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Nicaragua: Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, Request for Waivers of Performance Criteria, and Financing Assurances Review—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Nicaragua

In the context of the fourth review under the three-year arrangement under the Poverty Reduction and Growth Facility, request for waivers of performance criteria, and financing assurances review, the following documents have been released and are included in this package:

- the staff report for the fourth review under the three-year arrangement under the Poverty Reduction and Growth Facility, request for waivers of performance criteria, and Financing assurances review, prepared by a staff team of the IMF, following discussions that ended on **November 17, 2003,** 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 December 29, 2003**. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a staff statement of **January 23, 2004** updating information on recent developments.

- a Press Release summarizing the **views of the Executive Board as expressed during its January 23, 2004 discussion** of the staff report that completed the request and review.

- a statement by the Executive Director for Nicaragua.

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

Letter of Intent sent to the IMF by the authorities of Nicaragua*
Supplementary Memorandum of Economic and Financial Policies by the authorities of Nicaragua*
Technical Memorandum of Understanding by the authorities of Nicaragua*
HIPC Document
*May also be included in Staff Report

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

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NICARAGUA

Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, Request for Waivers of Performance Criteria, and Financing Assurances Review

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

Approved by Markus Rodlauer and G. Russell Kincaid

December 29, 2003

PRGF arrangement. A three-year PRGF arrangement for SDR 97.5 million (75 percent of quota) was approved on December 13, 2002. The first and second reviews were completed on June 18, 2003, and the third review on October 20, 2003. Because of the high program risks, quarterly reviews will continue through 2004.

Recent developments. Since the completion of the last review, economic developments have been broadly in line with the program. All performance criteria and benchmarks associated with this review were met, with the exception of one quantitative and one structural performance criterion. As explained in the paper, the staff supports the authorities' request for waivers.

Main review issues. The policy discussions focused on the macroeconomic framework for 2004; pending actions to meet the completion triggers for the enhanced HIPC Initiative; medium-term fiscal and debt sustainability; and structural reforms, focused on the fiscal and banking sectors.

Mission. The mission visited Managua during November 4–17 and met with Finance Minister Montealegre, Planning Minister De Franco, Central Bank President Alonso, other senior government officials and representatives of the assembly, civil society, and the private sector. The team comprised Philip Young (head), Sergio Martín, Oscar Melhado, Monica Perez dos Santos (all WHD), James Walsh (PDR), Luis Breuer (resident representative), and Rina Marcoux (assistant WHD). The mission collaborated closely with the World Bank and IDB, whose staff participated in some of the meetings.

Contents Page

Appendices

Attachments

Abbreviations and Acronyms

BCN	Central Bank of Nicaragua
BCP	Basel Core Principles
BPI	Indemnity Bonds
BRB	Bank Resolution Bond
CAFTA	Central American Free Trade Area
CPS	Combined Public Sector
DGA	General Directorate of Customs
DGI	General Directorate of Internal Revenue
DSA	Debt Sustainability Analysis
ENACAL	Nicaraguan Water and Sewerage Company
ENEL	Nicaraguan Electricity Company
ENITEL	Nicaraguan Telecommunications Company
FAD	Fiscal Affairs Department
FISE	Emergency Social Investment Fund
FOGADE	Deposit Guarantee Fund
FSAP	Financial Sector Assessment Program
FSS	Social Supplementary Fund
FX	Foreign Exchange
GDDS	General Data Dissemination System
HIPC	Heavily Indebted Poor Countries
IDB	Inter-American Development Bank
INIFOM	Nicaraguan Institute of Municipal Development
LOI	Letter of Intent
MFD	Monetary and Financial Affairs Department
NDP	National Development Plan
NIR	Net International Reserves
NPL	Nonperforming Loans
NPV	Net Present Value
PC	Performance Criterion
PLC	*Partido Liberal Constitucional*
PRGF	Poverty Reduction and Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSIA	Poverty and Social Impact Analysis
SB	Superintendency of Banks
SECEP	Secretariat of Coordination and Strategy of the Presidency
SIGFA	Integrated System for Financial Management and Auditing
SMEFP	Supplementary Memorandum of Economic and Financial Policies
TA	Technical Assistance
TMU	Technical Memorandum of Understanding
VAT	Value-added Tax
WB	World Bank

Executive Summary

Background

- **Despite the difficult political situation, the authorities have persevered with their program.** Political alliances have shifted repeatedly in recent months, with attendant risks to the program. However, reaching the HIPC completion point by year's end has been a widely shared national goal, helping the implementation of important reforms.
- **Macroeconomic performance has been generally satisfactory.** Economic activity is recovering, inflation remains subdued, and official reserves are above program targets. Formal sector employment is growing moderately, poverty indicators are improving, and further progress has been made in restructuring the domestic debt.
- **All quantitative and structural PCs for end-September 2003 were met, with two exceptions.** Completion of the asset recovery plan (PC for end-September) was slightly delayed, and the continuous PC against external arrears was not observed as some payments through Euroclear were not made to avoid attachment of funds by a vulture creditor.

Policy discussions

- **The macroeconomic framework for 2004 is being maintained.** The program assumes real GDP growth of 3.7 percent in 2004, with inflation targeted at 5 percent, and a further improvement in the central bank reserve position.
- **The fiscal program is on track, although important challenges remain.** The 2004 budget (approved by the assembly) is consistent with the program. Following two rounds of tax reform in 2002–03, fiscal reforms focus on strengthening tax administration, and passage of legislation on fiscal responsibility and debt management.
- **Monetary policy has been appropriately geared toward supporting the crawling peg exchange rate system.** The central bank is finalizing an exchange rate study that will evaluate medium-term options for greater exchange rate flexibility.
- **Financial sector reforms are continuing.** Recent actions taken include norms to limit maturity risk, reforms to the legal framework, and improvements in supervision. The ongoing FSAP should help identify key remaining vulnerabilities and reform needs.
- **Even after completion of debt relief under the enhanced HIPC Initiative, Nicaragua's public debt will remain large.** Fiscal consolidation will, therefore, need to continue for medium-term debt sustainability to be achieved.
- **Program risks remain high.** Domestic consensus on the program could weaken after HIPC completion and in the run-up to the November 2004 municipal elections. Economic vulnerabilities include the high public debt, weak banking sector, and widespread dollarization. Quarterly reviews will, therefore, continue through 2004.

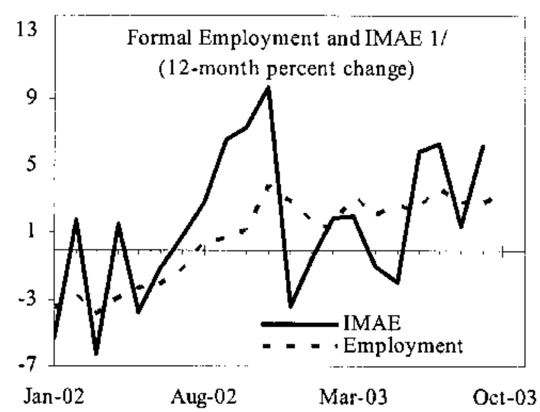
I. Background and Recent Developments

Overview

1. **Although the political situation has again become very difficult (Box 1), the authorities have persevered with implementation of the program.** In November, the transfer of former president Alemán from prison to house arrest signaled a political rapprochement between the opposition *Sandinistas* and the camp around the former president, potentially weakening President Bolaños's government. Soon thereafter, however, this rapprochement broke off and, in early December, Mr. Alemán was sentenced to 20 years in jail and a large fine (the sentence is still subject to appeal). Despite the political turbulence, the authorities have been able to keep the program on track, in part because there is a broad national consensus on the goal of reaching the completion point under the enhanced HIPC Initiative[1] by end-2003. Nonetheless, the volatile political situation implies heightened risks to the program. It remains to be seen how the shifting political alliances will settle and how the government can muster the necessary domestic support to carry the reform program forward, beyond HIPC completion.

2. **Macroeconomic performance has been generally satisfactory:**

- ***A moderate recovery is underway, with continued low inflation.*** Real GDP growth in 2003 is projected at around 2½ percent (up from 1 percent in 2002).[2] Credit to the private sector has recovered in recent months, and formal sector employment has been growing at an annual rate of 3–4 percent. The 12-month inflation rate was 6 percent in November, in line with the program.



1/ Monthly economic activity index.

- ***NIR surpassed the September program target by US$39 million (1 percent of GDP).*** This mainly reflects a stronger private capital balance and buoyant foreign remittances (projected to increase by 15 percent in 2003).[3] However, exports are expected to be flat this

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[1] Hereafter referred to as the HIPC completion point.

[2] On the supply side, most of the growth comes from manufacturing, commerce, transport, and communications. On the demand side, it is supported mainly by private consumption and public investment.

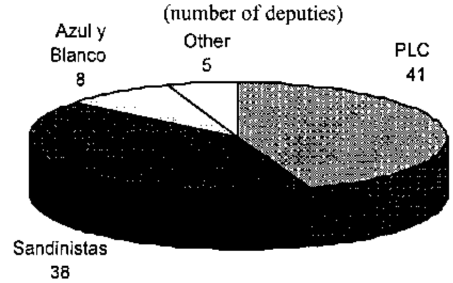
[3] The authorities did not want to raise the NIR floor from the programmed level because of the high volatility of these flows.

Box 1. Recent Political Developments and Program Risks

Background

Nicaragua has long been divided into two political camps, one of which fractured last year. The *Sandinistas* control about 40 percent of the electorate (mainly urban workers). *The Gran Partido Liberal* coalition, led by the *Partido Liberal Constitucional* (PLC, the party of which President Bolaños was a candidate), helped elect President Bolaños in 2001 and has about 55 percent of the electorate (mainly rural and businesspersons). In mid-2002, a majority of the PLC establishment withdrew its support from the government due to the prosecution of former president and PLC leader Alemán, on corruption charges. As a result, the government had to seek new alliances (mainly with the *Sandinistas*) for key policy initiatives.

Nicaragua: Composition of Assembly
(number of deputies)



Source: National Assembly.

Weak institutions and governance problems have compounded the stymieing effect of political polarization. Key public institutions, including the judiciary and the comptroller's office, are widely perceived to be controlled by particular interests, and the large domestic debt (which emerged mainly from repeated banking crises and compensation for confiscations during the *Sandinista* era) is viewed as at least partly a result of corruption. As a result, confidence in public institutions has been low, and governments have often found it difficult to build stable majorities in the assembly, ensure the rule of law, and administer consistent tax enforcement, regulation, and prudential oversight.

Recent events and heightened program risks

The tactical alliance between the government and the *Sandinistas* has all but ended, and it is not clear how and when the shifting political alignments will settle. In November 2003, a dispute over judicial reform led the *Sandinistas* to withdraw their support for the Bolaños administration. Soon thereafter, Mr. Alemán was transferred from prison to house arrest, in a move that was broadly perceived as politically motivated. Discussions then followed between the *Sandinistas* and PLC supporters of Mr. Alemán on several important political initiatives, such as delaying the 2004 municipal elections and restructuring the national assembly, the supreme court, and the electoral court, which could have seriously weakened the government. However, the rapprochement between the *Sandinistas* and Alemán's supporters broke down in early December. Mr. Alemán was subsequently sentenced to 20 years in jail and a large fine. A few days later, the government's 2004 budget was approved with the support of the PLC.

Public reaction to these developments has been mostly supportive of the government. Public opinion polls indicated that a large majority of the population disapproved of Mr. Alemán's transfer as politically motivated. Donors expressed concern over the apparent political interference in the judiciary. Most observers, including donors, have welcomed Mr. Alemán's subsequent conviction.

The volatile political situation implies heightened risks to the program. In the staff's view, while the situation is still fluid, the government can, once again, count on only a small minority of supporters in the assembly. Although this situation has been superseded somewhat by the strong and near-universal consensus on the importance of HIPC completion and associated reforms, sustained successful program implementation next year and beyond will require a new alliance of forces in support of prudent policies and reforms.

year, due to shortfalls in gold production and sluggish external demand for key export products (meat, sugar, and fishing products). Coffee is slowly recovering, following last year's sharp downturn in world prices.

- ***The fiscal program is broadly on track.*** Data through September 2003 show better-than-programmed results for the combined public sector's (CPS) overall deficit after grants (2.0 percent of GDP, compared with 2.5 percent of GDP in the program),[4] savings, and net domestic financing. A shortfall in central government tax revenues (0.2 percent of GDP) was more than offset by a lower quasi-fiscal deficit in the central bank.

- ***Further progress has been made in restructuring the domestic public debt.*** The three largest holders of bank resolution bonds (BRB) agreed to restructure US$320 million of debt falling due in 2003–04.[5]

3. **All PCs for end-September 2003 were observed, with two exceptions.** As reported in the Staff Report (10/3/03), the asset recovery program was completed in October, with all auction proceeds collected[6] and the remaining assets transferred to the finance ministry. On this basis, the staff supports a waiver of the September PC on concluding the asset recovery program. The continuous PC on the nonaccumulation of external arrears remains not observed because of Nicaragua's decision not to pay debt service through Euroclear on some of its bonds. To date, US$1.8 million in interest is overdue. If not addressed, overdue payments will rise to US$4.2 million after February 1, 2004, including US$0.2 million in late amortization payments. A waiver for this PC was granted at the last review, and the staff again supports a waiver in light of the small amounts of arrears and the actions taken by authorities.[7]

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[4] During this period, the CPS deficit before grants was 5.8 percent of GDP, compared with 6.4 percent of GDP in the program.

[5] Agreements with the two largest bondholders refinanced US$280 million of debt payments falling due in 2004 over 10 years, with semi-annual payments and an average annual interest rate of 8.4 percent. The third agreement restructured US$40 million falling due in December 2003 over three years, with semi-annual payments at an annual rate of 7.4 percent. The previous interest rate on these bonds was 11–21 percent.

[6] Proceeds for one sale (US$480,000) are pending the resolution of a legal dispute initiated by a bidder.

[7] In September 2003, a court in Brussels issued a decision requiring proportional debt-service payments by Nicaragua to a claimant when making payments through Euroclear. The authorities have appealed the decision and intend to seek an agreement with private creditors (on debt eligible for, but not included, in a 1995 World Bank–sponsored buyback) on terms

(continued)

4. **Poverty indicators have improved in recent years.** Between 1998 and 2001, the number of poor dropped from 47.9 percent to 45.8 percent of the population, while the share of extremely poor fell from 17.3 percent to 15.1 percent of the population. The improvement took place in both rural and urban settings and across much of the country. The exception was the rural central region, where poverty increased.[8] Despite these improvements, Nicaragua does not compare favorably to other countries in the region, with most social indicators worse than the regional average.

II. Policy Discussions[9]

5. **The macroeconomic framework for 2004 is being maintained.** The key economic objectives are:

	Prel. 2002	Prog. 1/ 2003	Proj. 2003	Prog. 1/ 2004	Rev. Prog. 2004
Real GDP growth (in percent)	1.0	2.3	2.3	3.7	3.7
Consumer prices (end period)	4.0	6.0	6.0	5.0	5.0
Gross international reserves (in millions of US$)	454.1	446.7	446.7	524.1	524.1
Change in augmented BCN reserve position (in millions of US$)	81.9	55.1	75.9	61.0	66.2
Combined public sector deficit after grants (in percent of GDP)	-5.5	-3.8	-3.2	-3.8	-3.8 2/

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

1/ As stated in the Staff Report (10/3/03).
2/ Assumes new pension system takes effect in July 2004 (compared with January 2004 assumed earlier). The deficit in the "Prog. 2004" column has been adjusted for this delay to be comparable with "revised program" column.

comparable to those extended by official creditors (see Appendix V of the Staff Report (10/3/03) for more detail).

[8] This region was particularly hard hit by the coffee crisis.

[9] Paragraph references (¶) in this section refer to the SMEFP, unless otherwise indicated.

A. Fiscal Policy

6. **The draft 2004 budget passed by the assembly is consistent with the program.**[10] The authorities noted that better collaboration with the assembly this year helped prevent a repeat of the problems that occurred with the 2003 budget (when the assembly approved significantly higher spending than submitted by the government). The mission also met with members of the assembly to stress the importance of passing a budget that is in line with the program—a prior action for the review and a key condition for HIPC completion. The authorities will continue monitoring expenditures closely to ensure meeting the program's fiscal targets, particularly given the recent (albeit small) revenue shortfalls.

7. **Achieving the programmed strengthening of the tax effort remains a challenge.** Revenues from the minimum corporate income tax have been below target, as some firms reported lower assets than in previous years while others opted to delay payments until lawsuits brought against the tax are settled.[11] The authorities are taking corrective measures, including legal actions against delinquent taxpayers and increased audits of firms, in the context of their action plan (¶7, first bullet) to improve tax administration (see below). In November 2003, the authorities published a sharply reduced list of VAT-exempted inputs (with exemptions reduced from inputs of 53 products to those of eight basic products, in line with the May 2003 tax reform).

8. **On the expenditure side, the aim is to improve the anti-poverty and pro-growth orientation of public spending (¶9).** In this context, the authorities intend to focus on the recommendations of the public expenditure commission (the Staff Report (10/3/03), paragraph 11 and ¶7, seventh bullet), including to improve financial management through creation of a unified registry of public investment, and better monitor public spending (structural benchmark). Since the recommendations will take time to implement, the authorities have made the commission permanent.

9. **The operating surplus of state enterprises is programmed to improve in 2004.** The public water and sewerage company (ENACAL), traditionally a weak performer, is being revamped; key managers have been replaced, efforts to collect bills and arrears are being stepped up (supported by a draft law submitted to the assembly), additional meters are being installed, and software is being updated to strengthen financial controls (¶8). Further

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[10] The budget aims at a CPS deficit (after grants) of 3.8 percent of GDP, savings of 2.9 percent of GDP, and poverty-reducing spending of 11.4 percent of GDP (¶5). According to Nicaraguan law, once approved by the assembly, the budget can only be modified through an initiative from the executive branch.

