efficiency of Nicaragua's payments system, including by designating the central bank as its sole supervisor and regulator, defining rules and responsibilities for market participants, and developing a system for money transfers in real time were also welcomed. Staff noted that these measures would help develop Nicaragua's inter-bank market, thus helping to lower the large levels of liquidity in the banking system.

STATISTICAL ISSUES

30. **An ongoing national accounts revision points to significantly higher GDP levels**. This work, supported by technical assistance from CAPTAC–DR, uses improved source surveys and statistical procedures (including in the areas of labor market statistics, balance of payments, and monetary accounts) and a new base year (2006). Preliminary results show that nominal GDP for 2006 will be revised up significantly, suggesting that the fiscal and external ratios of recent years could be markedly lower than currently estimated. Staff strongly welcomed the methodological improvements in the measurement of GDP and urged the authorities to publish a complete series with data up to 2011 as soon as possible.

31. **Data for the consolidated public sector do not encompass all state-owned enterprises and public agencies**. Staff noted that the current CPS definition excluded some large state-owned enterprises, which hampered a comprehensive analysis of government accounts. The authorities agreed that the CPS concept should be expanded.

STAFF APPRAISAL

32. **Prudent economic management and some important reforms have helped Nicaragua establish a record of macroeconomic stability and growth in recent years**. Helped by favorable export prices, resilient concessional assistance, and strong FDI, the Nicaraguan economy rebounded rapidly from the 2008-09 crisis. Tax revenues surged following a well-conceived tax reform and, with the help of expenditure restraint, turned fiscal deficits into a surplus in 2011. In addition, inflation

has remained stable and international reserves have increased.

33. Renewed public spending pressures should be contained. Adding the Venezuela-financed wage bonus to the government wage bill would materialize a fiscal risk flagged by staff in the past, and subsequently acknowledged by the authorities. Higher transfers to the electricity sector (including protecting the poor) and other spending pressures are also important risks. The authorities should resist accommodating all extra spending pressures, which would jeopardize their resolution to produce a central government deficit at or below ½ percent of GDP in 2012.

34. Attaining higher rates of growth to reduce poverty would require strengthening institutions, raising the effectiveness of public spending, and reducing labor market informality. Better auditing and supervision of government agencies, and further strengthening property rights would improve perceptions about institutions in the country. Reducing budget rigidities and earmarking is key to enhancing the efficiency and effectiveness of public spending (including in education). Continuing supervision of labor relations, reducing red tape for small and medium-sized firms, and introducing flexible social security schemes, would help reducing informality, thus raising incentives for human capital accumulation and firms' growth.

35. Improving infrastructure is fundamental to boost Nicaragua's productive potential. On the electricity sector, developing a tariff-setting framework that takes into account medium-term costs, electricity losses during distribution, and transfers to the poor is urgently needed to bring long-term sustainability to the sector and attract new investments. More broadly, it is necessary to increase infrastructure investment, including with public-private partnerships.

36. Fiscal consolidation should be the cornerstone of the government's economic policy. Given the large public investment needs, consolidation should be anchored on current spending restraint and broadening of the tax base. Staff urges the authorities to keep the momentum of recent tax reforms and work on eliminating remaining tax exemptions, reforming aspects of the corporate income tax, and reducing the complexity of the tax scheme for small businesses. The revenues obtained from these reforms could be used to raise public investment in infrastructure.

37. Reforming the pension system is necessary for fiscal sustainability. Changes in the pension benefits formula and gradual increases in retirement age should be adopted as early as possible.

More broadly, the reform should avoid increasing incentives for informality.

38. Reducing external vulnerabilities is another fundamental challenge. Plans to lower Nicaragua's dependence on oil imports should be given high priority. Building higher international reserves buffers to increase protection against shocks to the balance of payments should be a key monetary policy objective. Containing minimum wage increases and enacting productivity-boosting reforms would help safeguarding external competitiveness.

39. The financial sector has been resilient, but remaining vulnerabilities should be addressed. Staff welcomes the progress in developing and implementing stress-testing models for the banking system. Improving regional collaboration across national supervisors would further limit chances of banking stress. Staff welcomes current and planned measures to enhance Nicaragua's payments system, which will help to develop an inter-bank market in the country. Staff also welcomes the progress in setting up the supervisor of microfinance corporations and the broad discussion on the creation of a FIU. Staff recommends carefully reviewing and revising the draft law creating this unit to ensure that the intended improvements are made in accordance with the FATF standards and the recommendations of the 2009 CFATF report. The publication of comparable balance sheets for large financial cooperatives will improve the transparency of the use of concessional flows, including those from Venezuela.

40. Staff recommends that the next Article IV consultation takes place on the standard 12-month cycle.

Table 1. Nicaragua: Selected Social and Economic Indicators, 2008–13

I. Social and Demographic Indicators

Main export products: coffee, sugar (ethanol), meat, gold.

GDP per capita (current U.S. dollars, 2010)	1,136	Share of national income of richest 10 percent	41.8
GNI per capita 2010 (Atlas method, current US$)	1,110	Unemployment (percent labor force, 2010)	7.8
GINI Index (2009)	46.0	Poverty rate (national pov. line, in percent, 2009)	42.5
Population (millions, 2010)	5.8	Adult literacy rate (percent, 2009)	83.0
Life expectancy at birth in years (2010)	74.0	Infant mortality rate (per 1,000 live births, 2010)	23.0

II. Economic Indicators

	2008	2009	2010	2011	2012	2013
				Est.	Proj.	
Real sector			(Percent)			
GDP growth	2.8	-1.5	4.5	4.7	3.7	4.0
GDP deflator	15.0	3.9	6.0	11.1	8.6	7.9
Consumer price inflation						
End of period	13.8	0.9	9.2	8.0	8.6	7.5
Period average	19.8	3.7	5.5	8.1	9.2	7.9
External sector			(US$ millions)			
Current account	-1,570	-832	-969	-1,311	-1,677	-1,591
Exports of goods, f.o.b	2,530	2,390	3,157	4,057	4,474	4,828
Imports of goods, f.o.b.	-4,731	-3,929	-4,792	-6,125	-6,869	-7,197
Of which: oil	-963	-676	-751	-1,216	-1,332	-1,229
Capital and financial account [1/]	1,535	1,224	1,164	1,374	1,653	1,692
Of which: FDI	626	434	508	968	829	799
			(Percent of GDP; unless otherwise indicated)			
Current account	-24.6	-13.4	-14.7	-18.0	-21.4	-19.0
Exports of goods, f.o.b	39.7	38.5	47.9	55.6	57.2	57.7
Imports of goods, f.o.b.	-74.2	-63.2	-72.7	-83.9	-87.7	-86.1
Of which: oil	-15.1	-10.9	-11.4	-16.7	-17.0	-14.7
Capital and financial account [1/]	24.1	19.7	17.7	18.8	21.1	20.2
Of which: FDI	9.8	7.0	7.7	13.3	10.6	9.6
Fiscal sector						
Central government overall balance, after grants	-1.2	-2.8	-1.0	0.6	-0.5	-0.4
Revenues	19.0	18.9	19.6	21.1	21.5	21.6
Expenditures [2/]	23.2	24.1	23.0	23.2	24.4	23.9
Grants [2/]	2.9	2.4	2.5	2.7	2.4	1.9
Rest of NFPS overall balance	0.4	0.9	0.4	-0.1	-0.9	-0.5
Central bank balance	-0.7	-1.2	-0.9	-0.4	-0.7	-0.4
Combined public sector (CPS) balance, before grants	-4.6	-6.5	-4.0	-2.9	-4.7	-3.5
CPS overall balance, after grants	-1.5	-3.1	-1.4	0.1	-2.1	-1.3
Financing	1.5	3.1	1.4	-0.1	2.1	1.3
External	1.9	3.9	3.3	2.6	2.9	3.3
Domestic (including BCN operating balance)	-0.3	-0.8	-1.9	-2.7	-0.8	-1.8
Public sector debt						
Total	74.8	80.1	78.0	71.8	68.7	65.8
Domestic	19.7	21.2	19.2	16.0	13.7	11.0
External [3/]	55.1	58.9	58.8	55.8	55.1	54.8
Memorandum items:						
GDP (US$ million)	6,372	6,214	6,591	7,297	7,828	8,363
Gross reserves (US$ m) [1/]	1,141	1,573	1,799	1,892	1,879	1,990
(in months of imports excl. maquilas)	*2.9*	*4.9*	*4.7*	*4.0*	*3.5*	*3.6*
Net international reserves [1/]	1,030	1,423	1,632	1,711	1,697	1,809
Net international reserves (adjusted) [4/]	710	811	917	1,023	1,002	1,096
SDR allocations	…	165	165	165	165	165
Reserves on foreign deposits	320	447	550	522	530	548
Short-term liabilities	111	150	167	182	181	181
Oil price (average, US$/bbl)	97.0	61.8	79.0	104.0	114.7	110.0

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

[1/] Starting in 2009, figures include the SDR allocation for SDR105.1 million (US$165 million) of September 2009.

[2/] Figures for 2010-12 include off-budget wage bonus.

[3/] Actual and projection are based on the 2011 DSA Update. Estimates up to 2010 correspond to the legal situation.

[4/] Includes deposit insurance fund (FOGADE) and excludes the September 2009 SDR allocation and reserve requirements of commercial banks in foreign currency.

Table 2a. Nicaragua: Operations of the Central Government, 2009–16
(Millions of Córdobas)

	2009	2010	2011	2012	2013	2014	2015	2016
			Est.			Proj.		
Total Revenue	**23,859**	**27,575**	**34,548**	**39,610**	**44,620**	**50,045**	**55,974**	**62,516**
Tax	22,175	25,530	31,752	36,414	41,035	46,049	51,529	57,570
Income and property	7,865	8,481	11,335	13,108	14,682	16,364	18,458	20,654
VAT	3,885	4,028	4,605	5,226	5,790	6,546	7,178	8,102
Excises	3,339	5,541	6,070	6,875	7,858	8,850	9,998	11,126
Other	7,086	7,480	9,742	11,205	12,704	14,290	15,895	17,688
Nontax revenue	1,684	2,045	2,796	3,196	3,585	3,995	4,444	4,946
Total Expenditure	**30,424**	**32,430**	**37,932**	**44,919**	**49,384**	**55,128**	**61,590**	**68,572**
Current expenditures[1/]	23,410	24,866	29,660	34,896	37,804	41,991	46,720	51,741
Wages and salaries[2/]	8,615	9,603	11,294	12,325	13,450	14,836	16,253	18,086
of which: bonus	0	670	1,238	1,339	…	…	…	…
Goods and services	4,652	4,863	6,341	7,891	8,065	8,989	10,101	11,240
Interest	1,711	1,991	2,262	2,783	2,930	3,185	3,601	3,757
of which: external[3/]	553	595	709	886	1,068	1,228	1,346	1,407
Current transfers[4/]	8,432	8,409	9,763	11,897	13,359	14,981	16,766	18,657
Capital Expenditures[1/]	6,977	7,564	8,272	10,023	11,581	13,137	14,869	16,832
Domestically financed	904	1,699	2,023	2,650	2,895	3,457	4,102	4,850
Externally financed	6,073	5,866	6,249	7,373	8,685	9,680	10,767	11,982
Net lending	37	0	0	0	0	0	0	0
Overall balance (before grants)	**-6,564**	**-4,855**	**-3,384**	**-5,309**	**-4,771**	**-5,083**	**-5,616**	**-6,057**
Grants[5/]	3,080	3,504	4,389	4,358	3,929	4,379	4,871	5,420
of which: Project-related[6/]	2,742	2,396	3,151	3,636	3,929	4,379	4,871	5,420
Primary balance (after grants)	**-1,774**	**639**	**3,267**	**1,832**	**2,088**	**2,481**	**2,856**	**3,121**
Overall balance (after grants)	**-3,485**	**-1,351**	**1,006**	**-951**	**-842**	**-704**	**-745**	**-636**
Net Financing	**3,485**	**1,351**	**-1,006**	**951**	**842**	**704**	**745**	**636**
External	4,019	3,458	3,266	3,332	4,473	4,593	4,771	5,142
Amortizations[3/]	-911	-922	-865	-1,462	-1,396	-1,876	-2,352	-2,708
Disbursements	4,930	4,380	4,131	4,794	5,869	6,469	7,123	7,850
Project-related[6/]	3,331	3,470	3,097	3,736	4,756	5,301	5,896	6,561
Budget support[7/]	1,599	910	1,033	1,058	1,113	1,168	1,227	1,288
Domestic	-535	-2,107	-4,272	-2,381	-3,631	-3,889	-4,026	-4,506
Central Bank	-824	-2,204	-1,553	-366	-2,012	-2,998	-2,249	-2,538
Commercial Banks	-19	66	-228	0	0	0	0	0
Amortizations (gross)	-2,313	-2,864	-2,780	-5,228	-4,503	-4,149	-4,262	-4,291
Bonds issuance[8/]	2,414	2,555	2,312	2,867	4,204	4,502	3,408	3,578
Others[9/]	207	340	-2,023	345	-1,320	-1,245	-923	-1,255
Memorandum items:								
Monitorable wage bill[10/]	10,153	11,301	13,121	13,241	15,591	17,198	18,840	20,965
Poverty related expenditure	17,024	18,107	20,686	24,081	27,297	31,114	35,635	40,510
Central Government primary spending[11/]	28,713	30,440	35,670	42,136	46,455	51,943	57,989	64,815

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

Note: Some aggregates may not add up due to rounding.

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

2/ For 2010–12, it includes the off-budgetary wage bonus financed with Venezuela-related resources. From 2013 onward, the wage bonus is assumed to be absorbed by budget without counterpart of grant financing.

3/ Debt service is measured on accrual basis.

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

5/ For 2010–12, it includes the off-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/ The authorities' budget includes a US$45 million budget support loan from the IDB for 2012. This loan is still subject to approval by the IDBs' Board of Directors.

8/ It includes issuance of central government bonds to the social security institute (INSS).

9/ 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.

10/ It includes the wage bill of all decentralized agencies of the central government; and the extra-budgetary wage bonus.

11/ It includes the extra-budgetary wage bonus.

Table 2b. Nicaragua: Operations of the Central Government, 2009–16
(Percent of GDP)

	2009	2010	2011	2012	2013	2014	2015	2016
			Est.			Proj.		
Total Revenue	**18.9**	**19.6**	**21.1**	**21.5**	**21.6**	**21.7**	**21.8**	**21.9**
Tax	17.5	18.1	19.4	19.8	19.8	20.0	20.1	20.2
Income and property	6.2	6.0	6.9	7.1	7.1	7.1	7.2	7.2
VAT	3.1	2.9	2.8	2.8	2.8	2.8	2.8	2.8
Excises	2.6	3.9	3.7	3.7	3.8	3.8	3.9	3.9
Other	5.6	5.3	6.0	6.1	6.1	6.2	6.2	6.2
Nontax and current transfers	1.3	1.5	1.7	1.7	1.7	1.7	1.7	1.7
Total Expenditure	**24.1**	**23.0**	**23.2**	**24.4**	**23.9**	**23.9**	**24.0**	**24.0**
Current expenditures[1/]	18.5	17.7	18.1	18.9	18.3	18.2	18.2	18.1
Wages and salaries[2/]	6.8	6.8	6.9	6.7	6.5	6.4	6.3	6.3
of which: bonus	0.0	0.5	0.8	0.7	…	…	…	…
Goods and services	3.7	3.5	3.9	4.3	3.9	3.9	3.9	3.9
Interest	1.4	1.4	1.4	1.5	1.4	1.4	1.4	1.3
of which: external[3/]	0.4	0.4	0.4	0.5	0.5	0.5	0.5	0.5
Current transfers[4/]	6.7	6.0	6.0	6.5	6.5	6.5	6.5	6.5
Capital Expenditures[1/]	5.5	5.4	5.1	5.4	5.6	5.7	5.8	5.9
Domestically financed	0.7	1.2	1.2	1.4	1.4	1.5	1.6	1.7
Externally financed	4.8	4.2	3.8	4.0	4.2	4.2	4.2	4.2
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (before grants)	**-5.2**	**-3.4**	**-2.1**	**-2.9**	**-2.3**	**-2.2**	**-2.2**	**-2.1**
Grants[5/]	2.4	2.5	2.7	2.4	1.9	1.9	1.9	1.9
of which: Project-related[4/]	2.2	1.7	1.9	2.0	1.9	1.9	1.9	1.9
Primary balance (after grants)	**-1.4**	**0.5**	**2.0**	**1.0**	**1.0**	**1.1**	**1.1**	**1.1**
Overall balance (after grants)	**-2.8**	**-1.0**	**0.6**	**-0.5**	**-0.4**	**-0.3**	**-0.3**	**-0.2**
Net Financing	**2.8**	**1.0**	**-0.6**	**0.5**	**0.4**	**0.3**	**0.3**	**0.2**
External	3.2	2.5	2.0	1.8	2.2	2.0	1.9	1.8
Amortizations[3/]	-0.7	-0.7	-0.5	-0.8	-0.7	-0.8	-0.9	-0.9
Disbursements	3.9	3.1	2.5	2.6	2.8	2.8	2.8	2.8
Project-related[6/]	2.6	2.5	1.9	2.0	2.3	2.3	2.3	2.3
Budget support[7/]	1.3	0.6	0.6	0.6	0.5	0.5	0.5	0.5
Domestic	-0.4	-1.5	-2.6	-1.3	-1.8	-1.7	-1.6	-1.6
Central Bank	-0.7	-1.6	-0.9	-0.2	-1.0	-1.3	-0.9	-0.9
Commercial Banks	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Amortizations (gross)	-1.8	-2.0	-1.7	-2.8	-2.2	-1.8	-1.7	-1.5
Bonds issuance[8/]	1.9	1.8	1.4	1.6	2.0	2.0	1.3	1.3
Others[9/]	0.2	0.2	-1.2	0.2	-0.6	-0.5	-0.4	-0.4
Memorandum items:								
Monitorable wage bill[10/]	8.0	8.0	8.0	7.2	7.5	7.5	7.3	7.3
Poverty related expenditure	13.5	12.9	12.6	13.1	13.2	13.5	13.9	14.2
Central Government primary spending[11/]	22.7	21.6	21.8	22.9	22.5	22.5	22.6	22.7

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

Note: Some aggregates may not add up due to rounding.

[1/] Starting in 2008, a portion of capital spending was reclassified to current spending, namely wages and goods and services.

[2/] For 2010–12, it includes the off-budgetary wage bonus financed with Venezuela-related resources. From 2013 onward, the wage bonus is assumed to be absorbed by budget without counterpart of grant financing.

[3/] Debt service is measured on accrual basis.

[4/] Current transfers in 2009 includes payment of arrears to the electricity sector for US$28 million.

[5/] For 2010–12, it includes the off-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/] The authorities' budget includes a US$45 million budget support loan from the IDB for 2012. This loan is still subject to approval by the IDBs' Board of Directors.

[8/] It includes issuance of central government bonds to the social security institute (INSS).

[9/] 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.

[10/] It includes the wage bill of all decentralized agencies of the central government; and the extra-budgetary wage bonus.

[11/] It includes the extra-budgetary wage bonus.

Table 3a. Nicaragua: Operations of the Combined Public Sector, 2009–16
(Millions of Córdobas)

	2009	2010	2011	2012	2013	2014	2015	2016
			Est.			Proj.		
Central government overall balance	**-3,485**	**-1,351**	**1,006**	**-951**	**-842**	**-704**	**-745**	**-636**
Revenue	23,859	27,575	34,548	39,610	44,620	50,045	55,974	62,516
Expenditure[1/]	30,424	32,430	37,932	44,919	49,384	55,128	61,590	68,572
Current	23,410	24,866	29,660	34,896	37,804	41,991	46,720	51,741
of which: interest	1,711	1,991	2,262	2,783	2,930	3,185	3,601	3,757
Capital and net lending[2/]	7,013	7,564	8,272	10,023	11,581	13,137	14,869	16,832
Grants[3/]	3,080	3,504	4,389	4,358	3,929	4,379	4,871	5,420
Social Security Institute (INSS) balance	**784**	**1,492**	**1,449**	**494**	**1,042**	**981**	**991**	**474**
Contributions and revenues	7,783	9,627	10,875	11,355	12,742	14,037	15,433	16,946
Payments and expenses	6,999	8,135	9,440	10,864	11,700	13,056	14,442	16,472
Grants	0	0	14	3	0	0	0	0
Managua municipality (ALMA) balance	**60**	**86**	**-83**	**288**	**7**	**27**	**49**	**37**
of which: Grants	31	23	17	238	0	0	0	0
Overall Public Enterprises balance[4/]	**255**	**-960**	**-1,579**	**-2,397**	**-2,068**	**-2,344**	**-2,189**	**-2,571**
Revenue	4,035	3,972	4,573	5,116	5,872	6,453	7,178	8,126
Expenditure	5,048	5,085	6,665	7,743	8,602	9,450	9,998	10,841
Grants[5/]	1,268	154	513	230	662	652	631	143
Central Bank (BCN) operating balance	**-1,514**	**-1,249**	**-656**	**-1,256**	**-798**	**-691**	**-769**	**-856**
Overall CPS balance (after grants)	**-3,899**	**-1,982**	**136**	**-3,821**	**-2,660**	**-2,731**	**-2,663**	**-3,552**
Primary balance (after grants)	-2,167	46	2,511	-926	355	600	1,101	388
Total interest	1,733	2,028	2,375	2,895	3,015	3,332	3,765	3,939
Net Financing	**3,900**	**1,982**	**-136**	**3,821**	**2,660**	**2,731**	**2,663**	**3,552**
External	4,874	4,706	4,317	5,343	6,907	7,478	7,746	7,176
Amortizations	-931	-940	-996	-1,491	-1,427	-1,968	-2,449	-2,809
Disbursements[3/]	5,805	5,647	5,313	6,834	8,333	9,446	10,194	9,985
Domestic	-2,488	-3,973	-5,110	-2,777	-5,045	-5,438	-5,852	-4,480
Central Bank	-865	-780	94	-392	-848	-2,213	-1,230	-169
Commercial Banks	392	-2,243	-1,202	-229	-1,721	-1,918	-2,133	-2,374
Amortizations (gross)	-2,069	-1,828	-2,780	-4,174	-3,227	-2,066	-3,441	-2,586
Bonds issuance[6/]	807	1,156	429	2,373	1,164	1,220	1,466	1,487
Others[7/]	-753	-279	-1,650	-354	-414	-461	-513	-839
Central Bank (BCN) operating balance	1,514	1,249	656	1,256	798	691	769	856
Memorandum items:								
CPS primary balance (before grants)	-6,545	-3,634	-2,422	-5,755	-4,236	-4,431	-4,400	-5,176
CPS overall balance (before grants)	-8,278	-5,662	-4,797	-8,650	-7,251	-7,763	-8,165	-9,115

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

Note: Some aggregates may not add up due to rounding.