[11] Some members from the chamber of industry have challenged the new corporate income tax and other measures (mainly on procedural grounds). The process is expected to take several months. In the meantime, the tax reform is being implemented.

tariff adjustments are planned for June 2004, and billing and collection will be outsourced in the second semester of 2004. For the electricity sector, the government is developing a comprehensive reform, with World Bank and IDB assistance, to further improve efficiency, make government subsidies more transparent, and improve the legal and regulatory framework (¶14).

10. **Key fiscal reforms are underway to support medium-term fiscal sustainability (Box 2).**

- **The internal tax office (DGI) has already begun implementation of its reform plan (¶7, first bullet) and the customs office (DGA) will begin implementation in March 2004 (structural benchmarks).**[12] A new tax code was submitted to the assembly in November 2003 and its approval is expected by March 2004. The administrative career law for DGI and DGA was also submitted to the assembly in November 2003, with approval expected by June 2004.

- **In July 2003, the assembly approved the transfer of 4 percent of central government tax revenues to the municipalities starting in 2004, rising gradually to 10 percent, economic conditions permitting.**[13] The broad objective of decentralization is to improve the quality of spending through a gradual transfer of revenue and spending responsibilities.[14] The staff urged that the decentralization process be carried out in a cautious and fiscally neutral manner. Current tentative plans call for fiscal neutrality only after several years, with a net negative impact on the overall fiscal balance of about half a percent of GDP on average during 2004–06. The authorities said they would consider the staff's recommendations in finalizing their plans, with World Bank assistance. The executive branch will issue a presidential decree to modify the municipal transfers law by September 2004 (benchmark) in order to delineate clearly spending responsibilities between the municipal and central governments.[15]

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[12] These reform plans are being developed with technical assistance from the Fund and the IDB. Priority actions for the DGI include strengthening the large taxpayer unit and preparing a strategic information technology plan.

[13] The law envisages raising the share of revenues to be transferred by at least half a percentage point each year—as long as real GDP growth in the previous year exceeded 1 percent—rising to a minimum of 10 percent of revenues by 2010.

[14] Several institutions, including the ministry of finance, the comptroller's office, and the secretariat of coordination and strategy of the presidency (SECEP) will be involved in monitoring this spending.

[15] The World Bank's Poverty Reduction Support Credit (PRSC) also includes conditionality on allocating spending responsibilities between the central administration and municipalities.

Box 2. Attaining Fiscal Sustainability

A key goal of the authorities' medium-term strategy is attaining fiscal sustainability. The strategy builds on the achievements of the two-stage tax reform and includes a comprehensive set of actions aimed at improving tax administration, strengthening the legal framework, and increasing the efficiency of spending. The main components of the medium-term strategy are:

- **Tax administration reform.** The objective of reforming the domestic tax (DGI) and customs administrations (DGA) is to increase revenue collections by transforming the tax administration into a modern and efficient institution and strengthening the legal framework. The IDB and the Fund's Fiscal Affairs Department have been providing technical assistance. Reforms have already begun in the DGI, and will begin in the DGA in early 2004.

- **Tax code.** The tax code defines the obligations of taxpayers and tax officials and provides the tax administration with the legal tools to enforce collection and penalize evasion. A revised version was submitted to the assembly in November 2003.

- **Administrative career law for customs and tax office.** This law will strengthen human resource management in the domestic tax and customs administrations. It will define the criteria for hiring, promotion, and retirement and will regulate performance evaluation. Approval of the law is expected by June 2004.

- **Public spending commission.** The public spending commission has recommended steps to improve the composition and quality of spending with a view to enhancing economic growth and reducing poverty. The authorities have made the commission permanent to assist the government in implementing their recommendations.

- **Financial administration law.** The objective of this law is to improve, coordinate, and regulate the systems of public administration such as the budget, treasury, and public credit. The law will harmonize the methodology of the budget at the different levels of the public sector. A draft of the law will be submitted to the assembly by end-2004.

- **Fiscal responsibility law.** This law will determine ceilings for key variables, such as the combined public sector overall deficit and public debt. It will introduce the practice of multi-year budgeting. A fiscal stabilization fund will be created to avoid sharp fiscal adjustments and promote savings. A draft law will be submitted to the assembly by June 2004.

- **Civil service law.** This law regulates the career of public sector employees. It establishes a transparent hiring system and determines salaries according to responsibilities. The law was approved by the assembly in November 2003.

- **A law on fiscal responsibility will introduce a multi-year budgeting framework and establish ceilings for key variables such as the CPS deficit and public debt.** A draft law (¶7, third bullet) will be submitted to the assembly by June 2004 (performance criterion), and its approval is expected by December 2004 (benchmark).[16]

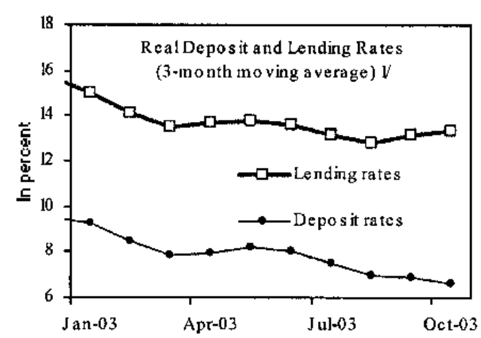
- **The authorities, in consultation with the World Bank, are preparing a roadmap for further pension reform.**[17] They are currently assessing policy options (including possible changes to contributions, eligibility, and benefits formulas) to ensure that the fiscal impact of the reform is sustainable (¶7, fourth bullet).

- **In November, the assembly approved a public debt law that establishes a centralized process for contracting public sector debt, both internal and external (benchmark for December 2003) (¶7, fifth bullet).** A new technical committee is to advise the government on debt issues to ensure that appropriate debt management criteria are used and the implications of new borrowing for debt sustainability considered. While staff supports most provisions of the law, some changes introduced in the legislative process are suboptimal—such as a provision that would empower municipalities to contract debt with government guarantees, powers that should be tightly circumscribed and monitored.

- **The Nicaraguan authorities have further refined the expenditure tracking mechanism for the use of HIPC interim debt relief, with assistance from the World Bank.** The Supplementary Social Fund is responsible for monitoring the use of budgetary savings resulting from HIPC debt relief, which is reflected in poverty-related outlays identified in the central government budget (¶7, sixth bullet).

B. Monetary and Exchange Rate Policies

11. **The stance of monetary policy is appropriate, as evidenced by the continued achievement of the program objectives for NIR and inflation (in the context of the crawling peg regime).** The authorities noted that the prudent stance of monetary and fiscal policy has continued to reinforce confidence, as reflected in an improved reserve position and the declining trend of interest rates over the past year. The monetary program for 2004 targets a further buildup of



Source: Central Bank of Nicaragua.
1/ U.S. dollar-linked instruments

[16] The law is being prepared with technical assistance from the IDB.

[17] A new pension law was approved in 2000.

US$20 million in NIR, plus a net repayment of BCN domestic debt equivalent to US$46 million, with base money growth of about 10 percent. The conduct and instruments of monetary policy, especially open market operations, are being examined in the context of the FSAP.[18]

12. **Exchange rate policy continues to follow the crawling peg system.** In 2004, the rate of crawl is to be lowered to 5 percent (¶11) (from 6 percent in 2003).[19] The central bank is working on its study of the exchange rate system.[20] The FSAP will examine the vulnerability of banks and firms to exchange rate and interest rate changes, in the context of widespread financial dollarization.

C. Financial Sector Reform

13. **Although official banking data continue to indicate a relatively sound situation, there are concerns about data accuracy.** Capital adequacy ratios average almost 18 percent, but the high provision coverage (149 percent of nonperforming loans) is likely to mask significant loan refinancing, including of coffee-related loans with uncertain recovery prospects. The authorities expected that the FSAP would help them assess the underlying vulnerability of the system and recommend ways to improve the data.

Financial Sector Indicators, 2001–03 1/

	2001	2002	Sept. 2003
Capital adequacy ratio (in percent)	16.3	18.1	17.8
Nonperforming loan ratio	2.9	3.5	3.4
Provisions in percent of NPLs	201.0	161.5	145.3
Pre-tax return on equity	50.8	56.6	61.5

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

1/ Comprises commercial banks. Revised information due to methodological changes.

14. **Better legal protection for bank supervisors is an urgent priority.** The authorities agreed with staff on the importance of such protection, highlighted by a number of recent court cases. They intend to propose legislation to grant legal protection to supervisors and central bank staff for their official actions—in line with recent MFD recommendations—by end-2003, with approval expected by mid-May 2004 (both submission and approval are PCs) (¶12).

[18] The first FSAP mission visited Managua in November/December 2003.

[19] The real effective exchange rate depreciated by 11 percent in the year to September. External competitiveness appears adequate.

[20] The authorities intend to complete the study by the time of the next program review (April 2004), allowing time to incorporate results of the first FSAP mission.

15. **Other key steps to strengthen the financial sector include (¶12):**

- A prudential norm to limit risks derived from maturity mismatches (adopted in October) in line with MFD recommendations and a benchmark under the program;

- Revision of the bank inspection manual, including new procedures for on-site inspection (benchmark for December 2003); and

- Reform of the legal framework in line with Basel Core Principles (benchmark for mid-May 2004).

D. Program Financing

16. **Program financing in 2004 will continue to rely heavily on concessional project and balance of payments loans.** The authorities will seek to ensure that all debt restructurings are on terms comparable to those extended by the Paris Club (Letter of Intent, ¶4). The donor community expressed strong support for the authorities' national development plans during the October 2003 consultative group meeting, and the current high level of assistance is expected to be sustained.

17. **Privatization is projected to yield about US$17 million in 2004.** This is less than half the amount in 2003 (reflecting mainly the completion of the asset recovery program). After a brief delay in the selection of the investment bank, offers for the government's remaining shares in ENITEL (telecommunications) were received on December 17, 2003 (benchmark) (¶14).[21] Regarding Hidrogresa, the authorities, in close consultation with the IDB and World Bank, have determined that privatization is not advisable at this time, in part because of current regulatory deficiencies; they intend to implement a regulatory reform of the sector, with technical assistance from the international financial institutions, before privatizing Hidrogesa.

[21] The foreign company managing ENITEL has one month to match the best offer, after which the government should decide on the bids the same day.

18. **The main elements of program financing in 2004 are as follows:**

Nicaragua: Program Financing

(In millions of U.S. dollars)

	Prog. 2003	Program 2004				
		QI	QII	QIII	QIV	Total
Total	**417.9**	**99.8**	**109.8**	**95.7**	**102.3**	**407.6**
Disbursement of loans	**243.1**	**79.0**	**70.6**	**67.4**	**42.9**	**259.9**
Total untied disbursements	60.1	37.5	25.0	15.0	0.0	77.5
IDB	34.8	0.0	25.0	0.0	0.0	25.0
World Bank	16.2	35.0	0.0	0.0	0.0	35.0
Others	9.1	2.5	0.0	15.0	0.0	17.5
Total tied disbursements	183.0	41.5	45.6	52.4	42.9	182.4
Disbursement of grants	**133.7**	**20.8**	**38.1**	**28.3**	**43.8**	**131.0**
Total untied grants	31.6	0.8	0.6	0.8	17.6	19.8
Total tied grants	102.1	20.0	37.5	27.5	26.2	111.2
Privatization	**41.1**	**0.0**	**1.1**	**0.0**	**15.6**	**16.7**

Source: Central Bank of Nicaragua.

E. Other Issues

19. **Trade policy.** The authorities' efforts at trade liberalization and regional integration continue. The last round of negotiations toward a U.S.-Central American Free Trade Area (CAFTA) made some progress in difficult areas, such as quotas for dairy products and safeguards for agricultural products. Nicaraguan industry and consumers are expected to benefit from CAFTA not only because of better access to the U.S. market, but also because of the closer regional integration expected to result from CAFTA. Tariff reductions under CAFTA would be phased in gradually over a period of up to 12 years. Since the final shape of CAFTA is still not known, it is not possible to estimate with certainty the fiscal impact. However, the authorities believe that, given Nicaragua's already low tariffs, their expected gradual reduction should have only minimal fiscal impact.

20. **Governance and institutions.** The authorities are pushing ahead forcefully with their efforts to improve governance, strengthen institutions, and fight corruption (Box 3). A civil service law, which aims at creating an efficient and nonpolitical civil service, was approved in November 2003, in line with World Bank recommendations (¶15). In addition, steps are being taken to strengthen public procurement practices and the comptroller's office, with assistance from the IDB. As part of the PRSP and the national development plan, the authorities have made public their strategy for judicial and electoral reform, and have launched a public consultation process (benchmarks for September and December 2003, respectively). The program incorporates a benchmark on presenting an action plan for

Box 3. Enhancing Governance and Promoting Stronger Institutions

Strengthening governance and institutions is key to sustaining private sector confidence, strong economic growth, and international support. The government has embarked on a comprehensive medium-term strategy that aims at improving growth and reducing poverty. The main elements of this strategy include:

- **Civil service reform.** The new civil service law provides the basis for improved management of public sector human resources, including by competitive selection, performance evaluation, and merit-based compensation based on improved job descriptions and classification. Significant progress has been achieved in the preparation of implementing regulations.

- **Public sector procurement reform.** Following preparatory work in the late 1990s with assistance from the IDB, the government began implementation in late-2002. The main components of this reform include:

  - **Comptroller's Office (CO):** upgrading the organizational and management structure, control mechanisms (including through independent auditing of procurement), training programs, and IT infrastructure. An independent firm will be hired to review the institutional structure and assist in the implementation of the action plan.

  - **Procurement.** Internal controls and procurement units of key public agencies are being strengthened. Progress achieved includes a study on risk-prone procurement areas, draft legislation to revise the existing public procurement law, and development of software to monitor the various stages of procurement. While these constitute substantive progress, additional efforts are needed to complete the reform and extend it to other public agencies.

- **Accountability and transparency is being strengthened through better financial management and auditing, as well as on online publication of key fiscal data.**

  - **SIGFA.** Originally launched in 1995, SIGFA became operational in 1998 for the core operations of the finance ministry (budgeting, treasury and accounting). By end-2002, the system was extended to budget formulation and execution for most central administration agencies; two subsystems on cash management and payroll were added; and audit standards were developed. Current actions focus on increasing coverage to most government entities, and adding subsystems on procurement, human resources, and fixed assets.

  - **Single account.** A component of SIGFA, it covers most budgeted revenues and expenditures, allowing for real-time information and control of the government's cash position. However, some agencies and donor disbursements remain outside the scope of SIGFA. Future actions include the development of cashflow programs and extending coverage to additional public agencies and external aid programs.

  - **Online publication.** Data on budget execution are available at the Finance Ministry's web page (www.hacienda.gob.ni); so are extensive data on foreign aid programs (www.cancilleria.gob.ni).

Judiciary reform. As part of the national development plan, the authorities in September 2003 presented their plan for judicial reform and initiated public consultations. The main elements of the plan are to strengthen independence of the judicial branch from political parties by modifying the procedures for selecting judges, and to improve the organizational structure and regulatory framework.

judicial reform by June 2004. Despite the efforts to improve governance, Nicaragua still has worse-than-average governance indicators compared with other countries in the region.

21. **Safeguards assessment.** The authorities are taking steps to implement the recommendations of the August 2003 update to the safeguards assessment (¶16). The BCN Board has adopted a policy to appoint external auditors for three-year terms. It has also committed to adopt International Accounting Standards beginning with the 2004 financial statements.

22. **Financing assurances review.** Nicaragua's outstanding commercial debt and the recent nonpayment of US$1.8 million in interest payments on domestically issued bonds held by nonresidents have triggered the Fund's lending-into-arrears policy. An assessment of financing assurances (Box 4) considers that the financing of the program is reasonably well assured. The authorities are pursuing a collaborative approach with holders of indemnity bonds and other private commercial creditors. Furthermore, in view of the relatively small payments that have been disrupted, the financing of the program remains intact.

Box 4. Review of Financing Assurances

The staff considers that in light of the steps the authorities have taken to pursue a collaborative approach with holders of the indemnity bonds and other private commercial creditors, they have met the good-faith criterion established under the Fund's policy for lending into arrears.

The authorities have continued their efforts to reach an agreement with commercial creditors holding debt eligible for, but not included in, a 1995 World Bank–sponsored buyback. Following the recent litigation in Belgium (the Staff Report (10/3/03)), the authorities are contacting all holders of unrestructured debt that was eligible for the 1995 debt buyback.

- **Discussions remain informal, and there is still no coordination among holders of the commercial debt.** The authorities have stressed that Nicaragua is a HIPC, and that the settlement terms must be at least comparable to those of the Paris Club.
- **Nicaragua has opened discussions with one private creditor, with the goal of achieving a settlement on Paris Club comparable terms.** The authorities hope the settlement will become a model for the remaining creditors. While the situation is still developing, staff considers that the authorities have engaged in good-faith negotiations.

The situation with the holders of *Bonos Para Indemnización* (BPIs) affected by the Brussels court decision in August is unchanged since the previous review. Debt service on these bonds has been included in the 2004 budget.

- **The authorities remain in contact with the holders of BPIs and have appealed the Brussels court decision.** The appeals process is likely to be protracted, with a decision on the case unlikely before February or March 2004.
- **Payments on the bonds are due semi-annually.** Following the interest payment of US$1.8 million due (and not made) in August 2003, the next payment is due in February 2004, including US$2.2 million in interest and US$0.2 million of principal. Should payment on these bonds continue to be enjoined in February 2004, the authorities will deposit this payment, as they have done with the previous one, in a special account at a local bank.