[1/] For 2010–12, it includes the off-budgetary wage bonus financed with Venezuela-related resources. From 2013 onward, the wage bonus is assumed to be absorbed by budget without counterpart of grant financing.

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

[3/] In 2010, a project-loan for US$17 million was reclassified into a grant. For 2010 and 2011, it includes the off-budgetary grant from Venezuela to finance the wage bonus.

[4/] It includes the state-owned water, electricity generation, electricity transmission, and port companies, as well as the telecommunications regulatory agency.

[5/] It includes a project grant for US$49.5 million received in December 2009 by the state-owned water company.

[6/] It nets out purchases of central government bonds by the social security institute (INSS).

[7/] 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.

Table 3b. Nicaragua: Operations of the Combined Public Sector, 2009–16

(Percent of GDP)

	2009	2010	2011	2012	2013	2014	2015	2016
			Est.			Proj.		
Central government overall balance	**-2.8**	**-1.0**	**0.6**	**-0.5**	**-0.4**	**-0.3**	**-0.3**	**-0.2**
Revenue	18.9	19.6	21.1	21.5	21.6	21.7	21.8	21.9
Expenditure[1/]	24.1	23.0	23.2	24.4	23.9	23.9	24.0	24.0
Current	18.5	17.7	18.1	18.9	18.3	18.2	18.2	18.1
of which: interest	1.4	1.4	1.4	1.5	1.4	1.4	1.4	1.3
Capital and net lending[2/]	5.5	5.4	5.1	5.4	5.6	5.7	5.8	5.9
Grants[3/]	2.4	2.5	2.7	2.4	1.9	1.9	1.9	1.9
Social Security Institute (INSS) balance	**0.6**	**1.1**	**0.9**	**0.3**	**0.5**	**0.4**	**0.4**	**0.2**
Contributions and revenues	6.2	6.8	6.6	6.2	6.2	6.1	6.0	5.9
Payments and expenses	5.5	5.8	5.8	5.9	5.7	5.7	5.6	5.8
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Managua municipality (ALMA) balance	**0.0**	**0.1**	**-0.1**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**
of which: Grants	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0
Overall Public Enterprises balance[4/]	**0.2**	**-0.7**	**-1.0**	**-1.3**	**-1.0**	**-1.0**	**-0.9**	**-0.9**
Revenue	3.2	2.8	2.8	2.8	2.8	2.8	2.8	2.8
Expenditure	4.0	3.6	4.1	4.2	4.2	4.1	3.9	3.8
Grants[5/]	1.0	0.1	0.3	0.1	0.3	0.3	0.2	0.1
Central Bank (BCN) operating balance	**-1.2**	**-0.9**	**-0.4**	**-0.7**	**-0.4**	**-0.3**	**-0.3**	**-0.3**
Overall CPS balance (after grants)	**-3.1**	**-1.4**	**0.1**	**-2.1**	**-1.3**	**-1.2**	**-1.0**	**-1.2**
Primary balance (after grants)	-1.7	0.0	1.5	-0.5	0.2	0.3	0.4	0.1
Total interest	1.4	1.4	1.5	1.6	1.5	1.4	1.5	1.4
Net Financing	**3.1**	**1.4**	**-0.1**	**2.1**	**1.3**	**1.2**	**1.0**	**1.2**
External	3.9	3.3	2.6	2.9	3.3	3.2	3.0	2.5
Amortizations	-0.7	-0.7	-0.6	-0.8	-0.7	-0.9	-1.0	-1.0
Disbursements[3/]	4.6	4.0	3.2	3.7	4.0	4.1	4.0	3.5
Domestic	-2.0	-2.8	-3.1	-1.5	-2.4	-2.4	-2.3	-1.6
Central Bank	-0.7	-0.6	0.1	-0.2	-0.4	-1.0	-0.5	-0.1
Commercial Banks	0.3	-1.6	-0.7	-0.1	-0.8	-0.8	-0.8	-0.8
Amortizations (gross)	-1.6	-1.3	-1.7	-2.3	-1.6	-0.9	-1.3	-0.9
Bonds issuance[6/]	0.6	0.8	0.3	1.3	0.6	0.5	0.6	0.5
Others[7/]	-0.6	-0.2	-1.0	-0.2	-0.2	-0.2	-0.2	-0.3
Central Bank (BCN) operating balance	1.2	0.9	0.4	0.7	0.4	0.3	0.3	0.3
Memorandum items:								
CPS primary balance (before grants)	-5.2	-2.6	-1.5	-3.1	-2.0	-1.9	-1.7	-1.8
CPS overall balance (before grants)	-6.5	-4.0	-2.9	-4.7	-3.5	-3.4	-3.2	-3.2

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

Note: Some aggregates may not add up due to rounding.

[1/] For 2010–12, it includes the off-budgetary wage bonus financed with Venezuela-related resources. From 2013 onward, the wage bonus is assumed to be absorbed by budget without counterpart of grant financing.

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

[3/] In 2010, a project-loan for US$17 million was reclassified into a grant. For 2010 and 2011, it includes the off-budgetary grant from Venezuela to finance the wage bonus.

[4/] It includes the state-owned water, electricity generation, electricity transmission, and port companies, as well as the telecommunications regulatory agency.

[5/] It includes a project grant for US$49.5 million received in December 2009 by the state-owned water company.

[6/] It nets out purchases of central government bonds by the social security institute (INSS).

[7/] 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.

Table 4. Nicaragua: Summary Accounts of the Central Bank, 2008–13
(Flows in millions of córdobas; unless otherwise indicated)

	2008	2009	2010	2011	2012	2013
				Est.	Proj.	
Exchange rate (córdobas/US$, period average)	19.4	20.3	21.4	22.4	23.6	24.7
Net international reserves (adjusted)[1/]	**-532**	**2,068**	**2,249**	**2,397**	**-505**	**2,335**
(In US$ millions)	-27	102	105	107	-21	94
Net domestic assets	**494**	**-1,409**	**-181**	**-936**	**1,605**	**-949**
Net credit to public sector (NFPS)[2/]	3,230	-808	-2,204	-1,553	-366	-2,012
Net credit to central government	932	-824	-2,204	-1,553	-366	-2,012
Net credit to RNFPS	2,299	16	0	0	0	0
Net credit to the financial system	-694	-1,529	-198	-2,379	-761	-670
Operational losses	848	1,514	1,249	656	1,256	798
Central bank bonds (net)	-3,102	-875	708	1,602	836	197
Medium- and long-term foreign liabilities	258	329	362	388	520	390
Other	-47	-38	-98	349	120	347
Currency	**-38**	**659**	**2,068**	**1,461**	**1,100**	**1,386**
Memorandum items:						
Gross reserves (US$ million, stock)[3/]	1,141	1,573	1,799	1,892	1,879	1,990
Net international reserves	1,030	1,423	1,632	1,711	1,697	1,809
Net international reserves (adjusted)[1/]	**710**	**811**	**917**	**1,023**	**1,002**	**1,096**
SDR allocations	…	165	165	165	165	165
Reserves on foreign currency deposits	320	447	550	522	530	548
Short-term liabilities	111	150	167	182	181	181
Central Bank paper (stock)	7,321	8,196	7,488	5,886	5,050	4,852
in percent of GDP	*5.9*	*6.5*	*5.3*	*3.6*	*2.7*	*2.3*
Currency (stock)	5,499	6,157	8,225	9,686	10,786	12,172
Year-on-year growth (percent)	*-0.7*	*12.0*	*33.6*	*17.8*	*11.4*	*12.8*

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

[1/]Program definition. Includes deposit insurance fund (FOGADE), and excludes 2009 SDR allocation and actual reserves of commercial banks in foreign currency.

[2/]Includes only "Titulos Especiales de Inversion."

[3/]Starting in 2009, figures include the SDR allocation for SDR105.1 million (US$165 million) of September 2009.