23. **Statistical issues.** While there has been substantial progress in improving Nicaragua's statistics, further work remains to be done. Current actions are focused on producing quarterly GDP numbers and aligning monetary statistics with international standards. The authorities are also taking steps to participate in the GDDS.

III. Medium-Term Strategy and Debt Sustainability

24. **The authorities' updated medium-term strategy aims at achieving strong economic growth, reducing poverty, and maintaining financial stability.** The strategy involves accelerating structural reforms, strengthening the development of human capital and basic infrastructure, creating an enabling environment for private sector development, and using international trade agreements to boost growth. Key sectors driving growth over the medium term include manufacturing and commerce, which together account for over one-third of GDP.

25. **The government's second annual progress report of the PRSP embodies these goals.**[22] While near-term growth projections have been trimmed somewhat reflecting recent trends, over the medium term, growth is expected to converge toward potential output growth, estimated to be about 5 percent. As discussed at the last review, the government's National Development Plan (NDP) aims at higher public investment (relative to the original PRGF-supported program targets) financed by concessional external resources, while maintaining the overall stabilization and reform goals of the program. The authorities remain committed to the PRSP process (Box 5), and they intend to broaden the NDP into a revised PRSP in early 2004, in close collaboration with World Bank and Fund staff (including at a workshop in Managua in January/February).

26. **Fiscal policy will continue to be geared to achieving debt sustainability.** The strategy aims at a steady reduction of the CPS deficit through continued improvements in tax administration, rationalization of government expenditures, and strengthening the performance of public enterprises. The primary deficit of the CPS (before grants) is targeted to decline from 3.6 percent of GDP in 2004[23] to 1.7 percent in 2008. Over the same period, the total public debt (face value) is projected to decline from 126 percent of GDP to 108 percent (in net present value (NPV) terms, the debt would fall from 70 percent of GDP to 66 percent over the same period).

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[22] The companion Joint Staff Assessment paper reviews and appraises the second PRSP progress report.

[23] Adjusted by assuming full-year pension reform, for comparability with the 2008 target.

Box 5. National Development Plan and the PRSP

The authorities remain fully committed to the PRSP process and the PRGF-supported program. The second PRSP progress report summarizes the authorities' actions to reduce poverty, and the new National Development Plan (NDP) aims at enhancing the PRSP. In particular, the NDP:

- develops in greater detail the first pillar on economic growth and structural reforms;
- expands on the need for institutional reforms; and
- incorporates geographic and migration analysis to public policies (by considering economic productivity of regions and migration flows in government policies).

The president announced a preliminary version of the plan in September 2003, noting that upon its adoption it will become the strategic guide of government policies. He requested comments from all stakeholders by end-2003.

In early 2004, the authorities intend to use the NDP as a basis for an enhanced PRSP. The intention is to incorporate the lessons of three years of implementing the PRSP (prepared in 2001) into a revised PRSP. Experience has shown, in particular, the need for:

- improved costing of social targets;
- increased emphasis on export growth through international trade agreements;
- detailed plans on judicial reform and decentralization;
- higher-quality public spending; and
- better alignment of the PRSP with the budget and the PRGF.

To these ends, the authorities are planning a growth workshop in early 2004, with broad-based participation including the multilateral organizations.

The reaction of local stakeholders to the NDP has been favorable. The authorities held regional workshops during the preparation of the NDP, and made presentations to selected groups, including political parties, press, business groups, and NGOs. Civil society groups called for greater participation in determining investment priorities. Some participants stressed the importance of a broad political consensus for reform of key institutions, such as the judiciary and electoral bodies.

The NDP was well received during the recent consultative group meeting in Managua. Donors agreed that it provided a sound long-term vision for Nicaragua. Specific suggestions for improvement included expanding public consultations and participation and greater attention to issues such as decentralization, social equity, gender equality, environment, and local markets. Donors also urged a more accessible form of presentation that makes the NDP easily understood by the public.

27. **A revised Debt Sustainability Analysis (DSA) underscores the need for continued prudent fiscal and external borrowing policies.** The authorities have updated, in close consultation with Fund and Bank staff, the external DSA for the completion point. At that time, nominal external debt is expected to drop to 81 percent of GDP (in NPV terms, 168 percent of exports). Assuming implementation of policies in line with the program and the PRSP, the external debt is projected to fall to 136 percent of exports by 2016. Alternative scenarios to test the vulnerability of the medium-term outlook to lower growth and foreign assistance, as well as higher domestic absorption (which has often preceded elections), underscore the importance of maintaining prudent macroeconomic policies. The results of the staff's DSA are presented in the accompanying completion point document.

28. **The authorities recognize that a prudent borrowing policy is necessary to keep the public debt on a sustainable path.** New laws on public debt and fiscal responsibility are aimed at strengthening debt management and ensuring that debt sustainability remains a focus of fiscal policy. The authorities intend to seek external financing, to the extent possible, only on highly concessional terms. In addition, the authorities are working to improve, with the support of the World Bank, the selection of investment projects in order to meet the objectives of the PRSP.

IV. Program Risks and Monitoring

29. **The difficult political situation remains a major program risk.** Recent progress with reforms has been able to build on the strong domestic consensus in favor of reaching the HIPC completion point. However, the recent political turbulence implies heightened risks for the program, and the domestic consensus for reforms could weaken after the completion point and in the run-up to the municipal elections (November 2004). Key economic vulnerabilities stem from high public debt, a weak banking sector, the crawling peg, and widespread dollarization (for example, since the government's debt is mostly dollar-denominated or -linked, a large devaluation would have a major effect on the fiscal position as well as the health of the banking system). On the upside, the favorable external environment provides a good opportunity to press ahead with key reforms, and the recent adoption of a prudent budget should also help lock in continued sound fiscal policy in 2004. Substantial external financing conditioned on successful program implementation should also promote policy and reform continuity.

30. **Program monitoring.** Quantitative PCs are being proposed through June 2004, and indicative quarterly targets through December 2004. Approval by the assembly of a 2004 budget consistent with the program is a prior action for this review. New PCs on granting legal protection to bank supervisors (submission for December 2003 and approval for mid-May 2004) and submission of the Law on Fiscal Responsibility (June 2004) are being proposed. In addition, benchmarks are being proposed for decentralization, tax administration, fiscal responsibility law, law on administrative career for DGI and DGA, judicial reform, and on the quality of public spending.

31. **The authorities have requested a modification of the 2004 PCs on public savings, net domestic financing, and net domestic debt reduction, as well as a change in the definition of the external arrears PC.** The recent restructuring of domestic public debt (paragraph 2) has made it operationally easier to calculate all interest payments on a cash basis.[24] Hence, the program targets have been redefined on a cash basis. In addition, the authorities have requested that the definition of net domestic debt reduction be expanded to include central government debt. The authorities have also requested that indemnity bonds (issued locally and governed by Nicaraguan law) be excluded from the performance criterion on external arrears. Finally, pension reform is now projected to begin on July 1, 2004, rather than January 1, 2004. The program has an adjustor for such a delay, but the latest six-month delay has been incorporated into the unadjusted PCs. These modifications do not imply any change in the policy stance. The original and revised PCs are shown in Table 1 of the Supplementary Memorandum of Economic and Financial Policies.

V. Staff Appraisal

32. **Performance under the PRGF-supported program has been satisfactory**. The staff commends the authorities for their strong ownership of the program, which has contributed to a broader understanding in Nicaragua that a stable macroeconomic framework, structural reforms, and better governance are essential to achieving strong and lasting economic growth and poverty reduction.

33. **While the program has produced favorable results, the economy remains vulnerable to shocks.** Real GDP growth is recovering, inflation remains subdued, the external position has strengthened, and economic prospects have improved. However, significant vulnerabilities remain, including from the large public debt, the weak financial sector, and widespread dollarization.

34. **Restoring macroeconomic stability has been an important achievement, but preserving it and delivering sustained rapid growth remains a challenge**. Boosting growth in a lasting way will require further investment, especially new private investment, which in turn will depend on greater legal certainty, institutional reforms, and better governance. With growth projected to rise and the external environment becoming more favorable, the coming year presents an excellent opportunity to move ahead forcefully with the reform agenda.

[24] In the past, interest payments were on a cash basis, except for those on bank resolution bonds, which were calculated on an accrual basis. The central bank and ministry of finance are taking steps to improve their debt statistics in order to estimate all interest payments on an accrual basis, in line with the latest GFS manual. Staff will work with the authorities to ensure that this is done as quickly as possible.

35. **Consolidating the domestic consensus on reform will be critical.** HIPC completion will be a major milestone for Nicaragua once approved by the Boards of the Bank and the Fund. The challenge then will be to maintain the support for reforms after this is achieved and in the run-up to municipal elections later next year. Nicaragua should use the improving economic situation not as grounds for complacency, but as an inspiration for pressing ahead with their medium-term growth and poverty reduction strategy. The program's design, including a prudent fiscal stance and external financing contingent on continued sound policies, should mitigate against those risks. The staff encourages the authorities to further deepen the public consultation process and reinforce the transparency of government policy, so that the public can add its support to the reform process.

36. **Continued strengthening of the public finances is key to macroeconomic stability**. In particular, tax administration must be improved and the quality of public spending (including poverty-reducing spending) enhanced. Over the medium term, continued fiscal consolidation coupled with debt relief under the enhanced HIPC Initiative and continued concessional donor support, especially grants, will be necessary to ensure sustainable debt dynamics. Given the risks to the baseline fiscal strategy, including from potential political difficulties in fully implementing all of the government's expenditure-rationalization and revenue-enhancing measures, as well as the uncertain yield from these complex reforms, staff recommends that the government prepare fiscal contingency plans.

37. **The staff emphasizes the need to strengthen the financial condition of state enterprises.** It welcomes the authorities' plans to improve the efficiency of water and sewerage operations while expanding these critical services. The situation in the electricity sector also remains a concern.

38. **Despite the progress achieved, the prudential and supervisory framework of the financial sector needs to be strengthened further.** The staff strongly welcomes the successful completion of the central bank's asset recovery program, a difficult yet essential element of the program. The staff urges the granting of appropriate legal protection to bank supervisors, to ensure their ability to work effectively, and encourages the planned overhaul of the legal framework for bank supervision, including introduction of effective consolidated supervision. The FSAP, which started in November 2003, will help identify the principal remaining vulnerabilities and reform needs in the financial sector.

39. **Nicaragua's structural reform program is expected to boost growth and reduce poverty.** The staff commends the authorities for pushing ahead with their efforts to improve governance, strengthen institutions, and fight corruption. The recent approval of a civil service reform is a major step forward in this direction. The staff also welcomes the design of a roadmap for future pension reform, with World Bank assistance, and the strengthening of public procurement practices and the comptroller's office, with support from the IDB. The staff encourages the authorities to allow for flexibility in adjusting the parameters of pension reform (including contributions, eligibility, and benefits formulas) in a manner that ensures fiscal sustainability. Judicial reform is particularly important for Nicaragua's ability to attract investment, and the staff urges the authorities to persevere with and accelerate their plans in this area.

40. **Close program monitoring remains essential.** The program's design should help mitigate the significant program risks, including through strong prior actions (including the budget for 2004) and quarterly reviews. The staff encourages the authorities to monitor developments under the program carefully, and to be prepared to address quickly any emerging program deviations.

41. **Based on the satisfactory performance under the program, the staff recommends completion of the fourth review under the PRGF, including waivers of two PCs.** Economic developments and policies remain broadly in line with the program, and the outlook has improved notably from what it was at the start of the program. Satisfactory assurances of external financing are evidenced by the large commitments for concessional aid and prospective debt relief under the enhanced HIPC Initiative. Moreover, in light of the steps the authorities have taken to pursue a collaborative approach with private creditors, staff is satisfied that the authorities have met the good faith criterion established under the Fund's policy for lending into arrears, and thus, recommends Board completion of the financing assurances review. The staff supports the authorities' request for two waivers of performance criteria because the deviations were minor and the authorities have taken corrective actions.

Box 6. Structural Conditionality

Structural conditionality in the current program. Structural conditionality under the Three-year PRGF Arrangement (2002–05) focuses on Table 2, SMEFP:

- ***Fiscal consolidation:*** The 2004 budget submitted to the assembly supports the key objectives of the program. The commission on the quality of public spending has been made permanent to monitor implementation of its recommendations. Action plans to strengthen the DGI and DGA are expected to reinforce tax administration and the legal framework. The administrative career law for customs and tax office will strengthen human resource management in DGI and DGA. Decentralization is aimed at improving the efficiency of public spending by ensuring greater participation and accountability at the local level for spending decisions. The tax code will define the obligations of taxpayers and tax officials and provide the legal framework to enforce collection and penalize evasion. The fiscal responsibility law will establish a multi-year expenditure framework, including medium-term fiscal targets. The government received a viable offer for the remaining shares of ENITEL in December 2003 and expects to complete the sale in January 2004.

- ***Financial system*:** Strengthening the prudential framework and enforcement of existing provisioning and capital requirements are key program elements. Implementation of new on-site technical and administrative procedures, setting up a new unit at the public deposit insurance agency (FOGADE) as well as implementing the necessary legal amendments for effective bank supervision (in line with Basel Core Principles) are also envisaged in the program.

- ***Governance and transparency*:** Changes to the legal framework of the banking system will include better protection and safeguards for staff of the Superintendency of Banks and the BCN. Judicial reform will support the government's efforts in fighting corruption, strengthening creditor protection and paving the way for foreign investment. The approval of a law on domestic and external indebtedness signals a commitment to a sustainable debt position over the long term.

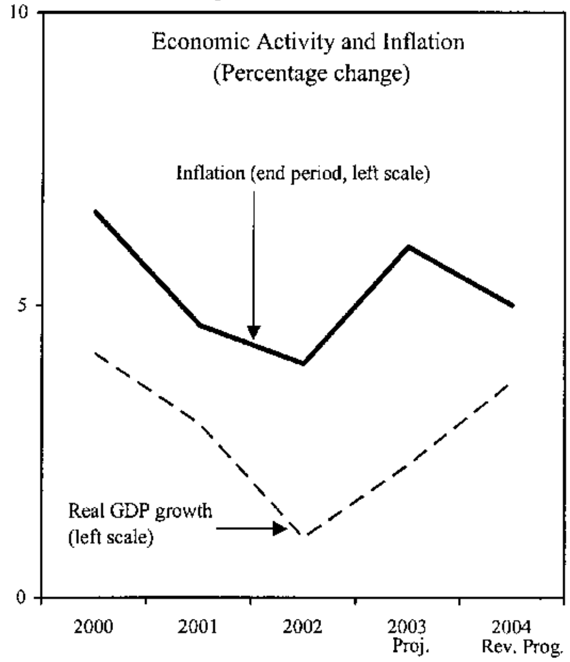
Status of structural conditionality from earlier programs. A three-year ESAF arrangement was approved in March 1998. The first and second reviews under the second annual arrangement of the program were completed in December 2000. The reviews included waivers for nonobservance of structural performance criteria relating to the approval of the social security reform law and issuance of final bid documents for the public electricity company's generation and distribution units and for 40 percent of the public telecommunications company's assets. By end-2001, those structural reforms were implemented. Discussion on the third annual PRGF could not be completed because of significant policy slippages, particularly in the fiscal area. For the third review of the PRGF, the structural benchmark for implementing regular on-site inspections by end-June 2003 was modified to allow more time for the necessary preparatory work.

Structural areas covered by World Bank and IDB. Disbursements of World Bank program loans are conditioned on strengthening the policy and regulatory environment in the telecommunications sector and the rural electricity sector, creating a more equitable and sustainable pension system, working toward improving the quality and planning of public spending reforming the public sector management system and civil service, improving the efficiency and soundness of financial intermediaries that serve small productive units in rural and peri-urban areas, strengthening the superintendency of banks, modernizing rural municipalities, developing human capital, reviving agriculture and strengthening natural resource management, rehabilitating road infrastructure and improving the road maintenance system, improving land administration and strengthening land rights, supporting the social safety net and combating rural poverty, and improving protection from natural disasters. IDB lending operations support strengthening the financial system, modernizing the comptroller's office and the judicial system, reforming the pension system, improving credit to small enterprises and rural cooperatives, reforming the electricity sector, reactivating rural production, supporting decentralization, reinforcing transportation infrastructure, strengthening social protection (with emphasis on child care), modernizing the water sector, reforming the health and education sectors, and improving transparency and control of public procurement.

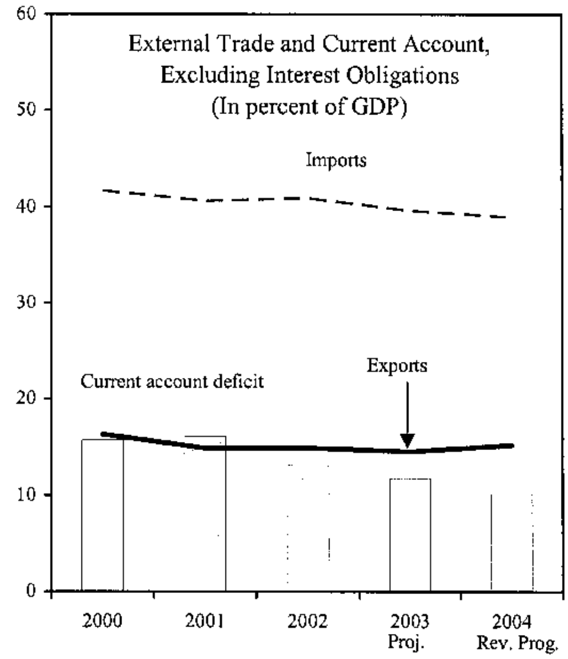
Other relevant structural conditions. Status of implementation of the seven floating HIPC completion point conditions is set out in Table 18. Additionally, the judicial branch has submitted legislation on a new judicial career system to the assembly.

Figure 1. Nicaragua: Main Economic Indicators

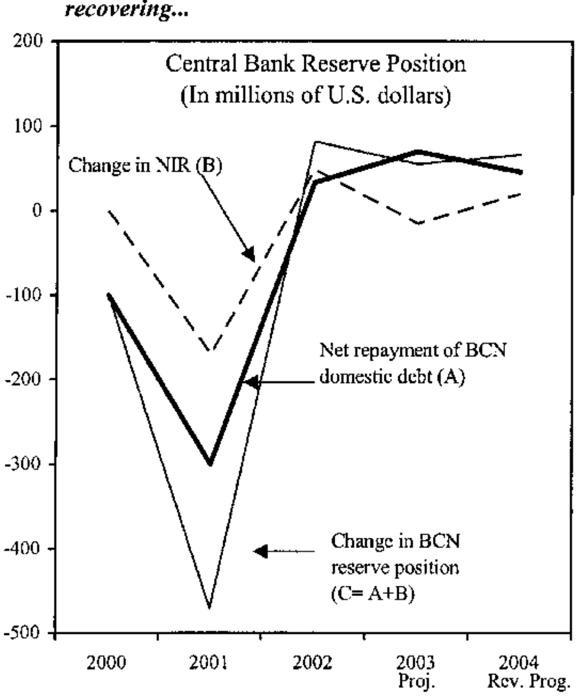
A moderate recovery is anticipated for 2003, with continued low inflation.



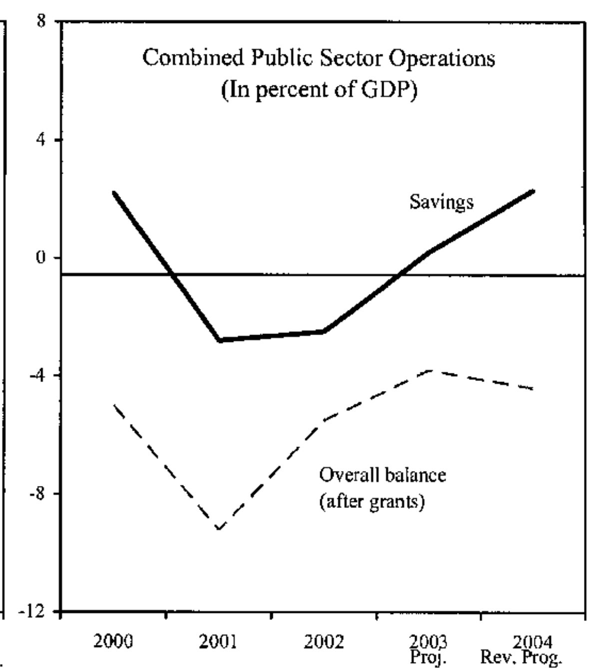
The current account deficit has narrowed, but remains high.



The central bank's reserve position is recovering...



...and the public finances are improving.



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

Table 1. Nicaragua: Selected Economic and Financial Indicators

	2000	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
(Annual percentage change; unless otherwise indicated)							
National income, prices, and unemployment							
Real GDP	4.2	3.0	1.0	2.3	2.3	3.7	3.7
Consumer prices (end of period) 2/	6.6	4.7	4.0	6.0	6.0	5.0	5.0
Consumer prices (period average) 2/	7.4	7.4	4.0	5.2	5.2	5.2	5.2
Unemployment rate (percent)	9.9	11.3	11.6	...	...	...	...
External sector							
Exports, f.o.b.	18.3	-8.1	0.6	-0.1	-0.9	9.3	6.8
Export volume	15.1	7.3	1.9	0.2	-2.2	5.0	3.6
Imports, f.o.b.	-3.0	-1.7	1.0	-0.8	-0.8	2.8	2.8
Import volume	-9.7	2.5	-1.2	-4.3	-4.3	3.2	3.2
Terms of trade (deterioration -)	-4.0	-11.2	-3.3	-3.9	-2.5	4.7	3.7
Nominal effective exchange rate end of period (depreciation -)	2.1	-2.9	-8.1	...	...	...	...
Real effective exchange rate end of period (depreciation -)	8.8	-0.6	-7.9	...	...	...	...
Money and credit							
Net domestic assets of the central bank 3/	22.7	141.7	-28.5	20.6	5.0	-3.6	-3.9
Net credit to nonfinancial public sector 3/	-35.7	343.2	-63.7	-86.3	-103.6	-87.0	-87.0
Net credit to financial institutions 3/	95.5	-54.0	-35.8	-3.4	-3.1	-11.8	-12.9
Currency in circulation	1.1	11.1	7.0	9.7	8.9	9.0	9.9
Financial system liabilities to the private sector	7.3	7.2	13.6	8.4	8.4	10.0	10.0
Financial system credit to the private sector	28.2	-43.5	12.2	13.8	13.8	11.6	11.6
Money income velocity (GDP/M3)	2.7	2.7	2.5	2.5	2.5	2.5	2.5
Interest rate on deposits (percent per annum) 4/	11.2	10.5	6.9	...	...	...	...
(In percent of GDP)							
Public sector							
Combined public sector savings 5/	2.2	-2.8	-2.5	0.2	0.2	2.9	2.9
Combined public sector primary balance (before grants) 5/6/	-6.2	-7.6	-3.3	-2.4	-2.0	-3.0	-3.0
Combined public sector overall balance (before grants) 7/	-9.5	-13.4	-10.5	-8.9	-8.4	-6.8	-6.8
Combined public sector overall balance (after grants) 6/7/	-5.0	-9.2	-5.5	-3.8	-3.2	-3.8	-3.8
Nonfinancial public sector savings	3.1	-1.5	-0.6	2.0	1.9	5.0	4.9
Nonfinancial public sector overall balance (before grants)	-8.5	-12.1	-8.6	-7.1	-6.7	-4.7	-4.7
Central bank operational results (losses -)	-0.9	-1.3	-2.0	-1.8	-1.7	-2.1	-2.1
Combined public sector debt 8/	207.9	213.9	213.7	122.1	209.6	117.5	126.2
Domestic debt	26.4	38.0	50.1	36.2	45.5	32.1	41.3
External debt	181.5	175.9	163.6	85.9	164.1	85.4	84.9
Savings and investment							
Gross domestic investment	33.4	32.1	32.1	31.9	31.5	30.6	31.0
Public	7.3	8.5	6.8	7.7	7.3	8.2	8.2
Private	26.1	23.5	25.3	24.2	24.2	22.4	22.7
National savings	10.8	9.7	10.7	12.6	13.6	15.4	15.1
Public	2.2	-2.8	-2.5	0.2	0.2	2.9	2.9
Private	8.5	12.5	13.2	12.4	13.4	12.5	12.3
External savings 9/	22.6	22.3	21.4	19.3	17.9	15.3	15.8
External sector							
External current account balance 10/	-23.6	-24.1	-19.6	-17.6	-17.9	-15.2	-15.8
(Excluding interest obligations)	-17.1	-17.9	-16.4	-14.4	-14.6	-12.2	-12.8
Trade balance (deficit -)	-25.4	-25.8	-26.0	-25.1	-25.2	-23.7	-24.3
(In percent of exports of goods and nonfactor services)							
Contractual debt service, before debt relief	45.3	38.5	45.0	37.9	38.1	30.8	31.1
Gross international reserves (in months of imports)	3.2	2.3	2.8	2.6	2.8	3.0	3.1

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

1/ As stated in the Staff Report (10/3/03), adjusted for delay in pension reform.
2/ For 2000, staff estimates using the new CPI dopted in 2001.
3/ In relation to currency in circulation at the beginning of the year.
4/ Six-month deposit rate, U.S. dollar-linked instruments, end of period.
5/ Includes central bank operational balance.
6/ For 2004, expected deterioration in the combined public sector primary balance is due to the reduction of the social security contributions (0.6 percent of GDP) resulting from the introduction of the privately managed pension funds in the second half of 2004.
7/ For 2001–03, HIPC interim debt relief from multilaterals is recorded as grants. The projections assume that the HIPC stock-of-debt operation will take place at the end of 2003.This will result in lower interest and amortization payments from 2004 onward.
8/ Nominal stock of debt relative to GDP. Data for 2002 have been revised upward, mainly reflecting inclusion of indemnity bond debt in 2002, to be issued in 2003 (subject to assembly approval), but for obligations incurred in 2002.
9/ Includes capital transfers.
10/ External current account deficit, excluding interest on debt to bilateral creditors that is eligible for debt rescheduling on terms comparable to those of the Paris Club.

Table 2. Nicaragua: Real Gross Domestic Product by Expenditure Category

	2000	2001	Prel. 2002	Projections 2003	2004
	(In millions of 1994 cordobas)				
Consumption	24,436	25,034	25,414	26,274	27,033
Private sector	20,910	21,417	22,277	23,100	23,853
Public sector	3,526	3,617	3,137	3,175	3,180
Gross domestic investment	8,291	7,933	8,018	7,501	8,080
Fixed capital formation	7,212	7,042	6,931	7,048	7,630
Private sector	5,532	5,227	5,413	5,396	5,693
Public sector	1,680	1,816	1,517	1,652	1,936
Inventory change	1,080	891	1,087	453	451
Gross domestic expenditure	32,727	32,967	33,432	33,775	35,113
Exports of goods and nonfactor services	6,775	7,362	7,116	7,152	7,616
Imports of goods and nonfactor services	12,408	12,430	12,366	12,110	12,851
GDP at market prices	**27,095**	**27,898**	**28,182**	**28,818**	**29,878**
	(Annual percentage change at constant prices)				
Consumption	3.8	2.4	1.5	3.4	2.9
Private sector	4.8	2.4	4.0	3.7	3.3
Public sector	-2.1	2.6	-13.3	1.2	0.2
Gross domestic investment	-13.1	-4.3	1.1	-6.4	7.7
Fixed capital formation	-8.0	-2.4	-1.6	1.7	8.3
Private sector	-4.8	-5.5	3.6	-0.3	5.5
Public sector	-17.3	8.1	-16.4	8.9	17.2
Gross domestic expenditure	-1.1	0.7	1.4	1.0	4.0
Exports of goods and nonfactor services	12.5	8.7	-3.3	0.5	6.5
Imports of goods and nonfactor services	-5.3	0.2	-0.5	-2.1	6.1
GDP at market prices	**4.2**	**3.0**	**1.0**	**2.3**	**3.7**
	(In percent of GDP at current prices)				
Gross domestic investment	33.4	32.1	32.1	31.5	31.0
Fixed capital formation	29.8	29.8	27.9	28.1	29.0
Private sector	22.5	21.2	21.1	20.8	20.8
Public sector	7.3	8.5	6.8	7.3	8.2
Inventory change	3.6	2.3	4.2	3.4	1.9
National savings	10.8	9.7	10.7	13.6	15.1
Private savings	8.5	12.5	13.2	13.4	12.3
Public savings	2.2	-2.8	-2.5	0.2	2.9
Memorandum items:					
Nominal GDP	50,145	53,653	57,051	61,927	68,077
Annual rate of growth	13.5	7.0	6.3	8.5	9.9
GDP deflator	8.9	3.9	5.3	6.2	6.0
CPI (avg)	7.4	7.4	4.0	5.2	5.2
CPI (eop)	6.6	4.7	4.0	6.0	5.0

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

Table 3. Nicaragua: Gross Domestic Product by Sector

	2000	2001	Prel. 2002	Projections 2003	Projections 2004
	(Annual percentage change at 1994 prices)				
Real gross domestic product	**4.2**	**3.0**	**1.0**	**2.3**	**3.7**
Taxes less subsidies on production and imports	0.7	5.3	-1.6	-0.4	4.0
Financial intermediation services	-2.1	2.4	10.1	10.0	10.0
Primary sector	**10.9**	**2.0**	**-0.2**	**1.9**	**2.8**
Agriculture	15.7	0.8	-5.1	-0.7	2.0
Livestock	7.8	5.1	4.4	4.2	3.5
Fishing	9.6	-4.9	7.0	5.7	2.6
Forestry	17.7	3.0	2.9	2.4	3.5
Mining	-14.9	5.5	5.1	4.6	5.2
Secondary sector	**4.3**	**3.9**	**-0.6**	**2.9**	**5.6**
Manufacturing	6.0	4.0	2.1	3.2	4.7
Construction	0.3	4.0	-11.8	3.5	10.8
Utilities (energy and water)	-0.2	3.0	2.5	-1.2	1.7
Services	**1.7**	**2.4**	**3.4**	**3.0**	**3.3**
Commerce	4.0	3.8	3.1	2.3	3.3
General government	-6.4	-0.1	-0.6	0.9	0.7
Transport and communications	2.0	2.2	6.2	5.5	5.5
Finance	1.5	-7.2	7.9	5.0	5.0
Real estate and housing	4.8	5.1	3.7	3.5	3.7
Other services	1.4	2.1	3.0	2.8	2.6
	(Contribution to real GDP growth)				
Real gross domestic product	**4.2**	**3.0**	**1.0**	**2.3**	**3.7**
Taxes less subsidies on production and imports	0.1	0.5	-0.2	0.0	0.4
Financial intermediation services	0.0	0.0	-0.2	-0.2	-0.2
Primary sector	**2.2**	**0.4**	**0.0**	**0.4**	**0.6**
Agriculture	1.5	0.1	-0.5	-0.1	0.2
Livestock	0.5	0.3	0.3	0.3	0.3
Fishing	0.2	-0.1	0.1	0.1	0.0
Forestry	0.2	0.0	0.0	0.0	0.0
Mining	-0.2	0.1	0.1	0.1	0.1
Secondary sector	**1.0**	**0.9**	**-0.1**	**0.7**	**1.3**
Manufacturing	1.0	0.7	0.4	0.6	0.8
Construction	0.0	0.2	-0.6	0.1	0.5
Utilities (energy and water)	0.0	0.1	0.0	0.0	0.0
Services	**0.8**	**1.1**	**1.5**	**1.4**	**1.6**
Commerce	0.7	0.7	0.6	0.4	0.6
General government	-0.5	0.0	0.0	0.1	0.0
Transport and communications	0.1	0.1	0.4	0.4	0.4
Finance	0.0	-0.2	0.2	0.1	0.1
Real estate and housing	0.3	0.3	0.2	0.2	0.3
Other services	0.1	0.1	0.2	0.2	0.2

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

Table 4. Nicaragua: Consolidated Operations of the Public Sector

(In percent of GDP; unless otherwise indicated)

	2000	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
Total current revenue	**20.0**	**19.7**	**20.3**	**22.1**	**21.9**	**21.9**	**21.9**
Current revenue of the general government	19.7	19.4	20.1	22.0	21.8	21.6	21.6
Operational surplus of public utilities	0.3	0.3	0.2	0.1	0.1	0.3	0.3
Total current expenditure	**17.8**	**22.5**	**22.8**	**21.9**	**21.7**	**19.0**	**19.0**
Consumption and transfers	14.1	16.3	15.2	15.0	15.0	14.8	14.8
Nonfinancial public sector interest payments 2/	2.8	4.9	5.7	5.1	5.1	2.2	2.1
Central bank operational results (losses +)	0.9	1.3	2.0	1.8	1.7	2.1	2.1
Combined public sector savings	**2.2**	**-2.8**	**-2.5**	**0.2**	**0.2**	**2.9**	**2.9**
Excluding interest payments	5.5	3.0	4.7	6.7	6.6	6.7	6.7
Capital expenditure and net lending (net of capital revenue)	**11.7**	**10.6**	**8.0**	**9.1**	**8.6**	**9.7**	**9.7**
Combined public sector primary balance (before grants)	**-6.2**	**-7.6**	**-3.3**	**-2.4**	**-2.0**	**-3.0**	**-3.0**
Combined public sector balance (before grants)	**-9.5**	**-13.4**	**-10.5**	**-8.9**	**-8.4**	**-6.8**	**-6.8**
Grants	**4.5**	**4.2**	**5.0**	**5.0**	**5.1**	**3.0**	**3.1**
Interim debt relief: HIPC 3/	0.0	1.1	2.0	1.9	1.9	0.0	0.0
Other 4/	4.5	3.0	3.0	3.2	3.3	3.0	3.1
Combined public sector balance (after grants) 5/	**-5.0**	**-9.2**	**-5.5**	**-3.8**	**-3.2**	**-3.8**	**-3.8**
Financing	**5.0**	**9.2**	**5.5**	**3.8**	**3.2**	**3.8**	**3.8**
Net external financing 3/	4.0	3.8	4.2	5.2	5.3	5.7	5.6
Privatization	2.9	0.9	0.4	1.0	1.0	0.4	0.4
Domestic financing, net	-1.9	4.5	0.9	-2.3	-3.0	-2.3	-2.3
Memorandum items:							
Total expenditure of the combined public sector	29.5	33.0	30.8	31.0	30.3	28.7	28.7
Total interest of the combined public sector	3.3	5.8	7.2	6.5	6.4	3.9	3.8
Total primary expenditure	26.2	27.3	23.6	24.5	23.9	24.9	24.9
Total primary current expenditure	14.5	16.7	15.6	15.4	15.4	15.2	15.2
Overall balance of the general government (after grants)	-6.6	-7.7	-3.2	-1.7	-1.3	-1.1	-1.1
Primary balance of the general government	-1.3	-2.8	2.5	3.4	3.8	1.0	1.0
Overall balance of the public enterprises (after grants)	0.0	-0.2	-0.4	-0.3	-0.3	-0.5	-0.6
Total poverty-reducing expenditure	8.9	9.0	10.2	11.0	11.0	11.2	11.4
Total HIPC debt relief 6/	0.0	2.1	6.0	5.8	5.8	5.5	5.5
From multilaterals	0.0	1.1	2.0	1.9	1.9	1.9	1.9
Interest	0.0	0.5	1.0	0.8	0.8	0.8	0.8
Principal	0.0	0.6	1.0	1.1	1.1	1.1	1.1
From bilaterals	0.0	0.9	4.0	4.0	4.0	3.6	3.6
Interest	0.0	0.4	1.6	1.5	1.5	1.7	1.7
Principal	0.0	0.5	2.4	2.5	2.5	1.9	1.9
GDP (in millions of cordobas)	50,145	53,653	57,051	61,927	61,927	68,077	68,077

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

1/ As stated in the Staff Report (10/3/03), adjusted for delay in pension reform.