Table 5. Nicaragua: Summary Accounts of Deposit Banks and the Financial System, 2008–13
(Flows in millions of córdobas; unless otherwise indicated)

	2008	2009	2010	2011	2012	2013
				Est.	Proj.	
			Commercial banks[1/]			
Net international reserves (adjusted)	**1,959**	**5,770**	**5,814**	**-874**	**2,697**	**344**
(in US$ millions)	102	313	137	-81	115	14
Net domestic assets	**1,239**	**-1,541**	**-2,070**	**12,304**	**8,297**	**12,553**
Net credit to nonfinancial public sector	-794	-692	1,713	-1,379	-761	5,918
Net credit to the financial system	-650	-1,488	-9,297	2,994	2,827	2,765
Net credit to the private sector	5,142	-3,479	2,539	7,065	2,886	3,167
Medium- and long-term foreign liabilities	-1,985	1,290	1,239	1,164	1,023	1,212
Other net assets	-474	2,828	1,736	2,460	2,323	-509
Liabilities	**3,198**	**4,229**	**3,744**	**11,430**	**10,994**	**12,897**
			Financial sector[2/]			
Net international reserves (adjusted)[3/]	**1,453**	**8,428**	**5,165**	**591**	**2,192**	**2,679**
(in US$ millions)	75	414	242	26	93	108
Net domestic assets	**1,733**	**-2,950**	**-2,251**	**11,368**	**9,902**	**12,553**
Net credit to nonfinancial public sector	2,436	-1,501	-491	-2,932	-1,127	3,906
Net credit to the private sector	5,142	-3,479	2,539	7,065	2,886	3,167
Medium- and long-term foreign liabilities	-1,727	1,618	1,601	1,551	1,543	1,602
Other net assets	-4,119	410	-5,900	5,683	6,600	3,878
Of which: Other financial institutions	-1,282	-3,150	-4,814	-1,274	-892	-624
Liabilities to the private sector	**3,186**	**5,478**	**2,914**	**11,958**	**12,094**	**15,232**
Memorandum items:						
Credit to the private sector (percent of GDP)	37.6	33.9	32.2	32.0	30.3	29.6
Credit to the private sector (year-on-year, percent)	12.5	-7.5	5.9	15.6	6.4	9.7
Foreign currency deposits (percent of total)	68.5	71.8	73.1	73.4	73.4	73.4

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

[1/] Includes Financiera Nicaraguense and Sociedades Financieras.
[2/] Includes Central Bank of Nicaragua.
[3/] 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 6. Nicaragua: Medium-Term Balance of Payments, 2008–17[1/]
(In millions of U.S. dollars; unless otherwise indicated)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
				Est.			Proj.			
Current account	**-1,570**	**-832**	**-969**	**-1,311**	**-1,677**	**-1,591**	**-1,527**	**-1,563**	**-1,556**	**-1,539**
According to BPM5 [2/]	-1,517	-760	-947	*-1,311*	-1,677	-1,591	-1,527	-1,563	-1,556	-1,539
Trade balance	-2,201	-1,540	-1,636	-2,068	-2,394	-2,370	-2,336	-2,325	-2,352	-2,392
Exports, f.o.b.	2,530	2,390	3,157	4,057	4,474	4,828	5,210	5,618	5,989	6,312
Imports, f.o.b.	-4,731	-3,929	-4,792	-6,125	-6,869	-7,197	-7,546	-7,943	-8,342	-8,704
Of which: oil imports	-963	-676	-751	-1,216	-1,332	-1,229	-1,178	-1,126	-1,051	-996
Services	-269	-148	-222	-178	-237	-245	-257	-270	-285	-288
Receipts	460	496	472	660	710	739	782	815	850	955
Payments	-729	-644	-694	-838	-947	-984	-1,038	-1,084	-1,135	-1,243
Income	-240	-263	-284	-256	-280	-280	-320	-387	-378	-377
Credits	23	6	9	17	35	36	32	35	38	38
Debits	-263	-269	-293	-273	-315	-316	-352	-422	-415	-416
Of which: official interest	-36	-33	-31	-34	-39	-46	-52	-57	-57	-57
Transfers to the private sector	1,140	1,118	1,173	1,192	1,235	1,304	1,385	1,418	1,460	1,518
Of which: remittances	818	768	823	912	1,003	1,083	1,170	1,228	1,290	1,359
Capital and financial account	**1,535**	**1,224**	**1,164**	**1,374**	**1,653**	**1,692**	**1,641**	**1,634**	**1,501**	**1,549**
Official	479	714	395	431	427	476	492	489	410	416
Official transfers	347	300	186	249	166	193	206	218	199	224
Of which: grants	347	300	186	249	166	193	206	218	199	224
Disbursements[3/]	219	330	285	259	335	368	393	403	359	316
Amortization	-75	-81	-71	-69	-74	-85	-107	-132	-148	-124
Other	-13	165	-5	-8	0	0	0	0	0	0
Private	1,057	511	770	943	1,225	1,216	1,150	1,145	1,092	1,133
Foreign direct investment	626	434	508	968	829	799	806	836	840	864
Of which: ALBA collaboration		147	11	45	222	208	358	404	90	0
Capital Transfers	52	99	17	4	0	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	-28	397	417	343	309	252	269
Assets	-67	-211	-278	-18	-129	-205	-115	-114	-90	-140
Medium- and long-term liabilities	527	196	460	597	525	622	458	424	342	410
Of which: ALBA collaboration[4/ 5/]	293	232	509	510	573	492	444	412	328	281
Other, including errors and omissions[6/]	-81	-8	62	-608	0	0	0	0	0	0
Overall balance	**-35**	**392**	**195**	**64**	**-24**	**101**	**114**	**71**	**-54**	**10**
Change in gross official reserves (- increase)[7/]	-38	-432	-226	-93	14	-112	-121	-77	49	-15
Exceptional financing	72	40	30	30	11	11	7	6	5	5
Memorandum items:										
Current account (in percent of GDP)	**-24.6**	**-13.4**	**-14.7**	**-18.0**	**-21.4**	**-19.0**	**-17.2**	**-16.6**	**-15.6**	**-14.6**
According to BPM5 [2/]	-23.8	-12.2	-14.4	-18.0	-21.4	-19.0	-17.2	-16.6	-15.6	-14.6
Excluding official interest	-23.2	-11.7	-13.9	-17.5	-20.9	-18.5	-16.6	-16.0	-15.0	-14.0
Non-oil, excluding interest	-8.1	-0.8	-2.5	-0.8	-3.9	-3.8	-3.3	-4.0	-4.5	-4.6
Alba-related flows (in percent of GDP)	**7.2**	**7.1**	**7.9**	7.6	**10.2**	**8.4**	**9.0**	**8.7**	**4.2**	**2.7**
FDI	2.1	2.4	0.2	0.6	2.8	2.5	4.0	4.3	0.9	0.0
Oil collaboration	4.6	3.8	4.9	7.3	7.9	6.4	5.5	4.4	3.3	2.7
Others[5/]	0.5	0.9	2.8	-0.4	-0.6	-0.6	-0.5	0.0	0.0	0.0
Gross reserves[7/]	1,141	1,573	1,799	1,892	1,879	1,990	2,111	2,188	2,139	2,154
in months of imports excl. maquilas	2.9	4.9	4.7	4.0	3.5	3.6	3.6	3.6	3.3	3.2
Oil price (average, US$/bbl)	97.0	61.8	79.0	104.0	114.7	110.0	102.8	97.2	93.3	91.0

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 2012. 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/]Untied grants are recorded above the line.

[3/]The disbursements for 2012 includes a US$45 million budget support loan from the IDB for 2012. This loan is still subject to approval by the IDBs' Board of Directors.

[4/]A portion of ALBA-related flows is being used to finance off-budget transport subsidies and wage bonuses in 2010–12.

[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.

Table 7. Nicaragua: Medium-Term Macroeconomic Framework, 2008–16

	2008	2009	2010	2011	2012	2013	2014	2015	2016
				Est.			Proj.		
Real sector					(Percent)				
GDP growth	2.8	-1.5	4.5	4.7	3.7	4.0	4.0	4.0	4.0
				(Contribution to real GDP, percent)					
Total consumption	3.5	-0.9	3.1	3.5	2.8	2.6	3.0	3.0	3.0
Of which : Public consumption	1.0	-0.3	-0.1	0.9	0.6	0.2	0.5	0.6	0.6
Total investment	-0.5	-6.2	1.3	3.7	1.7	1.7	1.5	1.5	1.5
Of which : Public investment	-0.1	0.7	-0.3	0.3	0.1	0.2	0.2	0.2	0.3
Exports of goods and services	4.1	1.3	5.6	2.6	3.3	2.6	2.6	2.7	2.7
Imports of goods and services	-4.4	4.3	-5.5	-5.1	-4.1	-2.9	-3.1	-3.2	-3.2
GDP deflator	15.0	3.9	6.0	11.1	8.6	7.9	7.2	7.0	7.0
Consumer price inflation (eop)	13.8	0.9	9.2	8.0	8.6	7.5	7.0	7.0	7.0
Consumer price inflation (average)	19.8	3.7	5.5	8.1	9.2	7.9	7.2	7.0	6.9
Saving and Investment									
Gross domestic investment	32.9	24.6	25.8	31.5	34.3	35.3	36.0	36.6	37.3
Private	27.1	17.5	19.4	24.7	27.0	27.8	28.3	28.8	29.3
Public	5.7	7.1	6.4	6.8	7.3	7.5	7.7	7.8	8.0
National savings	8.2	11.2	11.1	13.5	12.9	16.3	18.8	20.0	21.6
Private	4.0	7.2	6.1	6.7	7.7	10.1	12.3	13.3	14.9
Public	4.2	4.0	5.0	6.9	5.2	6.2	6.5	6.8	6.7
External savings	24.6	13.4	14.7	18.0	21.4	19.0	17.2	16.6	15.6
Private	23.1	10.3	13.3	18.0	19.3	17.7	16.0	15.6	14.4
Public	1.5	3.1	1.4	-0.1	2.1	1.3	1.2	1.0	1.2
Balance of payments					(Percent of GDP)				
Current account	-24.6	-13.4	-14.7	-18.0	-21.4	-19.0	-17.2	-16.6	-15.6
Exports of goods, f.o.b	39.7	38.5	47.9	55.6	57.2	57.7	58.7	59.7	60.1
Imports of goods, f.o.b.	-74.2	-63.2	-72.7	-83.9	-87.7	-86.1	-85.0	-84.5	-83.7
Of which: oil	-15.1	-10.9	-11.4	-16.7	-17.0	-14.7	-13.3	-12.0	-10.5
Income	-3.8	-4.2	-4.3	-3.5	-3.6	-3.4	-3.6	-4.1	-3.8
Transfers to the private sector	17.9	18.0	17.8	16.3	15.8	15.6	15.6	15.1	14.6
Capital and financial account[1/]	24.1	19.7	17.7	18.8	21.1	20.2	18.5	17.4	15.1
Of which: FDI	9.8	7.0	7.7	13.3	10.6	9.6	9.1	8.9	8.4
Public finances									
Central government									
Revenues	19.0	18.9	19.6	21.1	21.5	21.6	21.7	21.8	21.9
Grants[2/]	2.9	2.4	2.5	2.7	2.4	1.9	1.9	1.9	1.9
Expenditures[2/]	23.2	24.1	23.0	23.2	24.4	23.9	23.9	24.0	24.0
Current expenditure	17.1	18.5	17.7	18.1	18.9	18.3	18.2	18.2	18.1
Of which : Wage and salaries	6.2	6.8	6.8	6.9	6.7	6.5	6.4	6.3	6.3
Interest	1.2	1.4	1.4	1.4	1.5	1.4	1.4	1.4	1.3
Transfers	5.8	6.7	6.0	6.0	6.5	6.5	6.5	6.5	6.5
Capital expenditure	6.0	5.5	5.4	5.1	5.4	5.6	5.7	5.8	5.9
Combined public sector (CPS)									
Overall balance, before grants	-4.6	-6.5	-4.0	-2.9	-4.7	-3.5	-3.4	-3.2	-3.2
Overall balance, after grants	-1.5	-3.1	-1.4	0.1	-2.1	-1.3	-1.2	-1.0	-1.2
Central government overall balance, after grants	-1.2	-2.8	-1.0	0.6	-0.5	-0.4	-0.3	-0.3	-0.2
Rest of NFPS overall balance	0.4	0.9	0.4	-0.1	-0.9	-0.5	-0.6	-0.4	-0.7
Central bank balance	-0.7	-1.2	-0.9	-0.4	-0.7	-0.4	-0.3	-0.3	-0.3
Financing	1.5	3.1	1.4	-0.1	2.1	1.3	1.2	1.0	1.2
External	1.9	3.9	3.3	2.6	2.9	3.3	3.2	3.0	2.5
Domestic (including CB operating balance)	-0.3	-0.8	-1.9	-2.7	-0.8	-1.8	-1.3	-0.9	-0.4
Public sector debt									
Total	74.8	80.1	78.0	73.1	68.7	65.8	64.1	62.0	59.3
Domestic	19.7	21.2	19.2	17.3	13.7	11.0	9.2	7.1	5.5
External[3/]	55.1	58.9	58.8	55.8	55.1	54.8	54.9	54.8	53.8
Memorandum items:									
GDP (US$ million)	6,372	6,214	6,591	7,297	7,828	8,363	8,876	9,403	9,966
Gross reserves (US$ m)[1/]	1,141	1,573	1,799	1,892	1,879	1,990	2,111	2,188	2,139
(in months of imports excl. maquilas)	*2.9*	*4.9*	*4.7*	*4.0*	*3.5*	*3.6*	*3.6*	*3.6*	*3.3*

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

[1/] Starting in 2009, figures include the SDR allocation for SDR105.1 million (US$165 million) of September 2009.

[2/] Figures for 2010–12 include off-budget wage bonus.

[3/] Actual and projection are based on the 2011 DSA Update. Estimates up to 2010 correspond to the legal situation.

Table 8. Nicaragua: Statement of Operations of the Central Government (GFSM 2001)–Preliminary, 2009–16
(Percent of GDP)

	2009	2010	2011	2012	2013	2014	2015	2016
			Est.			Proj.		
Revenue	**27.5**	**28.9**	**30.5**	**30.1**	**29.6**	**29.7**	**29.8**	**29.8**
Taxes	17.5	18.1	19.4	19.8	19.8	20.0	20.1	20.2
Taxes on income , profits, and capital gains	6.2	5.9	6.8	7.0	7.0	7.0	7.1	7.1
Taxes on property	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Taxes on goods and services	5.7	6.8	6.5	6.6	6.6	6.7	6.7	6.7
VAT	3.1	2.9	2.8	2.8	2.8	2.8	2.8	2.8
Excises	2.6	3.9	3.7	3.7	3.8	3.8	3.9	3.9
Other taxes	5.6	5.3	6.0	6.1	6.1	6.2	6.2	6.2
Social contributions	5.4	5.7	5.7	5.6	5.6	5.6	5.6	5.6
Grants	2.5	2.5	2.7	2.5	1.9	1.9	1.9	1.9
Current	0.3	0.8	0.8	0.5	0.0	0.0	0.0	0.0
Capital	2.2	1.7	1.9	2.0	1.9	1.9	1.9	1.9
Other revenue	2.1	2.5	2.6	2.3	2.3	2.2	2.1	2.1
Expenditure	**29.6**	**28.8**	**28.9**	**30.3**	**29.5**	**29.6**	**29.7**	**29.8**
Expense	**24.1**	**23.4**	**23.9**	**24.8**	**23.9**	**23.9**	**23.9**	**23.9**
Compensation of employees	6.8	6.8	6.9	6.7	6.5	6.4	6.3	6.3
Of which : Bonus	0.0	0.5	0.8	0.7	…	…	…	… .
Use of goods and services	3.7	3.5	3.9	4.3	3.9	3.9	3.9	3.9
Interest	1.4	1.4	1.4	1.5	1.4	1.4	1.4	1.3
Of which : External	0.4	0.4	0.4	0.5	0.5	0.5	0.5	0.5
Subsidies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	6.7	6.0	6.0	6.4	6.4	6.5	6.5	6.5
Social benefits	3.2	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Other expense	2.3	2.5	2.4	2.6	2.4	2.4	2.4	2.5
Net acquisition of nonfinancial assets	**5.5**	**5.4**	**5.1**	**5.4**	**5.6**	**5.7**	**5.8**	**5.9**
Acquisitions of nonfinancial assets	5.5	5.4	5.1	5.4	5.6	5.7	5.8	5.9
Domestically financed	0.7	1.2	1.2	1.4	1.4	1.5	1.6	1.7
Externally financed	4.8	4.2	3.8	4.0	4.2	4.2	4.2	4.2
Gross Operating Balance	**3.4**	**5.5**	**6.6**	**5.3**	**5.7**	**5.8**	**5.9**	**5.8**
Net lending (+)/borrowing (–) *(after grants)*	**-2.1**	**0.1**	**1.5**	**-0.1**	**0.1**	**0.1**	**0.1**	**-0.1**
Net lending (+)/borrowing (–) (before grants)	**-4.5**	**-2.4**	**-1.2**	**-2.6**	**-1.8**	**-1.8**	**-1.8**	**-2.0**
Primary net lending (+)/borrowing (-)	**-0.7**	**1.5**	**2.9**	**1.4**	**1.5**	**1.5**	**1.5**	**1.3**
Total financing : Financial assets - Liabilities	**-2.1**	**0.1**	**1.5**	**-0.1**	**0.1**	**0.1**	**0.1**	**-0.1**
Net acquisition of financial assets	**0.1**	**2.8**	**2.4**	**0.6**	**1.5**	**1.7**	**1.3**	**1.1**
Domestic	0.1	2.8	2.4	0.6	1.5	1.7	1.3	1.1
Currency and deposits	0.0	2.8	2.4	0.6	1.5	1.7	1.3	1.1
Central Bank	0.1	1.3	0.6	0.2	1.0	1.3	0.9	0.9
Commercial Banks	-0.1	1.5	1.8	0.4	0.5	0.4	0.4	0.2
Loans	37	…	…	…	…	…	…	…
Net incurrence of liabilities	**2.2**	**2.7**	**0.9**	**0.7**	**1.4**	**1.6**	**1.2**	**1.1**
Domestic	-1.0	0.3	-1.1	-1.1	-0.8	-0.4	-0.7	-0.7
Debt securities	0.1	-0.2	-0.3	-1.3	-0.1	0.2	-0.3	-0.2
Loans	-1.3	0.2	0.4	0.0	0.0	0.0	0.0	0.0
Central Bank	-0.6	-0.3	-0.4	0.0	0.0	0.0	0.0	0.0
Commercial Banks	-0.7	0.5	0.8	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.2	0.2	-1.2	0.2	-0.6	-0.5	-0.4	-0.4
Foreign	3.2	2.5	2.0	1.8	2.2	2.0	1.9	1.8
Loans	3.2	2.5	2.0	1.8	2.2	2.0	1.9	1.8
Disbursement	3.9	3.1	2.5	2.6	2.8	2.8	2.8	2.8
Amortization	-0.7	-0.7	-0.5	-0.8	-0.7	-0.8	-0.9	-0.9

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

Table 9. Nicaragua: Financial Soundness Indicators, 2008–11
(In percent, unless otherwise indicated)

	2008	2009		2010		2011	
		Jun	Dec	Jun	Dec	Jun	Dec
Capital adequacy							
Regulatory capital to risk-weighted assets	15.3	16.7	16.5	16.4	16.6	15.7	14.8
Regulatory Tier 1 capital to risk-weighted assets[1/]	9.0	10.0	10.9	11.8	11.1	10.0	9.2
Asset quality							
Nonperforming loans to total gross loans	3.0	3.0	3.3	3.5	3.0	2.9	2.2
Nonperforming loans to total gross loans[2/]	6.7	8.3	10.9	11.0	8.0	7.4	5.9
Nonperforming loans net of provisions to capital	17.2	25.3	33.4	30.7	20.3	14.8	12.6
Earnings and profitability							
Return on assets	1.8	1.4	0.5	0.0	1.0	1.7	1.6
Return on equity	18.1	13.3	4.8	-0.1	10.8	18.0	16.7
Interest margin to assets	9.1	8.7	8.7	7.8	7.0	5.9	6.2
Liquidity							
Liquid assets to total assets	21.2	24.5	29.5	31.5	28.7	31.1	27.2
Liquid assets to total short-term liabilities	118.0	137.7	139.4	121.0	120.8	143.6	129.9
Exposure to FX risk							
Net open position in foreign exchange to capital	94.7	90.8	81.4	86.6	99.4	106.4	92.6
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	102,429	105,316
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	62.6	64.4
Of which: Foreign banks[4/]	25.7	26.3	29.1	27.8	26.3	17.0	18.3
Bank deposits (percentage of GDP)							
Private commercial	39.6	41.3	45.2	50.8	52.8	48.5	50.1
Of which: Foreign banks[4/]	17.7	18.4	20.0	19.7	20.0	13.1	14.6
Dollarization and maturity structure							
Banking system assets as percentage of GDP	58.2	60.4	63.8	68.6	68.7	62.6	64.4
Assets in foreign currency							
as percentage of banking system assets	69.5	68.0	70.2	68.9	72.0	73.2	71.6

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.

[4/] Refers to banks with more than 49 percent foreign ownership.