2/ Includes the interest cost of bank resolution (accrual basis for 2003 and cash basis for 2004).

3/ For 2001-03, HIPC interim debt relief from multilateral creditors is recorded as grants. Debt relief from bilateral creditors is recorded as exceptional financing. The projections assume that the HIPC stock-of-debt operation will take place at end-2003. This will result in lower interest and amortization payments from 2004 onward.

4/ Mainly project-related grants from bilateral donors.

5/ For 2004, expected deterioration in the combined public sector primary balance is due to the reduction of the social security contributions (0.6 percent of GDP) resulting from the introduction of the privately managed pension funds in the second half of 2004.

6/ For 2004, HIPC debt relief is defined as the difference between debt service before HIPC completion less debt service after HIPC completion.

Table 5. Nicaragua: Summary Operations of the Central Government

(In percent of GDP)

	2000	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
Total current revenue	**18.9**	**14.2**	**15.0**	**16.7**	**16.5**	**17.1**	**17.1**
Tax revenue	18.2	13.7	14.3	16.3	16.0	16.7	16.7
Nontax revenue and current transfers	0.7	0.5	0.7	0.4	0.5	0.4	0.4
Total current expenditures	**17.1**	**17.2**	**16.8**	**15.9**	**15.9**	**12.7**	**12.7**
Consumption and transfers	13.7	12.3	11.1	10.8	10.8	10.5	10.5
Of which: wages and salaries	4.7	3.9	4.4	4.5	4.5	4.3	4.2
Interest payments 2/	3.3	4.9	5.7	5.1	5.1	2.1	2.1
Savings	**1.8**	**-3.0**	**-1.8**	**0.8**	**0.6**	**4.4**	**4.4**
Capital expenditure and net lending (net of capital revenue)	12.8	9.4	6.8	7.7	7.3	8.2	8.2
Primary balance before grants	**-7.6**	**-7.5**	**-2.9**	**-1.8**	**-1.6**	**-1.6**	**-1.6**
Overall balance before grants	**-11.0**	**-12.4**	**-8.6**	**-6.9**	**-6.7**	**-3.7**	**-3.7**
Grants	4.7	3.5	4.5	4.5	4.6	2.5	2.5
Of which: HIPC interim relief 3/	0.0	1.1	2.0	1.9	1.9	0.0	0.0
Overall balance after grants	**-6.3**	**-8.8**	**-4.1**	**-2.3**	**-2.1**	**-1.2**	**-1.2**
Financing	**6.3**	**8.8**	**4.1**	**2.3**	**2.1**	**1.2**	**1.2**
Privatization and external (net) 3/	8.5	4.3	4.1	5.8	6.0	5.4	5.4
Domestic (net)	-2.2	4.5	0.0	-3.5	-3.9	-4.2	-4.2
Memorandum items:							
Total expenditure	29.8	26.6	23.7	23.6	23.3	20.8	20.8
Total primary expenditure	26.5	21.7	17.9	18.5	18.2	18.7	18.7
Total primary current expenditure	13.7	12.3	11.1	10.8	10.8	10.5	10.5

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

1/ As stated in the Staff Report (10/3/03).

2/ Includes the interest cost of bank resolution (accrual basis for 2003 and cash basis for 2004).

3/ For 2001-03, HIPC interim debt relief from multilaterals is recorded as grants. The projections assume that the HIPC stock-of-debt operation will take place at end-2003. This will result in lower interest and amortization payments from 2004 onward.

Table 6. Nicaragua: Consolidated Operations of the Public Sector - Quarterly

(In millions of cordobas)

	2003						2004				
	Prel.		QIII		QIV		QI		Revised Program		
	QI	QII	Prog. 1/	Prel.	Prog. 1/	Rev. Prog.	Prog. 1/	Rev. Prog.	QII	QIII	QIV
Total current revenue	**3,277**	**3,121**	**3,712**	**3,580**	**3,586**	**3,603**	**3,521**	**3,727**	**3,715**	**3,718**	**3,738**
Current revenue of the general government	3,263	3,120	3,658	3,565	3,569	3,586	3,465	3,674	3,671	3,678	3,690
Operational surplus of public utilities	14	1	54	16	16	17	56	53	44	40	48
Total current expenditure	**3,351**	**3,069**	**3,546**	**3,522**	**3,613**	**3,523**	**3,132**	**3,004**	**3,239**	**3,177**	**3,524**
Consumption and transfers	2,088	2,248	2,347	2,308	2,613	2,622	2,357	2,355	2,452	2,450	2,817
Nonfinancial public sector interest payments 2/	967	619	1,010	1,015	564	571	455	326	373	408	357
Central bank operating deficit	297	201	189	199	437	330	320	323	415	319	350
Combined public sector savings	**-74**	**53**	**166**	**58**	**-27**	**80**	**389**	**723**	**476**	**541**	**215**
Excluding interest payments	1,133	817	1,311	1,208	891	903	1,100	1,309	1,200	1,213	840
Capital expenditure and net lending (net of capital revenue)	**894**	**1,390**	**1,811**	**1,370**	**1,519**	**1,651**	**1,263**	**1,337**	**1,880**	**1,776**	**1,600**
Combined public sector primary balance (before grants)	**238**	**-572**	**-500**	**-162**	**-628**	**-748**	**-163**	**-28**	**-679**	**-563**	**-760**
Combined public sector balance (before grants)	**-968**	**-1,337**	**-1,645**	**-1,312**	**-1,547**	**-1,571**	**-874**	**-614**	**-1,404**	**-1,235**	**-1,385**
Grants	**345**	**995**	**1,047**	**1,065**	**728**	**775**	**290**	**330**	**607**	**450**	**696**
Interim debt relief: HIPC 3/	102	388	467	483	192	188	0	0	0	0	0
Other	243	607	580	582	537	586	290	330	607	450	696
Combined public sector balance (after grants)	**-623**	**-342**	**-598**	**-246**	**-819**	**-797**	**-585**	**-284**	**-797**	**-785**	**-689**
Financing	**623**	**342**	**598**	**246**	**819**	**797**	**585**	**284**	**797**	**785**	**689**
Net external financing	679	1,039	700	803	789	732	1,130	1,165	1,045	1,045	590
Privatization	0	0	17	18	604	604	0	0	17	0	248
Domestic financing, net	-56	-697	-119	-575	-575	-540	-545	-881	-265	-260	-149
Of which: central bank	-398	-719	-166	-475	-432	-350	-345	-629	-434	-615	-579

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

1/ As stated in the Staff Report (10/3/03), adjusted for delay in pension reform.

2/ Includes the interest cost of bank resolution (accrual basis for 2003 and cash basis for 2004).

3/ HIPC interim debt relief from multilaterals creditors is recorded as grants.

Table 7. Nicaragua: Summary Operations of the Central Government - Quarterly

(In millions of cordobas)

	2003						2004				
	Prel.		QIII		QIV		QI		Revised Program		
	QI	QII	Prog. 1/	Prel.	Prog. 1/	Rev. Prog.	Prog. 1/	Rev. Prog.	QII	QIII	QIV
Total current revenue	**2,453**	**2,279**	**2,862**	**2,764**	**2,742**	**2,752**	**2,752**	**2,752**	**2,800**	**3,041**	**3,037**
Tax revenue	2,383	2,234	2,835	2,656	2,627	2,637	2,683	2,683	2,730	2,970	2,968
Nontax revenue and current transfers	70	45	27	107	115	115	69	69	70	71	69
Total current expenditures	**2,483**	**2,259**	**2,712**	**2,710**	**2,411**	**2,419**	**2,128**	**1,999**	**2,133**	**2,161**	**2,332**
Consumption and transfers	1,517	1,640	1,705	1,696	1,850	1,850	1,676	1,676	1,763	1,756	1,978
Of which: wages and salaries	601	659	674	697	849	826	650	650	660	669	902
Interest payments 2/	966	619	1,007	1,014	562	569	453	323	370	405	354
Savings	**-30**	**20**	**150**	**54**	**331**	**333**	**624**	**753**	**667**	**880**	**705**
Capital expenditure and net lending (net of capital revenue)	794	1,210	1,463	1,166	1,264	1,364	1,084	1,084	1,573	1,508	1,372
Primary balance before grants	**142**	**-571**	**-306**	**-98**	**-371**	**-462**	**-8**	**-8**	**-536**	**-223**	**-313**
Balance before grants	**-824**	**-1,190**	**-1,313**	**-1,112**	**-933**	**-1,030**	**-461**	**-331**	**-906**	**-628**	**-668**
Grants	301	860	954	1,019	697	697	241	241	507	355	623
Of which: HIPC interim relief 3/	102	388	467	483	192	188	0	0	0	0	0
Balance after grants	**-522**	**-330**	**-359**	**-93**	**-236**	**-333**	**-220**	**-90**	**-400**	**-273**	**-45**
Financing	**-522**	**330**	**359**	**93**	**236**	**333**	**220**	**90**	**400**	**273**	**45**
Net external financing	648	1,001	632	742	718	686	1,058	1,058	944	952	484
Privatization	0	0	17	18	604	604	0	0	17	0	248
Domestic (net)	-125	-671	-291	-667	-1,086	-957	-838	-968	-561	-679	-688

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

1/ As stated in the Staff Report (10/3/03).

2/ Includes the interest cost of bank resolution (accrual basis for 2003 and cash basis for 2004).

3/ HIPC interim debt relief from multilaterals creditors is recorded as grants.

Table 8. Nicaragua: Summary Accounts of the Central Bank

(Flows in millions of cordobas; unless otherwise stated)

	2000	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog.1/	2004 Rev. Prog.
Exchange rate (cordobas/US$)	13	13	14	15	15	...	...
Net international reserves	**-374**	**-2,290**	**692**	**-227**	**88**	**318**	**321**
(In millions of US$)	-29	-170	49	-15	6	20	20
Net domestic assets	**393**	**2,485**	**-555**	**430**	**114**	**-90**	**-94**
Net credit to nonfinancial Public sector (NFPS) 2/	-627	6,690	-1,329	-1,974	-2,371	-2,189	-2,257
Operational losses	461	680	1,115	1,123	1,028	1,418	1,407
Net credit to the financial system 3/	1,656	-947	-698	-71	-72	-296	-296
CENIS, BOMEX, and TELs 4/	-1,274	-4,130	407	1,524	1,704	657	734
Foreign liabilities (Medium- and long-term)	161	174	143	262	252	247	246
Other 3/	16	18	-193	-434	-426	72	72
Currency	**19**	**195**	**136**	**202**	**202**	**227**	**227**
Memorandum items:							
Currency (stock)	1,754	1,949	2,086	2,288	2,288	2,515	2,515
Currency (annual change; in percent)	1	11	7	10	10	10	10
Strengthening of BCN reserve position (In millions of US$) 5/	-163	-470	82	55	76	61	66
Net repayment of BCN domestic debt (+)	-134	-300	33	70	70	41	46
Increase in NIR (+)	-29	-170	49	-15	6	20	20
Foreign currency deposits (in percent of banking system deposits) 6/	70	71	72	...	71	...	72
Foreign currency loans (in percent of total loans) 6/	83	84	83	...	83	...	84

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

1/ As stated in the Staff Report (10/3/03).
2/ Includes bonds of C$3,853 millions issued to recapitalize weak banks in 2001.
3/ From 2002 onward, asset recovery of closed banks is included in "other."
4/ *Certificados Negociables de Inversion* (CENIS), *Bonos en Moneda Extranjera* (BOMEX), and *Titulos Especiales de Liquidez (TELs).*
5/ Defined as the sum of the net repayment of BCN domestic debt and the change in NIR.
6/ Official data. Excludes other deposits/loans with implicit dollar indexation.

Table 9. Nicaragua: Summary Accounts of the Central Bank-Quarterly

(Flows in millions of cordobas; unless otherwise stated)

	2003						2004				
	Prel.		QIII		QIV		QI		Revised Program		
	QI	QII	Prog. 1/	Prel.	Prog. 1/	Rev. Prog.	Prog. 1/	Rev. Prog.	QII	QIII	QIV
Net international reserves	**-113**	**855**	**27**	**-196**	**-604**	**-440**	**0**	**-1**	**78**	**-62**	**305**
(In millions of US$)	-7	57	2	-13	-40	-29	0	0	5	-4	19
Net domestic assets	**-67**	**-881**	**-43**	**221**	**1,036**	**822**	**-202**	**-202**	**-106**	**35**	**179**
Net credit to nonfinancial public sector 2/	-345	-733	-673	-822	-432	-490	-345	-629	-434	-615	-580
Net credit to the financial system 3/	161	-671	-83	228	233	210	-221	-221	-126	3	49
CENIS, BOMEX, and TELs 4/	-193	355	584	874	738	669	0	286	1	99	348
Foreign liabilities (medium- and long-term)	53	22	164	154	23	23	14	15	18	215	0
Other 3/	257	147	-35	-214	474	411	349	348	435	333	362
Currency	**-180**	**-25**	**-16**	**25**	**432**	**383**	**-202**	**-202**	**-28**	**-27**	**485**
Memorandum items:											
Currency (stock)	1,906	1,881	1,791	1,906	2,288	2,288	2,086	2,086	2,058	2,031	2,516
Currency (annual change; in percent)	-3	7	4	11	10	10	10	9	9	7	10
Strengthening of BCN reserve position											
(In millions of US$) 5/	-23	75	47	19	9	6	0	18	5	2	41
Net repayment of BCN domestic debt (+)	-15	18	46	32	49	35	0	18	0	6	22
Increase in NIR (+)	-7	57	2	-13	-40	-29	0	0	5	-4	19

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

1/ As stated in the Staff Report (10/3/03).
2/ Includes bonds issued to recapitalize weak banks.
3/ From 2002 onward, asset recovery of closed banks is included in "other."
4/ Certificados Negociables de Inversion (CENIS), Bonos en Moneda Extranjera (BOMEX), and Titulos Especiales de Liquidez (TELs).
5/ Defined as the sum of the net repayment of BCN domestic debt and the change in NIR.

Table 10. Nicaragua: Operations of the Central Bank and the Financial System

(Stocks in millions of cordobas)

	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
I. Central Bank						
Net international reserves 2/	**213**	**1,000**	**745**	**745**	**1,104**	**1,104**
(In millions of U.S. dollars)	16	64	49	49	69	69
Net domestic assets	**1,736**	**1,086**	**1,543**	**1,543**	**1,412**	**1,412**
Net credit to NFPS	34,467	33,725	32,060	31,663	30,065	29,578
Net credit to the financial system	207	-675	-694	-695	-950	-951
CENIs, BOMEX and TELs	-7,456	-8,654	-7,646	-7,466	-7,410	-7,142
Medium- and long-term foreign liabilities	-23,806	-25,477	-26,735	-26,745	-27,959	-27,970
Other	-1,676	2,167	4,558	4,785	7,665	7,897
Currency	**1,949**	**2,086**	**2,288**	**2,288**	**2,516**	**2,516**
II. Consolidated Financial System						
Net international reserves	**3,014**	**4,462**	**5,279**	**5,542**	**6,960**	**7,745**
(In millions of U.S. dollars)	224	313	349	367	437	486
Net domestic assets	**16,366**	**17,365**	**18,305**	**18,043**	**18,574**	**17,788**
Net credit to nonfinancial public sector	30,445	33,072	31,691	31,984	29,507	29,418
Credit to the private sector	13,576	10,830	12,986	12,986	15,140	15,140
Medium- and long-term foreign liabilities	-24,475	-26,624	-27,897	-27,908	-29,150	-29,161
Other net assets	-3,179	86	1,526	980	3,077	2,391
Liabilities to the private sector	**19,380**	**21,826**	**23,585**	**23,585**	**25,533**	**25,533**

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

1/ As stated in the Staff Report (10/3/03).

2/ For 2003, program figure is repeated in the projection column, to serve as a base for the 2004 revised program number.