Table 10. Nicaragua: Millenium Development Goals, 1990,1995, and, 2000-2010

	1990	1995	2000	2005	2010
Goal 1: Eradicate extreme poverty and hunger					
Employment to population ratio, 15+, total (%)	…	53.8	56.2	58.1	59.7
Employment to population ratio, ages 15-24, total (%)	…	46.4	46.2	46.8	45.9
Poverty gap at $1.25 a day(PPP) (%)	5.6$^{/1993}$	3.1$^{/1998}$	3.7$^{/2001}$	2.4	…
Malnutrition prevalence, weight for age (% of children under 5)	…	…	7.8$^{/2001}$	4.3	5.7$^{/2007}$
Prevalence of undernourishment (% of population)	…	…	25.0$^{/2001}$	…	19.0$^{/2008}$
Goal 2: Achieve universal primary education					
Primary completion rate, total (% of relevant age group)	39.2	49.0	66.2	74.6	80.9
School enrollment, primary (% net)	67.0	72.9	79.2	88.0	92.5
Goal 3: Promote gender equality and empower women					
Proportion of seats held by women in national parliaments (%)	15.0	11.0	10.0	20.7	20.7
Ratio of girls to boys in primary and secondary education (%)	119$^{/1989}$	…	105.2	101.9	101.6
Goal 4: Reduce child mortality					
Immunization, measles (% of children ages 12-23 months)	82.0	85.0	86.0	95.0	99.0
Mortality rate, infant (per 1,000 live births)	51.6	42.0	34.4	28.1	22.6
Mortality rate, under-5 (per 1,000)	68.0	53.6	42.7	34.1	26.9
Goal 5: Improve maternal health					
Births attended by skilled health staff (% of total)	…	61.0$^{/1993}$	66.9$^{/2001}$	73.7$^{/2007}$	…
Contraceptive prevalence (% of women ages 15-49)	…	48.7$^{/1993}$	68.6$^{/2001}$	72.4$^{/2007}$	…
Maternal mortality ratio (modeled estimate, per 100,000 live births)	170	150	130	110	95
Goal 6: Combat HIV/AIDS, malaria, and other diseases					
Incidence of tuberculosis (per 100,000 people)	108	85	68	53	42
Prevalence of HIV, total (% of population ages 15-49)	0.1	0.1	0.1	0.2	0.2$^{/2009}$
Tuberculosis case detection rate (%, all forms)	66	72	70	66	100
Goal 7: Ensure environment sustainability					
CO2 emissions (metric tons per capita)	0.60	0.60	0.70	0.70	0.76$^{/2008}$
Forest area (% of land area)	37.5	…	31.7	28.8	25.9
Improved sanitation facilities (% of population with access)	43.0	44.0	48.0	50.0	52.0
Improved water source (% of population with access)	74.0	77.0	80.0	83.0	85.0
Terrestrial protected areas (% of total land area)	15.4	29.2	36.7	36.7	36.7
Goal 8: Develop a global partnership for development					
Internet users (per 100 people)	0	0	1.0	2.6	10.0
Mobile cellular subscriptions (per 100 people)	0	0	1.8	20.6	65.1

Source: Millennium Development Goals, World Bank.
Note: A superscript indicates the nearest available data point for the respective column (year).

INTERNATIONAL MONETARY FUND

NICARAGUA

June 12, 2012

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Western Hemisphere Department

CONTENTS

ANNEX I. FUND RELATIONS

(As of May 31, 2012)

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

II. General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	130.00	100.00
Fund holdings of currency (Exchange Rate)	130.01	100.01
Reserve Tranche Position	0.00	0.00

III. SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	124.54	100.00
Holdings	111.69	89.68

IV. Outstanding Purchases and Loans:	**SDR Million**	**Percent Quota**
ECF Arrangements	115.60	88.92

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF [1/]	Oct 05, 2007	Oct 31, 2011	78.00	78.00
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 [1/]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2012	2013	2014	2015	2016
Principal	5.57	10.74	14.42	19.18	20.90
Charges/Interest	0.01	0.02	0.25	0.21	0.16
Total	5.58	10.75	14.66	19.38	21.06

[1/] 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:

	Enhanced Framework
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.

Definitions:

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 floating completion point triggers including predefined key policy reforms.

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)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
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.

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 June 11, 2012, the exchange rate in the official market was C$23.4814 per U.S. dollar. Nicaragua has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions.

XI. Article IV Consultation:

The previous consultation was completed by the Executive Board on July 9, 2010 (PIN No. 10/83). The last Fund-supported program review (Seventh Review under the ECF Arrangement and Financing Assurances Review) was concluded on October 21, 2011.

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 2010.

Dept.	Purpose	Time of Delivery
FAD	Revenue Administration	March 2012
FAD	Customs	January 2012
FAD	Public Financial Management	January 2012
FAD	Revenue Administration	October 2011
FAD	Tax Policy	August 2011
FAD	Public Financial Management	April 2011
FAD	Public Financial Management	September 2010
FAD	Customs	May 2010
FAD	Public Financial Management	April 2010
FAD	Customs	February 2010
FAD	Revenue Administration	February 2010
FAD	Revenue Administration	January 2010
MCM	Stress Testing	May 2012
MCM	Cash Management	April 2012
MCM	Monetary and Foreign Exchange Policy	March 2012
MCM	Bank Supervision and Regulations	March 2012
MCM	Monetary and Foreign Exchange Policy	December 2011
MCM	Bank Supervision and Regulations	November 2011
MCM	Monetary and Foreign Exchange Policy	October 2011
MCM	Payment Systems Modernization and Oversight	September 2011
MCM	Risk-based Supervision	July 2011
MCM	Review Process of Conducting Open Market Operations	June 2011
MCM	Bank Supervision and Regulations	April 2011
MCM	Risk Management Workshop	March 2011
MCM	Training on Stress Testing	February 2011
MCM	Monetary and Foreign Exchange Policy	February 2011
MCM	Monetary and Foreign Exchange Policy - Seminar on Inflation Targeting	November 2010
MCM	Financial Sector Supervision	October 2010

MCM	STE: Bank Supervision and Regulations	October 2010
MCM	Monetary Policy - Liquidity Forecasting	August 2010
MCM	Risk-based Supervision	June 2010
MCM	Financial Sector Supervision	March 2010
STA	Monetary and Financial Statistics	January 2012
STA	Balance of payments statistics	November 2011
STA	Annual and Quarterly National Accounts Statistics	August 2011
STA	Monetary and Financial Statistics	June 2011
STA	Balance of payments statistics	June 2011
STA	Balance of payments statistical techniques	June 2011
STA	Export and Import Price Indexes	May 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

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

ANNEX II. BANK-FUND COUNTRY LEVEL JOINT MANAGERIAL ACTION PLAN, 2012–13[1]

Products	Mission timing	Expected delivery
A. Mutual information on relevant work programs		
The Fund work program		
Strategy: An ECF arrangement for 2007-2011 concluded successfully on October 21, 2011. The IMF-supported program entailed macroeconomic policies anchored on containing expenditures, paving the way for fiscal consolidation, and protecting the external position. Technical assistance will focus on tax administration, improving payment systems and financial regulation and oversight. As of now, an IMF staff visit is planned for the second half of 2012 and an Article IV mission is scheduled to take place in the spring of 2013.		
Article IV	May 2012	Board discussion in June 2012
Ex Post Assessment of Longer-Term Program Engagement	May 2012	Board discussion in June 2012
FADTA: Revenue Administration	July 2012	TA report at the end of the final mission
FADTA: Public Financial Management	July 2012	TA report at the end of the final mission
MCMTA: Stress Testing	July 2012	TA report at the end of the final mission
MCM TA: Payment System Organization	June 2012	TA report at the end of the final mission
MCM TA: Risk-based Supervision	July 2012	TA report at the end of the final mission
MCM TA: Monetary and Foreign Exchange Policy	August 2012	TA report at the end of the final mission
MCM TA: Introducing IFRS	October 2012	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		

[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.

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. The Bank is currently preparing a new assistance strategy in partnership with the Nicaraguan government.		
A. Lending		
A.1 Second Land Administration Project in Support on Nicaragua's Land Program	TBD	Bank approval by February 2013
A.2 Nicaragua Rural Telecom Additional Finance	TBD	Bank approval by June 2012
B. Technical assistance and Analytical Work.		
B.1. Innovations for Rural Women's Economic Empowerment	June 18-22, 2012	Final delivery by June 2012
B.2. Country Economic Memorandum	June 25-26, 2012	Delivery to client by September 2012
B.3. Nicaragua Agriculture Public Expenditure Review	June 18-22, 2012	Final delivery by August 2012
B.4. Nicaragua: Consumer Protection # 10136	August, 2012	Delivery to client by November 2012
B.5. Adaptation of Nicaragua's Water Supplies to Climate Change	TBD	Board Approval by October 2012

ANNEX III. RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

(As of April 30, 2012)

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)	*10.6*
2010	National Sustainable Electrification and Renewable Energy Program I	30.5
	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
	San Jacinto-Tizate Geothermal Power Project (Non-sovereign)	*40.0*
2011[1]	Improving Family and Community Health in Highly Vulnerable Municipalities	20.0
	National Sustainable Electrification and Renewable Energy Program II	22.0
	Integral Housing Improvement Program	20.0
	Improving Social Protection and Health expenditures and Public Management	45.0

2012	Program to accompany the implementation of the National Policy for children in Prioritized Communities	20.0
	Sustainable Agricultural Productivity Program *	40.0
	Integrated Health Networks *	36.2
	Support to the Transportation Sector II *	59.2
	National Sustainable Electrification and Renewable Energy Program III *	35.0
	Improving Expenditures on Health and Social Protection II *	45.0
	Rent to Own: Innovation to Improve Access to Social Housing (Non-sovereign)	*10.0*

[1] Carry-over of US$64.2 million for 2012.
* Pending for Approval.

IDB Loan Commitments and Disbursements

As of April 30 2012, there were 31 projects in the IDB's current sovereign loan portfolio with a total commitment of US$699.6 million, and an undisbursed balance of US$328.65 million. Basic infrastructure (roads and energy) accounts for almost 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 April 30 2012, there were 27 non-reimbursable technical cooperations (for the public sector) in execution with an approved commitment of US$13.0 million and an available balance of US$8.5 million. The Multilateral Investment Fund has: (i) 17 non-reimbursable technical cooperations (including regional operations) in execution with an available balance of US$7.5 millions; and (ii) 7 loans in execution from the Social Entrepreneurship Program with an approved commitment of US$2.3 million and an available balance of US$1.1 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 in late 2012.

ANNEX IV. STATISTICAL ISSUES

(As of April 30, 2012)

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 1993 (SNA93)*. GDP estimates with 1994 as the base year are available up to the fourth quarter of 2011. 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 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*. The Regional national accounts Statistics Advisor visited Managua during January 24–28, 2011 to prepare a work plan on TA and training needs on national accounts statistics as well as to provide TA in quarterly national accounts (QNA). The first TA mission on QNA was conducted during August 29-September 2, 2011. The second TA mission dealt with the quarterly flow of funds table and was conducted during October 2–14, 2011. The third mission dealt with the quarterly flow of funds table and the quarterly financial accounts by institutional sector and was conducted during November 28–December 9, 2011. 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 during the third quarter. **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. An STA mission conducted in April-May 2011 recommended the creation of a department in charge of public fiscal statistics (Dirección de Estadísticas de Finanzas Publicas) and requested the reporting of quarterly data for the IFS for the Central Government. In the medium term is expected also the quarterly reporting of the consolidated public sector accounts. 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*. 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. In January 2012, STA provided technical assistance under the second phase of the Regional Project on Harmonization of Monetary and Financial Statistics. The mission developed a work plan to compile surveys for the other financial corporations following the recommendations of the *Monetary and Financial Statistics Manual and Monetary* and *Financial Statistics Compilation Guide*. The mission encouraged the authorities of the central bank to start the compilation of monthly data for insurance companies and recommended the compilation of the monetary and financial statistics for credit and savings cooperatives. The mission prepared an action plan aimed at improving the collection, compilation, and dissemination of monetary data. In December 2011 and May 2012, MCM provided technical assistance to implement stress testing on the banking system. The mission team explained to Central Bank and Superintendency of Banks and Other Financial Institutions (SIBOIF) the process with particular emphasis on hands-

on training.