Table 11. Nicaragua. Balance of Payments
(In millions of U.S. dollars; unless otherwise indicated)

	2000	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
Current account	**-931**	**-962**	**-785**	**-723**	**-732**	**-652**	**-676**
Excluding interest obligations	-674	-715	-656	-591	-600	-521	-549
Trade balance	-1003	-1028	-1040	-1028	-1033	-1017	-1038
Exports, f.o.b.	645	593	596	596	591	651	631
Imports, f.o.b.	-1,648	-1,620	-1,636	-1,624	-1,624	-1,669	-1,669
Nonfactor services (net)	-32	-26	-17	-1	-6	28	18
Receipts	311	328	322	345	345	383	383
Payments	-343	-354	-338	-347	-351	-354	-365
Official interest obligations 2/	-257	-247	-130	-132	-132	-131	-127
Other current transactions (net)	361	339	401	438	438	468	472
Factor services receipts	31	15	8	8	8	13	11
Noninterest factor services payments	-69	-77	-71	-77	-77	-86	-87
Private transfers	400	402	464	507	507	541	547
Capital account	**627**	**550**	**623**	**535**	**566**	**439**	**465**
Official (net)	346	362	245	346	356	340	317
Official transfers	308	342	321	323	330	250	230
Public sector consolidated	176	121	120	127	134	130	130
Other	132	173	130	120	120	120	100
HIPC interim relief from multilaterals	0	49	71	76	76	76	0
Disbursements 3/	220	217	203	240	243	261	258
Amortization 2/ 3/	-171	-177	-278	-217	-217	-172	-172
Other (net) 4/	-11	-20	0	0	0	0	0
Other Capital (private)	282	188	378	189	210	100	148
Foreign direct investment	265	132	218	192	200	157	200
Commercial banks	17	-85	-7	-65	-47	-54	-101
Commercial credits	0	70	34	0	0	0	0
CENIs	0	52	17	0	-2	0	-1
Private capital transfers	0	44	59	48	48	40	48
Net other private capital flows	0	0	81	14	11	-43	2
Errors and omissions	0	-25	-24	0	0	0	0
Overall balance	**-304**	**-412**	**-162**	**-188**	**-166**	**-212**	**-211**
Change in net international reserves (- increase)	21	170	-49	15	-7	-20	-20
Of which: IMF (net)	64	-5	4	20	20	44	44
Net change in arrears (decrease -) 5/	-97	-285	-574	-1794	-1794	0	0
Of which: overdue payments 6/	0	0	0	5	5	0	0
Exceptional financing	211	526	785	1966	1966	232	231
Paris Club rescheduling	71	31	228	20	20	15	15
Non-Paris Club rescheduling 5/	98	495	557	1938	1938	209	209
Of which: HIPC interim relief	0	58	168	166	166	0	231
Additional relief from Paris Club creditors	0	0	0	7	7	4	4
Memorandum items:							
Current account (in percent of GDP)	-23.6	-24.1	-19.6	-17.6	-17.9	-15.2	-15.8
Excluding interest obligations (in percent of GDP)	-17.1	-17.9	-16.4	-14.4	-14.6	-12.2	-12.8
Gross reserves (in millions of U.S. dollars)	496.7	382.8	454.1	446.7	446.7	524.1	524.3
Gross reserves (in months of imports)	3.2	2.3	2.8	2.6	2.8	3.0	3.1
Net international reserves (in millions of U.S. dollars)	186.7	15.8	64.3	49.3	49.3	69.2	69.2
Debt service ratio 7/	45.3	38.5	45.0	37.9	38.1	30.8	31.1
Debt service ratio, actual payments 7/	19.6	21.8	17.2	12.3	12.4	9.2	7.4
Gross official grants and loans (in percent of GDP)	14.0	12.6	13.3	14.4	14.7	13.3	12.8
Net official grants and loans (in percent of GDP)	10.7	10.7	10.4	11.7	11.9	10.1	10.3
GDP (millions of US$)	3,953	3,991	4,003	4,100	4,099	4,284	4,272

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

1/ As stated in the Staff Report (10/3/03).
2/ Interest and amortization shown before all debt relief.
3/ Medium- and long-term.
4/ Short-term debt, and private debt due to official creditors. As of 2002, short-term debt is included in total interest and amortization payments.
5/ In 2002, this represents arrears cleared under bilateral agreements at terms comparable to those offered by the Paris Club. Clearance in 2003 is associated with completion point, and debt remaining to other non-Paris Club creditors, with whom agreements have not yet been finalized.
6/ Not considered arrears for program purposes.
7/ In percent of exports of goods and nonfactor services.

Table 12. Nicaragua: Public Sector Domestic Debt (stocks in net present value)

(In millions of U.S. dollars)

	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
BCN liabilities	**670**	**653**	**531**	**517**	**457**	**447**
Certificados Negociables de Inversiones (CENIs)	610	595	531	517	457	447
Auctioned	187	185	236	183	237	172
Coffee-related	10	9	0	0	0	0
Bank resolution (from Interbank onward)	413	402	295	334	220	275
Bonos en Moneda Extranjera (BOMEX)	21	10	0	0	0	0
Titulos Especiales de Liquidez (TELs)	39	48	0	0	0	0
MHCP liabilities	**809**	**699**	**868**	**744**	**847**	**769**
Indemnization bonds (BPIs) 2/	763	538	850	574	839	596
Recognition of debt incurred in 2002 (BPIs) 3/	0	125	0	141	0	158
New issues	0	0	0	0	0	0
Other paper	46	36	18	29	8	15
Combined public sector domestic debt	**1,479**	**1,352**	**1,399**	**1,261**	**1,304**	**1,216**
In percent of GDP	37.1	33.8	34.1	30.8	30.4	28.5
Memorandum items:						
Debt reduction on accrual basis (+) (flows)	**-533**	**-126**	**88**	**-91**	**-95**	**-46**
Central bank	-408	-16	90	-136	-74	-71
Central government	-125	-110	-2.0	45.0	-21	25
Net repayment of BCN Domestic Debt (+) (flows)	...	**33**	**108**	**108**	**77**	**86.3**
Central bank	...	33	70	70	41	46.1
Central government	...	0	38	38	36	40.2

Sources: Central Bank of Nicaragua; and Ministry of Finance.

1/ As stated in the Staff Report (10/3/03); MHCP liabilities were adjusted by recognition of indemnity bonds debt and exclusion of INSS.
2/ Increase in 2002 reflects previously awarded court claims on properties confiscated during the Sandinista government.
3/ Data for 2002 have been revised upward, mainly reflecting inclusion of indemnity bond debt in 2002, to be issued in 2003 (subject to assembly approval), but for obligations incurred in 2002.

Table 13. Nicaragua: Public Sector External Debt and Debt Service

	2000	2001	Prel. 2002	2003 1/ Prog. 2/	2003 1/ Proj.	2004 Prog. 2/	2004 Rev. Prog.
(In millions of U.S. dollars; end of period)							
Total debt	7,242	7,040	6,705	3,520	7,009	3,656	3,627
Bilaterals	4,124	3,740	3,177	1,117	3,216	1,098	826
Multilaterals	2,260	2,343	2,574	2,397	2,731	2,553	2,474
Commercial banks 3/	817	909	954	0	1,056	0	282
Other	41	48	0	5	5	5	0
(In percent of GDP)							
Total debt	181	176	164	86	164	85	85
Bilaterals	103	93	78	27	75	26	19
Multilaterals	57	59	63	58	64	60	56
Commercial banks	20	23	23	0	25	0	6
Other	1	1	0	0	0	0	0
(In millions of U.S. dollars)							
Total debt service obligations	422	429	413	357	357	319	316
Principal	164	182	284	225	225	188	188
Interest	257	248	130	132	132	131	127
Debt service paid	188	257	158	116	116	95	93
Principal	111	127	120	72	72	49	39
Interest	77	130	37	44	44	46	54
Debt service not paid	234	173	255	241	241	224	222
Principal	53	55	163	153	153	139	149
Interest	180	118	92	88	88	85	73
(In percent of GDP)							
Total debt service obligations	11	11	10	9	8	7	7
Principal	4	5	7	5	5	4	4
Interest	6	6	3	3	3	3	3
Debt service paid	5	6	4	3	3	2	2
Principal	3	3	3	2	2	1	1
Interest	2	3	1	1	1	1	1
Debt service not paid	6	4	6	6	6	5	5
Principal	1	1	4	4	4	3	3
Interest	5	3	2	2	2	2	2
(In percent of exports of goods and nonfactor services)							
Total debt service obligations	46	47	41	38	32	31	26
Principal	18	20	28	24	20	18	15
Interest	28	27	13	14	12	13	10
Debt service paid	20	28	16	12	10	9	8
Principal	12	14	12	8	6	5	3
Interest	8	14	4	5	4	4	4
Debt service not paid	25	19	25	26	22	22	18
Principal	6	6	16	16	14	13	12
Interest	20	13	9	9	8	8	6

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

1/ Stocks at end-2003 reflect an evisaged stock operation at completion point. Central Bank estimates of the commercial debt stock should the envisaged stock operation not occur are for US$205.6 million 2003 and US$209 million in 2004.

2/ As stated in the Staff Report (10/3/03).

3/ Stocks now include commercial debt owed to creditors not participating in 1995 debt buyback operation. Completion point envisages treatment of these debts on terms analogous to those offered by the Paris Club.

Table 14. Nicaragua: Revised Phasing of IMF Disbursements and Reviews

Date of Disbursement	Amount (In millions of SDRS)	
First year program		
December 2002	6.965	Executive Board approval of PRGF arrangement and first-year program.
June 2003	13.930	Completion of first and second reviews; observance of end-December and end-March performance criteria.
October 2003	6.965	Completion of third review, observance of end-June 2003 performance criteria.
January 2004	13.930	Completion of fourth review and observance of end-September 2003 performance criteria and approval of second-year program.
Second year program		
April 2004	6.965	Completion of fifth review and observance of end-December 2003 performance criteria.
July 2004	6.965	Completion of sixth review and observance of end-March 2004 performance criteria.
October 2004	6.965	Completion of seventh review and observance of end-June 2004 performance criteria and approval of the third-year program.
January 2005	6.965	Completion of eighth review and observance of end-September 2004 performance criteria.
Third year program		
April 2005	13.930	Completion of ninth review and observance of end-December 2004 performance criteria.
October 2005	13.920	Completion of tenth review and observance of end-June 2005 performance criteria.
Total	**97.500**	

Sources: FIN and WHD.

Table 15. Nicaragua: Indicators of Financial Obligations to the Fund (as of November 15, 2003)

(In millions of SDRs; unless otherwise indicated)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Outstanding Fund credit (end of period)	118.6	128.3	143.5	173.4	182.3	159.2	136.1	112.0	90.4	71.0	51.5	32.0
Poverty Reduction and Growth Facility (PRGF) disbursements		7.0	20.9	41.8	27.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total debt service to the Fund	5.1	2.5	6.7	13.1	20.2	24.3	24.2	25.2	22.5	20.2	20.2	20.1
Principal	4.0	2.0	5.7	11.9	19.0	23.1	23.1	24.2	21.6	19.4	19.5	19.5
Charges and interest	1.1	0.5	1.0	1.2	1.2	1.2	1.1	1.0	0.9	0.8	0.7	0.6
Total debt service to the Fund after HIPC assistance	5.1	0.6	3.6	4.5	2.3	9.4	9.9	12.2	16.2	20.2	20.2	20.1
Outstanding Fund credit (end of period) In percent of quota	91.2	98.7	110.4	133.4	140.2	122.5	104.7	86.2	69.5	54.6	39.6	24.6
Debt service to the Fund (in percent of total debt service due after rescheduling) 1/	4.2	0.5	4.1	6.9	3.0	10.2	10.1	12.9	18.5	20.4	18.9	16.7
Total debt-service ratio (after rescheduling) 1/	16.3	17.2	12.4	9.0	10.0	11.4	11.3	10.3	8.8	9.4	9.5	10.1
Of which: IMF	0.7	0.1	0.5	0.6	0.3	1.2	1.1	1.3	1.6	1.9	1.8	1.7
Repayment to IMF/reserves (in percent)	1.7	0.2	1.0	1.1	0.5	2.0	2.0	2.3	2.9	3.5	3.3	3.2

Source: IMF, Finance Department.

1/ IMF service net of delivery of HIPC assistance based on indicative drawdown schedule specified in the decision point document (Table 11 of the Staff Report (10/3/03)) in all cases.

Table 16. External Financing Requirements and Sources

(In millions of U.S. dollars)

	2001	Prel. 2002	2003 Prog. 1/	2003 Proj.	2004 Prog. 1/	2004 Rev. Prog.
Gross financing requirements	**-967**	**-1121**	**-953**	**-984**	**-902**	**-926**
External current account deficit (excluding official transfers)	-962	-785	-723	-732	-652	-676
Debt amortization	-177	-278	-217	-217	-172	-172
Gross reserves accumulation	177	-52	-5	-27	-64	-64
IMF repurchases and repayments	-5	-5	-8	-8	-14	-14
Gross financing sources	**967**	**1121**	**953**	**984**	**902**	**926**
Foreign direct investment (net)	132	218	192	200	157	200
Debt financing from private creditors	81	183	-3	11	-57	-52
Trade pre-financing	70	34	0	0	0	0
Commercial banks' reserves	-85	-7	-65	-47	-54	-101
Other private capital (including CENIS)	96	157	62	58	-3	49
Official transfers	342	321	323	330	250	230
Disbursements (medium- and long-term loans)	217	203	240	243	261	258
Of which: balance of payments financing	35	35	59	60	75	75
Of which: expected new commitments	...	15	30	30	50	50
IMF disbursements	0	9	28	28	59	59
Net change in arrears	-285	-574	-1794	-1794	0	0
Other flows 2/	-45	-24	0	0	0	0
Exceptional financing 3/	526	785	1966	1966	232	231

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

1/ As stated in the Staff Report (10/3/03).
2/ Includes all other net financial flows, and errors and omissions.
3/ Includes only traditional debt rescheduling.

Table 17. Nicaragua: Medium-Term Macroeconomic Framework

			Prel.	Revised Prog. 1/		Staff Projections			
	2000	2001	2002	2003 1/	2004	2005	2006	2007	2008
	(Annual percentage change)								
GDP at constant prices	4.2	3.0	1.0	2.3	3.7	3.8	4.2	4.6	4.8
Consumer prices (end of period) 1/	6.6	4.7	4.0	6.0	5.0	4.5	4.0	3.0	2.0
Consumer prices (period average) 1/	7.4	7.4	4.0	5.2	5.2	4.7	4.2	3.5	2.5
GDP deflator	8.9	3.9	5.3	6.2	6.0	4.5	3.9	3.1	2.2
Exports, f.o.b.	18.3	-8.1	0.7	-0.9	6.8	6.8	6.3	6.2	6.1
Export volume	15.1	7.3	1.9	-2.2	3.6	2.1	4.0	4.4	4.4
Imports, f.o.b.	-3.0	-1.7	1.0	-0.8	2.8	4.5	4.4	4.2	4.7
Import volume	-9.7	2.5	-1.2	-4.3	3.2	4.9	4.6	3.7	3.8
Terms of trade (deterioration -)	-4.0	-11.2	-3.2	-2.5	3.7	5.1	2.4	1.3	0.7
	(In percent of three-year average of exports of goods and nonfactor services)								
Debt service ratio, after HIPC relief	21.5	22.4	16.9	12.4	9.5	10.6	12.0	12.0	10.9
	(In percent of GDP)								
External current account balance	-23.6	-24.1	-19.6	-17.9	-15.8	-13.1	-11.9	-11.0	-10.2
External current account, excluding interest obligations	-17.1	-17.9	-16.3	-14.6	-12.8	-12.0	-10.9	-10.3	-9.5
Total current revenue	20.0	19.7	20.3	21.9	21.9	21.5	21.6	21.9	22.1
Total current expenditure	17.8	22.5	22.8	21.7	19.0	18.0	18.6	17.6	17.1
Combined public sector savings	2.2	-2.8	-2.5	0.2	2.9	3.5	3.0	4.3	5.0
Combined public sector primary balance (before grants)	-6.2	-7.6	-3.3	-2.0	-3.0	-3.1	-3.5	-2.2	-1.7
Combined public sector balance before grants	-9.5	-13.4	-10.5	-8.4	-6.8	-6.3	-6.6	-5.4	-4.7
Combined public sector balance (after grants)	-5.0	-9.2	-5.5	-3.2	-3.8	-3.0	-3.2	-1.8	-0.9
Combined public sector debt 2/	207.9	213.9	213.7	209.6	126.2	123.7	119.5	114.1	108.3
Domestic debt	26.4	38.0	50.1	45.5	41.3	38.7	35.9	32.4	28.6
External debt	181.5	175.9	163.6	164.1	84.9	85.0	83.6	81.7	79.7
Private sector S-I gap	-17.5	-11.0	-12.1	-10.8	-10.5	-9.9	-8.2	-8.5	-8.5
Investment	33.4	32.1	32.1	31.5	31.0	30.8	29.9	30.9	30.3
Private sector	26.1	23.5	25.3	24.2	22.7	22.6	21.7	22.6	22.1
Public sector	7.3	8.5	6.8	7.3	8.2	8.2	8.2	8.2	8.2
National savings	10.8	9.7	10.7	13.6	15.1	16.1	16.5	18.4	18.6
Private sector	8.5	12.5	13.2	13.4	12.3	12.7	13.5	14.1	13.6
Public sector	2.2	-2.8	-2.5	0.2	2.9	3.5	3.0	4.3	5.0
External savings 3/	22.6	22.3	21.4	17.9	15.8	14.7	13.4	12.5	11.7
Memorandum items:									
Nominal GDP (in millions of cordobas)	50,145	53,653	57,051	61,927	68,077	74,101	79,804	86,095	92,251
GDP (millions of US$)	3,953	3,991	4,003	4,099	4,272	4,433	4,637	4,877	5,145
Gross international reserves to M3	22.0	21.2	24.9	24.2	27.0	28.9	29.3	29.5	29.8
Gross international reserves (in millions of U.S. dollars)	497	383	454	447	524	583	618	654	697
Gross reserves (in months of imports)	3.2	2.3	2.8	2.8	3.1	3.4	3.5	3.5	3.6
Debt service ratio 4/	45.3	38.5	45.0	38.1	31.1	31.7	30.9	28.5	25.2
Debt service ratio, actual payments 4/	19.6	21.8	17.2	12.4	7.4	7.5	9.1	9.6	9.6
Gross official grants and loans (in percent of GDP)	14.0	12.6	13.3	14.7	14.7	13.0	11.0	10.3	9.9
Net official grants and loans (in percent of GDP)	10.7	10.7	10.0	12.2	12.2	10.9	9.6	8.9	8.6

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

1/ Assumes that private pension funds initiate operations in July 2004.

2/ Nominal stock of debt relative to GDP. Data for 2002 have been revised upward, mainly reflecting inclusion of indemnity bond debt in 2002, to be issued in 2003 (subject to assembly approval), but for obligations incurred in 2002.

3/ Includes capital transfers.

4/ In percent of exports of goods and nonfactor services.