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.

STA provided technical assistance for improving the balance of payments and the international investment position in April 2009 and April 2010. A one-week CAPTAC TA mission on international investment position statistics also visited Managua in March 2010.

In October 2010 and November 2011 CAPTAC provided technical assistance for improving the compilation of services statistics in the goods and services account of the balance of payments. The External Sector Area (ESA) of the Central Bank of Nicaragua has been using a mix of administrative records and quarterly/annual business surveys to compile services statistics. The ESA faced difficulties while implementing some recommendations regarding services statistics made by previous TA missions. In particular, the ESA was unable to access disaggregated data on insurance services from the Superintendency of Banks and Other Financial Institutions (SIBOIF). Coverage and compilation issues regarding services statistics within the framework of the adoption of the sixth edition of the *Balance of Payments and International Investment Position Manual* (*BPM6*) guidelines were addressed. The mission reviewed several questionnaires, particularly those related to foreign direct investment and free trade zones. The authorities have made progress in the implementation of the recommendations regarding services statistics of previous TA. Nonetheless, they need to coordinate with the SIBOIF the implementation of insurance's accounts catalog, and improve the access of the Central Bank to SIBOIF's database.

In December 2011, CAPTAC provided assistance on Export, Import and Producer Price Statistics. As part of the national accounts project, the Central Bank of Nicaragua has been developing a system of Integrated Indices of Prices, Value, and Volume for Imports and Exports. Preliminary unit value indices have been developed, nonetheless, some of these unit value indices have been determined to have strange behavior.

Data dissemination: Nicaragua has participated in the General Data Dissemination System (GDDS) since February 2005. Data ROSC was published in December 2005.
In April 2012, a STA mission assessed Nicaragua's data compilation and dissemination practices

against the Special Data Dissemination Standard (SDDS) requirements for coverage, periodicity, and timeliness, and provided the authorities with recommendations to meet all SDDS requirements. Nicaragua meets the SDDS requirements for coverage for all compiled and disseminated SDDS data categories except for general government operations; balance of payments; and the international investment position. After the implementation of recommendations, Nicaragua could subscribe to the SDDS by end-2013.

Nicaragua: Table of Common Indicators Required for Surveillance

(AS OF MAY 29, 2012)

	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	5/29/2012	5/29/2012	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	5/29/2012	5/29/2012	D	D	D		
Reserve/Base Money	5/29/2012	5/29/2012	D	D	D		
Broad Money	5/29/2012	5/29/2012	D	D	D	O, LO, LO, LO	LO, O, LO, LO, LO
Central Bank Balance Sheet	4/30/2012	5/29/2012	M	M	M		
Consolidated Balance Sheet of the Banking System	March 2012	5/29/2012	M	M	M		
Interest Rates[2]	5/24/2012	5/29/2012	W	W	W		
Consumer Price Index	April 2012	5/29/2012	M	M	M	O, LO, LO, LO	LO, LO, LO, O, LO
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	March 2012	5/10/2012	M	M	M	LO, LNO, LNO, LO	O, O, O, O, LO
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	March 2012	5/10/2012	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Q4 2011	5/10/2012	Q	Q	Q		
External Current Account Balance	Q4 2011	5/10/2012	Q	Q	Q	LO, LO, LNO, LO	LO, O, LO, LO, LO

Nicaragua: Table of Common Indicators Required for Surveillance (continued)

(AS OF MAY 29, 2012)

Exports and Imports of Goods and Services	March 2012	5/10/2012	M	M	M		
GDP/GNP	Q4 2011	April 2012	Q	Q	Q	O, O, O, LO	LO, O, LO, O, LNO
Gross External Debt	Dec. 2011	5/10/2012	M	M	M		
International Investment Position[6]	2011	5/10/2012	A	A	A		

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

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

[3] Foreign, domestic bank, and domestic nonbank financing.

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

[5] Including currency and maturity composition.

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

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

[8] Reflects 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).

[9] Same 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.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 12/75
FOR IMMEDIATE RELEASE
July 12, 2012

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2012 Article IV Consultation with Nicaragua

On June 27, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] and discussed the Ex Post Assessment of Longer-Term Program Engagement (EPA)[2] with Nicaragua.

Background

Macroeconomic developments in Nicaragua have been broadly positive since 2010. Real gross domestic product (GDP) grew on average 4.6 percent during 2010-11, underpinned by robust consumption and investment. Inflationary pressures abated somewhat to 8 percent by end-2011 (from 9.2 percent at end-2010), as world commodity prices eased. Although the external current account deficit widened in 2011 (to 18 percent of GDP), larger capital inflows (mainly sizable foreign direct investment) produced a small surplus in the balance of payments, thus increasing international reserves.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

[2] An EPA is required for all members having longer-term program engagement with the Fund. EPAs are intended to provide an opportunity to step back from continuing program relations to consider an analysis of the economic problems facing the country, review progress under Fund-supported programs, and draw forward-looking lessons for future Fund engagement.

The fiscal outturn of 2011 surpassed expectations. The tax reform of 2009 and the strong output recovery boosted tax revenues, while central government spending as a share of GDP remained broadly stable. As a result, the central government recorded a surplus of 0.6 percent of GDP (following a deficit of 1 percent of GDP in 2010), which was primarily used to pay down debts of the state-owned electricity generation company. Elsewhere in the public sector, a deterioration in the fiscal result of the social security system, the municipality of Managua, and the state-owned enterprises was partly offset by a smaller operating deficit of the central bank than in 2010. On net, the consolidated public sector recorded a small surplus for the first time since 2007.

Monetary policy continued to bolster the international reserves position and conditions in the financial system strengthened. The central bank maintained the crawling-peg system, which helped anchor inflation expectations. Banks' liquidity remained ample while credit growth picked up significantly towards the end of the year. Nonperforming loans ratios declined as banks' profitability improved and deposits (in local and foreign currency) rose.

Looking ahead, real GDP growth is expected to slow in 2012 and inflation to rise to between 8 and 9 percent owing to oil price increases. The consolidated public sector is projected to post a deficit in 2012 as some spending pressures resurface, but its fiscal position is expected to improve gradually in the medium term with expenditure restraint at the level of the central government, central bank, and state-owned enterprises. The external current account balance is expected to widen in 2012 on the back of weaker external demand and a larger oil bill, which would reduce moderately the international reserves coverage. Risks to the economic outlook for 2012 are tilted to the downside given Nicaragua's exposure to economic activity abroad.

The Ex Post Assessment (EPA) reviewed Nicaragua's performance under the 2007–11 program supported by an Extended Credit Facility (ECF) arrangement. The EPA concluded that although the Nicaraguan economy was buffeted by a series of adverse shocks between 2007 and 2011, the ECF-supported program was effective in helping the authorities develop an appropriate policy framework to support macroeconomic stability. The program also paved the way for some reforms of the tax system and the energy sector, but it fell short in key areas, such as pensions and public financial management.

Executive Board Assessment

Executive Directors welcomed Nicaragua's robust economic recovery and favorable macroeconomic performance on the back of sound policies, high export prices, and large investment inflows. Nevertheless, Directors underscored that important macroeconomic and structural challenges remain to be addressed, including widespread poverty and large external imbalances. With downside risks prevailing due to the uncertain global environment, Directors encouraged the authorities to maintain prudent macroeconomic policies and step up the pace of structural reform.

Directors stressed that fiscal consolidation should be the cornerstone of macroeconomic stability. With wage bonuses and higher electricity subsidies worsening the fiscal outlook for 2012, Directors urged firm expenditure restraint. In the medium term, reforms to strengthen further the revenue effort and to revamp the pension system will be critical, alongside current expenditure restraint, in accommodating higher social and infrastructure spending while maintaining fiscal sustainability. Particularly important will be to widen the tax base by curtailing exemptions.

Directors underscored that reducing external vulnerabilities related to the large external current account deficit will be a key challenge in the period ahead. They supported plans to cut back on oil imports and increase international reserves. They also stressed the importance of reducing the size and improving the composition of the public debt, and encouraged the authorities to step up efforts to obtain debt relief on HIPC terms from non-Paris Club creditors.

Directors urged the authorities to prioritize and address the key structural impediments to growth and poverty reduction. They highlighted the need to strengthen governance and institutions, improve public financial management, reduce labor market informality, and tackle weaknesses in the energy sector.

Directors welcomed the progress in improving banking supervision, reflected in the overall soundness of the financial system. They encouraged concerted action to deal with remaining vulnerabilities, including increased collaboration with regional supervisors. Directors welcomed the creation of a financial intelligence unit, and urged the authorities to seize the opportunity to bring the regime against money laundering and terrorism financing into compliance with international standards.

Directors welcomed the conclusion of the Ex Post Assessment that the Fund’s engagement in Nicaragua during 2007–11 contributed to macroeconomic stability. They noted, however, that exogenous shocks and at times weak program ownership led to uneven progress in structural reforms. In light of this, Directors highlighted several lessons for the future. In particular, Directors stressed that policies should have strong ownership by the authorities, structural reforms should be well designed and well targeted, and implementation should be flexible to accommodate unexpected shocks and capacity constraints.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Nicaragua: Selected Social and Economic Indicators, 2008–13

	2008	2009	2010	2011	2012	2013
				Est.	Proj.	
Real sector			(Percent)			
GDP growth	2.8	-1.5	4.5	4.7	3.7	4.0
GDP deflator	15.0	3.9	6.0	11.1	8.6	7.9
Consumer price inflation						
End of period	13.8	0.9	9.2	8.0	8.6	7.5
Period average	19.8	3.7	5.5	8.1	9.2	7.9
	(Percent of GDP; unless otherwise indicated)					
External sector						
Current account	-24.6	-13.4	-14.7	-18.0	-21.4	-19.0
Exports of goods, f.o.b	39.7	38.5	47.9	55.6	57.2	57.7
Imports of goods, f.o.b.	-74.2	-63.2	-72.7	-83.9	-87.7	-86.1
Of which: oil	-15.1	-10.9	-11.4	-16.7	-17.0	-14.7
Capital and financial account [1/]	24.1	19.7	17.7	18.8	21.1	20.2
Of which: FDI	9.8	7.0	7.7	13.3	10.6	9.6
Gross reserves (US$ m)[1/]	1,141	1,573	1,799	1,892	1,879	1,990
(in months of imports excl. maquilas)	2.9	4.9	4.7	4.0	3.5	3.6
Fiscal sector						
Central government overall balance, after grants	-1.2	-2.8	-1.0	0.6	-0.5	-0.4
Revenues	19.0	18.9	19.6	21.1	21.5	21.6
Expenditures[2/]	23.2	24.1	23.0	23.2	24.4	23.9
Grants[2/]	2.9	2.4	2.5	2.7	2.4	1.9
Combined public sector (CPS) balance, before grants	-4.6	-6.5	-4.0	-2.9	-4.7	-3.5
CPS overall balance, after grants	-1.5	-3.1	-1.4	0.1	-2.1	-1.3
Financing	1.5	3.1	1.4	-0.1	2.1	1.3
External	1.9	3.9	3.3	2.6	2.9	3.3
Domestic (including BCN operating balance)	-0.3	-0.8	-1.9	-2.7	-0.8	-1.8
Public sector debt						
Total	74.8	80.1	78.0	73.1	68.7	65.8
Domestic	19.7	21.2	19.2	17.3	13.7	11.0
External[3/]	55.1	58.9	58.8	55.8	55.1	54.8

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

[1/]Figures include the SDR105.1 million (US$165 million) allocation of September 2009.