Table 18: Nicaragua. Status of Poverty Reduction and Structural Measures for Reaching the Enhanced HIPC Initiative Floating Completion Point

	Monitoring Institution and Compliance	
1. **Preparation of a fully participatory PRSP and its satisfactory implementation for at least one year** as evidenced by the joint staff assessment of the country's annual progress report presented to the Boards of the IMF and IDA. The full PRSP was submitted to the IMF Board in September 2001. A report of the second year of its implementation was presented in November 2003.	WB/IMF	Done
2. **The use of budgetary savings resulting from the interim relief under the HIPC Initiative** would be in accordance with the proposals set out in Appendix III (www.imf.org), and would be reported in the PRSP process. A reliable tracking mechanism of poverty reducing expenditures was approved and is operating.	WB	Done
3. **Maintenance of a stable macroeconomic framework, and satisfactory performance under a program supported by a PRGF arrangement.** The Board approved the first and second reviews under the three-year PRGF arrangement in June 2003, and the third review in October 2003. Fourth review is presented for Board approval.	IMF	Done
4. **Implementation of reforms to promote human capital development and social protection.** Key reforms are:		
a. **Approval of a satisfactory school autonomy law** to strengthen the legal foundations for the envisaged sector reform, which aims at encouraging, *inter alia*, greater parental participation in education. A law considered satisfactory by the World Bank was approved in February 2002. Implementing regulations in place since 2002.	WB	Done
b. **Approval of a satisfactory general health law and adoption of corresponding implementing regulations** to strengthen the health ministry's regulatory and normative roles, and establish a solid legal framework for the sector's modernization program, granting more autonomy to hospitals and local health systems. A law deemed satisfactory by the World Bank became effective in November 2002. Implementing regulations were approved and published in January 2003. Law is being implemented.	WB	Done
c. **Adoption of an action plan to introduce an effective social protection program, based on the results of a pilot program started in 2000.** A pilot program was concluded in 2002 and the second phase of the social protection net program is under implementation.	IDB	Done
5. **Implementation of governance strengthening measures, which encompass:**		
a. **Enactment and advance in implementation of a satisfactory civil service law** to, *inter alia*, reduce political interference in hiring/firing decisions affecting civil servants. Law was approved in November 2003 and significant progress has been made in implementing the law.	WB	Done
b. **Introduction of a satisfactory system of management and inspection of public sector procurement.** Implementation of the program agreed with the IDB started in October 2002. Satisfactory system in place.	IDB	Done
c. **Satisfactory progress in implementing the plan to strengthen and improve the efficiency of the comptroller's office.** Program agreed with the IDB started in December 2002. Satisfactory implementation.	IDB	Done
d. **Approval of the law on penal procedures and initiation of training programs and technical preparations for its implementation.** A law on penal procedures (Law 411) was published in December 2001. Implementation of the law started at end-2002. Training programs and technical preparations are advanced.	IDB	Done
e. **Approval of the law on public prosecutors and initiation of training programs and technical preparations for its implementation.** A law on public prosecutors (Law 342) was published in October 2000. Implementing regulations approved. Training programs and technical preparations are advanced.	IDB	Done
6. **Implementation of remaining actions needed to introduce a satisfactory pension system of funded private sector managed, and individual accounts.** This includes especially the passage of a law to create a supervisory authority for pension funds, the staffing of this supervisory authority, and the restructuring of the social security institute. A new Pension Law had been approved in 1999 and the Pension Superintendency Law was approved in 2001. The pension superintendency has been staffed and a new superintendent was appointed in early June 2003. Measures to restructure INSS have been implemented.	WB/IDB/ IMF	Done
7. **Divestment of:**		
a. **ENITEL:** 40 percent of ENITEL's shares were divested and a management contract was awarded in August 2001. Workers were given 1 percent of the shares, and offered an additional 10 percent for purchase. The government received a viable offer for the remaining shares of ENITEL in December 2003 and expects to complete the sale in January 2004.	WB	Pending (Expected to be done by mid-January 2004)
b. **All remaining electricity-generating units of ENEL:** The authorities succeeded in divesting two electricity generating plants (Geosa, Gemosa), but two others remain in public hands (Hidrogesa, Gecsa). Investors have shown little interest in Gecsa, which is obsolete, and the authorities have determined, in close consultation with the IDB, that privatization of Hidrogesa is not advisable at this time, since it could result in an excessive concentration of market power in one firm. Power generating capacity has been rising as a result of increased private sector participation. To improve overall efficiency in the power sector, the authorities will begin implementing a plan agreed with IDA and the IDB to strengthen the sector's policy, legal, and regulatory framework.	IDB	Not done (Waiver recommended.)

Table 19. Nicaragua: Comparative Social Indicators

	Nicaragua	Costa Rica	El Salvador	Guatemala	Honduras	Average for Latin America and the Caribbean
Rank in 2002 UNDP Human Development Index (out of 173 countries)	118	43	104	120	116	...
GNI per capita, (current US$)	731	4,060	2,040	1,680	900	3,580
Life expectancy at birth (years) (2000)	68.9	77.5	70.2	65.2	66.0	70.0
Under-5 mortality (per 1,000 live births) (2000)	40.8	13.4	35.4	38.8	43.8	32.0
People not expected to survive to age 40 (in percent of population) (1999)	11.5	4.0	10.9	15.6	16.0	9.7
Undernourished people (as percent of total population)	29	5	12	22	21	12
Population without access to safe water (1999)	21	2	26	8	10	22
Per capita health exp. in PPP, U.S. dollars (1998)	54	257	143	78	74	...
Physicians per 100,000 people (1990-99)	86	141	107	93	83	...
Adult illiteracy (2000)	33.5	4.4	21.3	31.4	25.4	11.7
Primary school net enrollment (1997) (percent of relevant age of the population)	78.6	91.8	89.1	73.8	87.5	93.3
Secondary school net enrollment (1997) (percent of relevant age of the population)	50.5	55.8	36.4	34.9	36.0	65.3
Income share of:						
the richest 20 percent of the population	63.6	51.0	56.4	60.6	59.4	...
the poorest 20 percent of the population	2.3	4.4	3.3	3.8	2.2	...
Gini Index (1997-98)	60.3	45.9	52.2	55.8	56.3	...
Percent of population below official poverty line 1/	47.9	19.0	50.3	54.3	63.1	50.7

Sources: World Bank World Development Indicators 2002; Szekely, Lustig, Cumpa, and Mejia (2000); and UNDP Human Development Report 2001 and 2002.

1/ Not comparable across countries due to methodological issues. For Guatemala, Honduras, and Nicaragua, the information refers to the Poverty Reduction Strategy Paper.

Table 20. Nicaragua: Comparative Governance Indicators 1/

	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
Nicaragua						
2001/02	52.0	47.6	17.5	39.7	32.0	39.7
1997/98	57.6	37.7	29.7	37.0	25.5	18.2
Costa Rica						
2001/02	84.8	86.5	66.5	72.7	72.2	79.4
1997/98	87.8	81.2	73.5	90.9	71.5	76.6
El Salvador						
2001/02	51.5	56.8	35.6	56.2	39.7	36.6
1997/98	49.4	48.1	44.5	99.4	29.7	41.6
Guatemala						
2001/02	35.4	32.4	32	52.1	21.6	30.9
1997/98	33.1	22.1	45.8	66.7	10.3	18.8
Honduras						
2001/02	46.0	38.4	27.3	41.8	23.7	27.3
1997/98	51.2	36.4	36.1	43.6	17.0	11.0
Average for Central America						
2001/02	53.9	52.3	35.8	52.5	37.8	42.8
1997/98	55.8	45.1	45.9	67.5	30.8	33.2
Average for Latin America						
2001/02	54.5	43.3	40.5	52.8	40.7	42.4
1997/98	59.1	45.0	48.3	66.4	43.9	46.7

Source: Kaufmann, Kraay, Zoido-Lobaton (2002), http://info.worldbank.org/governance/kkz/.

1/ Percentile rank with a higher number denoting better governance.

Nicaragua—Fund Relations
(As of October 31, 2003)

VI. Membership Status: Joined: 03/14/1946; Article VIII since 7/30/1964.

VII. General Resources Account:

	SDR Million	Percent of Quota
Quota	130.00	100.00
Fund Holdings of Currency	130.01	100.01

VIII. SDR Department:

	SDR Million	Percent of Allocation
Net cumulative allocation	19.48	100.00
Holdings	0.13	0.67

IX. Outstanding Purchases and Loans:

	SDR Million	Percent of Quota
ESAF/PRGF arrangements	145.50	111.92

X. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	12/13/2002	12/12/2005	97.50	20.90
ESAF/PRGF	03/18/1998	03/17/2002	148.96	115.32
ESAF	06/24/1994	06/23/1997	120.12	20.02

XI. Projected Obligations to Fund (with Board-approved HIPC Assistance):

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

	Overdue	Forthcoming				
	12/31/2002	2003	2004	2005	2006	2007
Principal	0.0	2.00	11.85	19.03	23.06	23.06
Charges/Interest	0.0	0.42	1.00	0.91	0.81	0.69
Total	0.0	2.43	12.85	19.94	23.88	23.76

XII. Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ million)[1]	3,267.00
Of which: IMF assistance (US$ million)	81.47
(SDR equivalent in millions)	62.98
Completion point date	Floating
Disbursement of IMF assistance (SDR million)	
Assistance disbursed to the member	2.55
Interim assistance	2.55
Completion point balance	0.0
Additional disbursement of interest income[2]	0.0

XIII. Safeguards Assessments:

The updated assessment of the BCN, which was completed on August 29, 2003, found that it continues to maintain strong safeguards and has taken steps to implement most of the recommendations made in the 2001 safeguards assessment. However, staff noted that some vulnerabilities remain in the BCN's external audit mechanism and financial reporting practices. In order to mitigate these vulnerabilities, staff recommended that the BCN (i) adopt International Accounting Standards (IAS) beginning with the 2004 financial statements; (ii) disclose the differences between IAS and the BCN accounting practices in its 2002 and 2003 financial statements; and (iii) adopt a policy to appoint external auditors for three-year terms through an open competitive bidding process. A task force will be established by the BCN to ensure adequate training for the transition to full IAS.

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[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.

[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.

XIV. 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. In November 1999, the monthly crawl was reduced from an annual rate of 9 percent to 6 percent.

As of October 30, 2003, the exchange rate in the official market was C$15.40 per U.S. dollar.

XV. Article IV Consultation:

The last consultation was completed by the Executive Board on November 19, 2002 (IMF Country Report No. 03/24). It is expected that the next Article IV consultation with Nicaragua will be held on a standard 24–month cycle subject to the provisions of the decision on consultation cycles approved by the Board on July 15, 2002.

XVI. Technical Assistance:

Dept.	Purpose	Time of Delivery
FAD	Tax administration	October 2003
FAD	Tax reform	March 2003
FAD	ROSC fiscal transparency module	November 2001
FAD	Mission to review energy taxation and advise on the system of exemptions, exonerations, tax holidays, and other incentives with regard to the major indirect taxes major indirect taxes	January 2000
MFD	Banking legislation and banking supervision	September 2003
MFD	Banking supervision	October 2002
MFD	Banking restructuring	November 2001
MFD	Assessing CBN's debt sustainability and streamline its open market operations, with special focus on providing liquidity to CBN's securities and increase their marketability.	July 2001
MFD	Workshop on payments system.	January 27–29, 1999
MFD	Consultancy on introducing an exchange rate band.	October 1999
OIA	Mission to assess the management, organizational structure, and internal control systems and procedures of the Superintendency of Banks and Other Financial Institutions.	February 2000

Dept.	Purpose	Time of Delivery
STA	Monetary and finance statistics	November 2003
STA	National accounts	November 2001
STA	Monetary and finance statistics	November 2001
STA	Monetary and finance statistics	September 2001
STA	Mission on money and banking statistics.	June–July 1999

XVII. Resident Representative:

Mr. Breuer assumed the position of resident representative in Nicaragua in August 2002.

Nicaragua—Relations with the World Bank Group
(As of October 31, 2003)

I. Financial Relations

A. Bank Loans and IDA Credits

(In millions of U.S. dollars)

	Bank	IDA	Total
Fully disbursed loans (31) and credits (25)	229.6	928.9	1,158.5
Credits/loans currently undisbursed	0.0	203.4	203.4
Total (net of cancellations)	**229.6**	**1,132.3**	**1,361.9**
Of which			
Repaid	224.1	24.5	248.5
Borrower obligations	0.0	948.6	948.6
Amount sold and repaid	5.6	0.0	5.6

B. World Bank/IDA Loan Commitments and Disbursements

1. As of October 31, 2003, total loans/credits disbursed and undisbursed from the Bank/IDA amounted to US$1,362 million, of which US$203 million remain to be disbursed. In view of its low income and high indebtedness, Nicaragua has been an IDA-only country since lending resumed in the early 1990s. Since 1999, annual IDA gross disbursements have averaged US$74 million. This amount reflects the return to a normal lending program, following the exceptional financing induced by emergency reconstruction needs in the aftermath of hurricane Mitch in October 1998. These needs triggered a rapid response on the part of IDA, which more than doubled gross disbursements from US$51 million in 1997 to US$120 million in 1999. The decline of gross disbursements since then mirrors the winding down of reconstruction activities.

2. Nicaragua reached the HIPC Decision Point on December 21, 2000, qualifying for IDA debt relief assistance equal to US$379 million. Since January 1, 2001, IDA has provided Interim HIPC assistance equivalent to a 90 percent reduction on debt service to IDA.

II. Plans for the Next 12 Months

3. IDA has prepared a new Country Assistance Strategy (CAS) and Programmatic Structural Adjustment Credit (PSAC), which were presented to the Board in March 2003. IDA is currently preparing a Poverty Reduction Strategy Credit (PRSC) to support the implementation of the government's poverty reduction strategy. In addition, future projects being considered for IDA support include a Rural Micro-Finance Development Project, Education and Health Projects, a Public Sector Management Project and a Competitiveness Project.

Nicaragua—Relations with the Inter-American Development Bank
(As of November 30, 2003)

I. Financial Relations

A. Statement of IDB Loans
(In millions of U.S. dollars)

Year	Purpose	Amount
2003	Public sector modernization and fiscal reform	25.0
	Multisector credit	30.0
	Modernization of agricultural health services	7.3
2004	Plan Puebla-Panama roads program for competitiveness	40.0
	Roads Program for Competitiveness II	40.0
	Social Sector Reform Program II	15.0
	Support to SECEP	6.0
	Citizen's Security	7.0
	Population and Housing Census	5.0
	Education for Children and Adults	10.0

B. IDB Loan Commitments and Disbursements

As of November 30, 2003, there are 32 projects in the Bank's portfolio for US$698.1 million, with an undisbursed balance of US$446.3 million. During 2003–04, 10 projects for US$185.3 million are programmed. All three projects for 2003 have been approved.

During 2002, Nicaragua received US$45.7 million (nominal) of HIPC interim debt relief from the IDB. For 2003, interim relief of US$39.1 million is projected.

II. Recent Technical Assistance

The Bank's program for 2003–04 also includes 19 new nonreimbursable technical cooperation projects for US$7.1 million.

III. Recent Agreements

Nicaragua's country strategy for 2002–05 was approved by the Board in February 2003.

IV. Recent Events

The Bank hosted the Consultative Group Meeting for Nicaragua in Managua on October 27–28, 2003. The international community strongly supported the government's macroeconomic policies, its anticorruption campaign, and the country's National Development Plan.

REPUBLICA DE NICARAGUA

Managua, December -22, 2003

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. Köhler:

1. We are attaching the Supplementary Memorandum of Economic and Financial Policies (SMEFP) that reviews economic developments and policy implementation through September 2003 under the PRGF arrangement approved in December 2002, and sets out specific objectives and targets for the period December 2003–June 2004. Based on the good track record and policies adopted, we request completion of the fourth review under the PRGF arrangement and the establishment of corresponding performance criteria (PCs) for end-June 2004. Moreover, Nicaragua has substantially met the conditions for reaching the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative, including in a few areas where developments since the 2000 decision point have required modifications of some conditions. Therefore, we request that the Executive Boards of the Fund and the Bank approve reaching the completion point under the enhanced HIPC Initiative. We also request a waiver for the nonobservance of two PCs (paragraph 2 below).

2. Nicaragua's economic performance through September 2003 has been consistent with the program. Macroeconomic policies have been in line with the PRGF arrangement, and progress has been made on the structural agenda. However, the structural PC on concluding the asset recovery plan was completed by end-October, rather than by end-September, due to a brief delay in the completion of administrative procedures for transferring residual assets to the ministry of finance and collecting the sales proceeds. In addition, the continuous PC on the stock of arrears was missed by a small amount following a lawsuit attaching any payment on Nicaragua's indemnity bonds (BPI) made through Euroclear.

3. Extensive public consultations have been held on the National Development Plan (NDP), including with civil society groups, business organizations, local governments, and the international community. Taking into account the comments we have received, we will incorporate the NDP's strategic elements into an enhanced PRSP by mid-2004.

4. We are committed to continue good faith negotiations with all non-Paris Club official and private creditors to seek debt relief comparable to that granted by Paris Club creditors under the enhanced HIPC Initiative.

5. We are confident that the policies and measures set forth in the SMEFP are adequate to achieve the program's objectives under the PRGF arrangement. However, we stand ready to take, in consultation with the Fund, further measures that may be needed for the successful implementation of the program, and to ensure compliance with all required criteria necessary to reach the completion point under the HIPC Initiative by end-2003. To this end, we will continue consulting with the Fund on relevant economic and financial policies, and provide the Fund with the necessary data on a timely basis for monitoring purposes. Consistent with our intention to keep the public informed about our policies and objectives, the government will publish the SMEFP and will report on the progress of the program periodically.