[2/]Figures for 2010-13 include off-budget wage bonus.

[3/]Actual and projection are based on the 2011 DSA Update. Estimates up to 2010 correspond to the legal situation.

Statement by Mr. Pérez-Verdía, Executive Director for Nicaragua, and Mr. Cosenza Jimenez, Advisor to Executive Director June 27, 2012

We would like to thank staff for their illustrative and balanced reports and for their constructive dialogue with our authorities. Our authorities concur with the main messages of the reports and we simply wish to emphasize the following points:

1. Recent Economic Developments

As the reports indicate Nicaragua's macroeconomic situation is sound and stable with the central government and the consolidated public sector posting a 0.6 percent and 0.1 percent surplus, respectively, in 2011. Current expenditure was reduced, tax revenues increased in 2011 and reserves are at a comfortable level. Public external debt remains stable at about 55 percent of GDP. Economic growth is expected to remain in the 4.0-4.7 percent range, while inflation will be in the 7-9 percent range. Bank capitalization and liquidity are ample and nonperforming loans have decreased to 2.2 percent.

The authorities plan to issue their new medium term economic and financial program in the next couple of months. The program will continue to gear policy towards the attainment of social objectives, in a context of strengthened macroeconomic stability. In the near term the government will continue to promote fiscal consolidation in a context of increased public investment to support growth.

The authorities continue to place great importance on equitable growth and on pro-poor spending. As a result, poverty continues to decrease. It is estimated that the percentage of the population living under the international poverty line, that is those earning less than $2 per day, decreased from 48.3 percent in 2005 to 42.5 percent in 2009.

2. Outlook and Policies

- **The Formal and Informal Sectors**

In spite of the significant accomplishments mentioned in the previous paragraphs, Nicaragua is still beset by widespread poverty and low income per capita. Poverty has indeed fallen, but not enough or sufficiently fast. Indeed, deeper poverty reduction demands faster economic growth; which in turn requires higher economic productivity.

The authorities agree with staff that one of the main obstacles to higher productivity is the size of the informal sector. The temporary and ephemeral nature of informal employment discourages investing in worker training and in the technology and tools necessary to raise productivity. The authorities are fully cognizant of the need to reduce the size of the informal sector. Consequently, they seek to decrease or eliminate the perceived disadvantages of formalization, while simultaneously explaining its inherent advantages. This requires, *inter alia*, the simplified access to micro finance services and the elimination of red tape and onerous charges and taxes levied on micro and small enterprises. It also demands better monitoring efforts to ensure that companies do not operate clandestinely in the informal sector simply to avoid paying a fair wage and providing social benefits to their employees while simultaneously evading taxes and social security contributions. To this end, simplified electronic processes are being implemented to reduce red tape and taxes are being kept low for micro and small enterprises. In addition, a single identification number will be issued to all companies by the national and local governments and by the Social Security Institute, thus ensuring that registration with any one of them will lead to registration with the other two, thereby rendering evasion more difficult.

The government's strategy to reduce the informal sector also comprises investing wisely in health, education and in infrastructure, particularly in the electricity sector. The authorities are committed to improve the composition and effectiveness of public spending prioritizing infrastructure investment. This commitment already bore fruit in 2011.

Informality notwithstanding, Nicaragua has recorded important gains in competitiveness. Nevertheless, the authorities are aware of the need to continue to improve the business climate and the staff reports recognize steady improvements in external competitiveness, in a framework of an export strategy based on product diversification, the consolidation of traditional and new markets and the negotiation of free trade agreements. Furthermore, important efforts are being made to achieve a broad consensus on key economic decisions, through a tripartite approach involving the private sector, workers and the government. As a consequence of these efforts direct foreign investment reached a record in 2011 when $967 million flowed into the economy, nearly doubling the 2010 figures. The investment-promotion agency, Pro Nicaragua, actively seeks foreign investment and its efforts are partially responsible for the recent surge in investment flows. The relative calm and social cohesion that prevail in the country bode well for continued foreign direct investment flows henceforth.

- **The Electricity Sector**

The authorities wish to acknowledge that the document *Lifting a Constraint on Growth: Achievements and Challenges of Nicaragua's Electricity Sector*, included in the Selected Issues annex, has made a valuable, and welcome, contribution to the understanding of the sector issues. As that document indicates, Nicaragua, as a non oil-producing country, has suffered from the steep fuel price increases registered in the last decade. Electricity production is predominantly (70 percent) fuel-based. Nicaragua, however, is endowed with ample natural resources that can be harnessed to meet its electricity needs and the authorities are committed to dramatically altering the *status quo* by 2017. By then it is expected6 that 75 percent of the electricity will be generated with natural, renewable resources, mainly hydroelectric, geothermal, eolic and biomass, where additional 270MW, 100 MW, 120 MW and 20 MW, respectively, are expected to come on-line by 2016. Several private companies, local and foreign, are already building the generating stations that will sell their renewable energy to the private distribution companies that already operate in the country, with the state assuming a subsidiary role.

This transformation of the electricity sector underpins the authorities' strategy to address the financial difficulties that beset it. The tariffs currently charged to consumers would appear adequate for the cost of producing, transmitting and distributing electricity once the new renewable energy generating stations are commissioned. The issue therefore is how to best bridge the financial gap that the sector will experience between now and 2017. The authorities fully understand that a financially healthy sector, with adequate generation capacity and tariffs, low electricity losses and targeted subsidies, is a fundamental precondition for accelerated growth. Based on this understanding, they currently work in the definition of the strategy to follow in the 2012-2017 transition period, as they expect that the situation will be vastly ameliorated once the new, renewable energy stations come into operation by 2017.

- **Social Security Reform**

The authorities appreciate the advice and technical assistance that the Fund has provided on this issue. They fully recognize the importance of the issue and the need to proceed cautiously so as not to erect an additional barrier to formalization. The authorities intend to undertake a public consultation process with regard to the social security reform and, once that process is concluded, to submit a proposal to the National Assembly to modify the current system.

3. Fiscal Policy

The authorities remain firmly committed to further consolidate public finances by continuing to control expenditures and enhance revenue collection. As stated in the Article IV Staff Report, expenditures were contained in 2011 and revenue collection improved. Nicaragua's tax burden is 19.4 percent, which is reasonable for a low income country. Nevertheless, the authorities have decided to complete the tax reform process begun in 2009 in order to render the system more progressive and equitable, while simultaneously making it simpler to operate and monitor. Although revenue enhancement is not the goal of the reform, it is likely that a streamlined system which reduces tax incentives and exemptions and incorporates the proper use of transfer prices will result in higher revenues. The authorities have recently begun a consultation process with all stakeholders, including the private sector. It is expected that the result of this participative and transparent process will culminate in September so that the anticipated results of the reform may be reflected in the budget to be submitted to the National Assembly in mid October. It is estimated that the National Assembly will subsequently enact this new tax legislation and that the new system will be implemented in 2013.

Finally, the authorities are committed to improve the quality of expenditure thereby creating the space for additional investment in infrastructure, in human capital and in the social safety nets. The authorities' resolve is evinced in the current expenditure reduction posted in 2011.

4. Monetary and Exchange Rate Policies

The Staff Report for the Article IV Consultation states that the exchange rate is "broadly in line with fundamentals". The authorities will continue to implement an announced annual devaluation with respect to the US dollar, as this has served the country well hitherto. As indicated in the Staff Report, reserves remain at a comfortable level, amounting to the equivalent of 2.6 times the monetary base. Although the current account deficit (18 percent of GDP) might appear high, it reflects Nicaragua's high dependence on oil imports and significant investment needs. This deficit has been partially offset by the recovery of important flows, in particular, remittances (mainly from the USA and Costa Rica) which are now stable and estimated to be about 12.5 percent of GDP, while income from tourism represents 5 percent of GDP. The remaining current account deficit is fully financed with FDI, grants and concessional loans.

5. Financial Sector Policy

In the financial sector the authorities will continue to upgrade regulation and supervision, as well as expand the supervisory perimeter to include microcredit organizations and credit cooperatives. In general, the sector is healthy and no major issues afflict it. Furthermore, the micro credit subsector is on firmer ground after new legislation was enacted to promote and regulate it.

6. Debt Management Policy

About one quarter of the outstanding public external debt is with non-Paris Club members. Although the negotiation process has been excruciatingly slow, the authorities remain steadfast in bringing it to fruition. Furthermore, the authorities' commitment to further fiscal consolidation ensures a reduction of the public debt henceforth. Finally, the authorities will continue to prioritize external financing through grants and concessional loans, while developing the domestic debt market. In order to further advance in pending debt relief, Nicaragua will, once again, request full participation of all creditors in the debt reduction initiatives.

7. Aid and Transparency

As mentioned in the reports, Nicaragua receives substantial financial support from several sources, including Venezuela. In the latter case, assistance is provided through a private sector entity, without sovereign guarantee and its use, along with that of other important external financing, is transparently presented in a biannual report on official external aid. The staff reports also delve into the deleterious consequences of a sudden stop of the Venezuelan support. However, the question of sustainability of the support provided by Venezuela is no different from that of other important partners, and the historically strong ties between Nicaragua and Venezuela render the probability of such an event extremely low. Nevertheless, if the risk of reduction of external aid was to materialize, the necessary adjustment would be implemented to limit a significant adverse impact on the fiscal position.

8. Conclusion

As the Ex Post Assessment indicates, the ECF program recently completed by Nicaragua was quite successful. Although the international environment worsened significantly after the program was initiated, the Fund and the authorities responded flexibly and adapted the program to the new reality. Given these circumstances, it is not surprising that the completion of some of the reviews was delayed. However, the authorities persevered and the program was successfully completed. This clearly attests the ownership of the program by the authorities. In fact, the successful performance in the last two programs evinces Nicaragua's strong ownership of the programs supported by the Fund.

We close by reiterating our appreciation for the thorough and detailed work that underlies the reports prepared by the IMF mission teams. Our authorities appreciate the high quality dialogue that resulted from their visits to Nicaragua and will give due consideration to their recommendations and observations.