6. We propose that the Fund carry out reviews under the program in March 2004, June 2004, and September 2004 and based on the observance, respectively, of end-December 2003, end-March 2004, and end-June 2004 quantitative and structural performance criteria established in Tables 1 and 2 of the attached memorandum.

7. We assure you that the government of Nicaragua remains committed to the implementation of the program, and reaching the HIPC completion point by end-2003.

Sincerely yours,

/s/
Mario B. Alonso I.
President
Central Bank of Nicaragua

/s/
Eduardo Montealegre Rivas
Minister of Finance

SUPPLEMENTARY MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

1. We have made continued progress in implementing the strategy embodied in the Poverty Reduction Strategy Paper (PRSP), as updated in the 2003 PRSP progress report, and the program supported by the Poverty Reduction and Growth Facility (PRGF). This memorandum supplements the Memorandum of Economic and Financial Policies of November 19, 2002, and the associated supplements of June 3, 2003 and October 2, 2003, and outlines the key next steps envisaged in implementing our program. Moreover, Nicaragua has substantially met the conditions for reaching the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative, including a few areas where developments since the 2000 decision point have required modifications of some conditions. Therefore, we request that the Executive Boards of the Fund and the Bank approve reaching the completion point under the enhanced HIPC Initiative.

2. Economic performance has been broadly in line with the program. Real GDP growth is projected to increase to 2.3 percent in 2003 and 3.7 percent in 2004. Twelve-month inflation through November was about 6 percent (in line with the program target of 6 percent for end-2003). Net international reserves surpassed the September performance criterion (PC) by US$39 million (about 1 percent of GDP). The deficit of the combined public sector (CPS) (after grants) narrowed to 2.3 percent of annual GDP in the first nine months of 2003, below the path envisaged in the program. In January–September 2003, poverty-reducing spending reached 7.7 percent of GDP, higher than the program target of 7.4 percent of GDP.

3. Macroeconomic policies have been in line with the PRGF arrangement, and progress has been made on the structural agenda. However, the structural PC on concluding the asset recovery plan was completed by end-October, rather than by end-September, due to a brief delay in the completion of administrative procedures for transferring residual assets to the ministry of finance and collecting the sales proceeds. In addition, the continuous PC on the stock of arrears was missed by a small amount following a lawsuit attaching any payment on Nicaragua's indemnity bonds (BPI) made through Euroclear.

4. Our key economic objectives in the macroeconomic framework for 2003–04 are the following:

Key Macroeconomic Objectives

	Prel.	Revised Program 1/	
	2002	2003	2004
Real GDP growth (in percent)	1.0	2.3	3.7
Consumer prices (end period)	4.0	6.0	5.0
Gross international reserves (in millions of US$)	454	447	524
Change in augmented BCN reserve position (in millions of US$)	82	55	66
Combined public sector deficit after grants (in percent of GDP)	-5.5	-3.8	-3.8 2/
Deficit before pension reform	-5.5	-3.8	-3.2
Cost of pension reform	0.0	0.0	-0.6 2/

Sources: Central Bank of Nicaragua (BCN); Ministry of Finance; and Fund staff estimates/projections.
1/ As outlined in our Letter of Intent and SMEFP of October 2, 2003.

2/ Assumes pension reform from July 2004.

5. We remain fully committed to the medium-term fiscal strategy outlined in the program supported by the PRGF arrangement. For 2004, our fiscal program targets a CPS deficit (after grants) of 3.2 percent of GDP. Including the revenue losses associated with the pension reform (estimated at 1.2 percent of GDP on an annual basis), the deficit target is about 3.8 percent of GDP. CPS savings are projected to rise from 0.2 percent of GDP in 2003 to 2.9 percent of GDP in 2004, about 2.0 percentage points of which reflects lower interest payments due to HIPC debt relief.

Fiscal Indicators 1/

(In percent of GDP)

	2002	2003		2004	
	Prel.	Prog. 2/	Proj.	Prog. 2/	Assuming no Pension Reform
Combined public sector deficit after grants	-5.5	-3.8	-3.2	-3.8	-3.2
Combined public sector deficit before grants	-10.5	-8.9	-8.4	-6.8	-6.2
Combined public sector savings	-2.5	0.2	0.2	2.9	3.5
Combined public sector primary savings	4.7	6.7	6.6	6.7	7.3
Combined public sector primary expenditure	23.6	24.5	23.9	24.9	24.9
Tax revenues of the central government	14.3	16.3	16.0	16.7	16.7
Total poverty-reducing spending	10.2	11.0	11.0	11.4	11.4

Sources: Central Bank of Nicaragua; and Ministry of Finance.

1/ Assumes HIPC completion point is reached at end-2003.

2/ As outlined in our letter of Intent and SMEFP of October 2, 2003.

6. The 2004 budget approved by the assembly in December is in line with the PRGF-supported program and the spending priorities embodied in the PRSP. The budget is designed to support economic growth and reduce poverty, while preserving the program goals of low inflation, a strengthened external position, and attaining fiscal sustainability. It will achieve these aims through improvements in the efficiency of public expenditures and strengthened revenue collections (including through improved tax administration). Primary current expenditures at 15.2 percent of GDP will remain at about the same level as in 2003. Poverty-reducing expenditures will rise to 11.4 percent of GDP (from 11 percent of GDP in 2003), and public investment mainly in infrastructure and human capital will increase to 9.7 percent (from 9.0 percent in 2003). If foreign financing of capital spending is lower than expected, as shown in the table below, we will postpone capital spending by an equivalent amount, while making every effort to protect poverty-reducing spending.

External Financing
(In millions of U.S. dollars)

		2004				
	2003	QI	QII	QIII	QIV	Total
Untied Resources	91.7	38.3	25.6	15.9	17.6	97.3
Loans	60.1	37.5	25.0	15.0	0.0	77.5
Grants	31.6	0.8	0.6	0.8	17.6	19.8
Tied Resources	285.1	61.5	83.1	79.9	69.9	293.6
Loans	183.0	41.5	45.6	52.4	42.9	182.4
Grants	102.1	20.0	37.5	27.5	26.2	111.2

Source: Central Bank of Nicaragua.

7. **A range of other fiscal reforms are underway to support medium-term fiscal consolidation.** These include:

- **Tax administration.** The tax office has completed its reform plans ahead of schedule and has begun strengthening the large taxpayer unit and preparing their strategic plan on information technology. The customs office will complete its plans by March 2004.[27] A new tax code was submitted to the assembly in November 2003 and its approval is expected by March 2004. The law on administrative career for DGI and DGA was also submitted to the assembly in November 2003 and its approval is expected by June 2004.[28] Starting in 2004, these efforts are projected to increase tax revenues by 0.2 percent of GDP per year until 2008.

[27] The Fund and the IDB are providing technical assistance to these agencies.

[28] The tax code describes the rights and obligations of taxpayers and tax officials, including sanctions for tax evasion.

Internal Tax Administration's Action Plan for 2004

Key Actions	Expected Date of Implementation
1. Strengthen the tax office's large taxpayers unit by updating database on large taxpayers, establishing new procedures to monitor nonfilers and delinquent taxpayers, and improving effectiveness of large taxpayer audits.	March
2. Reorganize the DGI and redefine assignments to each core functional department (tax collection, audit and tax enforcement).	June
3. Present a three-year strategic IT plan.	September
4. Establish a system to systematically exchange taxpayer-related information among the DGI, DGA, INSS, and other public institutions.	September
5. Develop a data warehouse to support tax audit and tax enforcement work.	December
6. Set up a tax collection system via financial institutions.	December

- **Fiscal decentralization.** In July 2003, the assembly approved the municipality transfers law, which includes a provision for transferring the equivalent of 4 percent of tax collections to the municipalities starting in 2004, rising gradually to 10 percent by 2010, economic conditions permitting. In order to make the decentralization process fiscally sustainable, we will issue during 2004 a presidential decree to modify the regulations of the municipality law and a legal framework that redefines the responsibilities of the *Fondo de Inversión Social de Emergencia* (FISE) and *Instituto Nicaragüense de Fomento Municipal* (INIFOM). Both of these measures aim at balancing, in the medium term, the resource transfers with the corresponding transfers of expenditure responsibilities to municipalities. The broad objective is to improve the efficiency of public spending by ensuring greater participation and accountability at the local level for spending decisions.

- **Law on fiscal responsibility.** This law will establish a multi-year budgeting framework, and establish ceilings for key variables such as the CPS deficit and public debt. A draft law will be submitted to the assembly by June and its approval is expected by December 2004.

- **Pension reform.** Following the approval of a new pension law and the establishment of the superintendency of pensions, in consultation with the World Bank, we have prepared a roadmap for pension reform and updated the estimates of the fiscal impact of the pension reform. Together with the World Bank, we are assessing various policy options to ensure that the cost of the reform is consistent with fiscal sustainability.

- **Debt management.** The assembly has approved the public debt law that establishes a single process for contracting public sector debt, both internal and external. The law empowers a Technical Debt Committee to advise the government on debt issues, to ensure that financing costs are minimized, and to consider the implications of new borrowing for debt sustainability.

- **Tracking HIPC interim relief**. We have developed a monitoring mechanism that adequately tracks the use of budgetary savings from HIPC interim relief through the Supplementary Social Fund. The use of the budgetary savings is reflected in the central government budget, which identifies the government's total poverty-related outlays.

- **Public expenditure.** The government's main objective is to ensure fiscal sustainability by increasing the quality and efficiency of public expenditures. To this end, the government has made permanent the public expenditure commission, created in July 2003, to monitor implementation of its recommendations. In addition, the government will (i) initiate calculations of the recurrent cost implications of public investment, with a view to including only new projects that are fiscally sustainable; (ii) establish a unified official registry of public investment so that all foreign- and domestic-financed projects are monitored through a centralized system; and (iii) improve monitoring of all public spending, including poverty-reducing expenditures, based on information provided through the integrated administrative and financial management system (SIGFA), the Supplementary Social Fund (FSS), and the single treasury account.

8. We will continue improving the efficiency of public enterprises. The water and sewerage company (ENACAL) is strengthening its management to improve collections of overdue accounts. A draft law sent to the assembly in October 2003 will provide the legal backing needed for this effort. In addition, more water meters are being purchased, meter-reading operations will be rationalized, and tariffs will be reviewed in mid-2004. With assistance from the IDB, we intend to develop a medium-term strategy for improving the efficiency of operations. We expect these efforts to result in higher operating surpluses in the coming years. With respect to the power sector, we are developing a plan for reforming this sector, further improving financial and operational efficiency, making government subsidies more transparent, and improving the legal framework.

9. The preliminary recommendations of the high-level public expenditure commission have been included in the 2004 budget. The recommendations focus on steps to improve the efficiency of current expenditures, estimate the recurrent costs of investment projects, increase coordination with donors, and strengthen the tracking of poverty-spending (in line with World Bank advice).

Public Expenditure Commission Recommendations

- Increase the efficiency of primary current spending.
- Maintain the 2004 budget's current expenditure ceiling, despite the additional cost of municipal transfers and municipal elections.
- Carry out a study to assess the optimal manner to transfer expenditure responsibilities to the municipalities. Two consultants have been hired to identify expenditures that could be transferred in the short run.
- Improve the poverty-reducing-tracking mechanism by full compliance with the guidelines of the Social Supplementary Fund.
- Improve the classification of poverty spending.

10. Monetary policy will remain guided by the objectives of maintaining low inflation and reducing domestic debt, while strengthening the central bank reserve position with a further buildup of US$20 million of NIR, plus a repayment of BCN domestic debt of US$46 million in 2004. In addition, the revised program targets a reduction of US$40 million in central government debt. We expect that the forthcoming assessment under the Financial Sector Assessment Program (FSAP) will contribute to strengthened management of monetary policy.

11. Exchange rate policy will continue to be guided by the crawling peg arrangement. The annual rate of crawl vis-à-vis the U.S. dollar will be reduced to 5 percent in 2004 (from 6 percent in 2003), in line with the end-period inflation target of 5 percent.

12. We continue to work on strengthening the financial sector. In this context:

- We recognize that for purposes of providing a sound legal framework for banking supervision in Nicaragua, strengthening legal protection of staff of the Superintendency of Banks (SB) and the BCN who perform supervisory activities is essential. Thus, a draft law providing legal protection to BCN staff and SB staff from personal liability for supervisory actions taken in good faith in the course of performing supervisory duties, was submitted to the assembly in December 2003 and its approval is expected by mid-May 2004.
- We are enhancing prudential norms and supervision in line with Basel Core Principles. The SB approved in November 2003, norms to limit risk derived from maturity mismatches.
- We are working closely with the IMF and World Bank staff on the FSAP. A first mission has taken place and the second one is planned for early 2004. We

look forward to the recommendations of the FSAP, which we hope will contribute to future reforms in the financial sector.

- We are revising the Manual of Bank Inspection, in line with IMF's Monetary and Financial Systems Department (MFD) recommendations, to incorporate new technical and administrative procedures for on-site inspections.

13. Extensive public consultations have been held on the National Development Plan (NDP), including with civil society groups, business organizations, local governments, and the international community. Taking into account the comments, we will incorporate the NDP's strategic elements into an enhanced PRSP by mid 2004.

14. We have substantially met the trigger conditions for reaching the completion point under the enhanced HIPC Initiative, except for the sale of the state-owned power companies' (ENEL) remaining electricity-generating plants. However, regarding Hidrogesa, we have determined, in close consultation with the IDB, that privatization of this firm is no longer advisable, since it could result in an excessive concentration of market power in one firm. Moreover, the competitiveness of the electricity sector has been rising as a result of increased private sector participation in generation and distribution. To achieve the original goal of improving overall efficiency in the electricity sector, we are discussing with the IDB a comprehensive regulatory reform of the sector. The sale of the remaining government shares in the telecommunications company (ENITEL) has been delayed due to valuation problems, but we received a viable offer on December 17, and expect to complete the process by mid-January 2004.

15. We continue to pursue other important structural reforms envisaged in the program. The executive has met with the other branches of government to discuss ways of strengthening the judicial system. The government presented its proposal for judicial reform in September 2003 and initiated national consultations. Upon the completion of this process, we intend to present an action plan by June 2004 that will be based on the broadest possible political consensus. We also have made progress in improving governance and combating corruption. The assembly approved a new civil service law in November (taking into account the most recent round of World Bank comments). In addition, with support of the World Bank and the IDB, we are strengthening public procurement practices and the comptroller's office.

16. We have implemented all of the recommendations of the Fund's 2001 safeguards assessment, with one exception. The exception relates to disclosure of the differences between International Accounting Standards and the current financial reporting practices of the BCN. We expect to disclose the differences after the comptroller's office approves the 2002 financial statement. In November 2003, the Board of the BCN approved a resolution to appoint external auditors for three-year terms. We have also agreed on an action plan for implementation of the second assessment, including the adoption of international accounting practices by the BCN.

17. Implementation of the second annual program supported by the PRGF arrangement will continue to be monitored through quarterly reviews, performance criteria, and benchmarks. Tables 1 and 2 present the quantitative PCs for end-March 2004 and end-June 2004, as well as indicative targets for September–December 2004. We continue to be firmly committed to the success of the program and stand ready to implement additional measures, as needed, to achieve its objectives.

Table 1. Nicaragua: Quantitative Performance Criteria for PRGF-Supported Program

	Cumulative Flows from January 1, 2002				Cumulative Flows from January 1, 2004							
					March 31, 2004		June 30, 2004		September 30, 2004		Dec. 31, 2004	
	September 30, 2003			Dec.31, 2003		Rev.		Rev.		Rev.		Rev.
	Prog. 1/	Actual	Deviation (-)	Prog. 1/	Prog.	Prog.	Indicative	Prog.	Indicative	Indicative	Indicative	Indicative
	(In millions of cordobas)											
Net domestic financing of the combined public sector (ceilings)	-61	-805	744	-927	-545	-881	-724	-1,146	-911	-1,406	-1,144	-1,555
Savings of the combined public sector (floors)	-1,438	-1,414	24	-1,332	389	723	775	1,199	1,243	1,740	1,538	1,954
Net domestic assets of the central bank (ceilings)	-806	-1,282	476	-126	-202	-201	-391	-308	-108	-273	-90	-94
	(In millions of U.S. dollars)											
Net international reserves of the central bank (floors)	46	85	39	34	0	0	10	4.9	-9	1	20	20
Net repayment of public domestic debt (+) (floors) 2/	13	68	55	103	0	39	12	47	23	58	41	86
Disbursements of nonconcessional external debt contracted 3/ or guaranteed by the public sector (ceilings)	0	0	0	0	0	0	0	0	0	0	0	0
Stock of external payments arrears (ceilings) 3/	0	2	-2	0	0	0	0	0	0	0	0	0
	(In millions of cordobas)											
Indicative targets												
Tax revenue of the central government (floors)	15,724	15,410	-314	18,217	2,683	2,683	5,412	5,412	8,382	8,382	11,350	11,350
Total primary expenditure of the central government (ceilings)	18,105	18,269	-164	21,700	2,766	2,766	6,090	6,109	9,369	9,379	12,728	12,729
Deficit of the combined public sector, before grants (ceilings)	-9,856	-9,621	235	-11,501	-874	-614	-2,376	-2,018	-3,754	-3,253	-5,049	-4,638
Net domestic financing of the nonfinancial public sector (ceilings) 4/	-3,478	-3,753	275	-3,910	-591	-1,204	-1,321	-1,884	-1,725	-2,463	-2,437	-2,961
Memorandum items												
Net repayment of public domestic debt of the central bank	13	68	55	103	0	18	12	18	23	24	41	46
Net repayment of the public domestic debt of the central government	26	28	2	36	14	21	20	29	24	33	36	40

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

1/ Program as stated in EBS/03/138.

2/ In 2003 and 2004, program and indicative columns (from EBS/03/138) only include central bank debt. Revised program and revised indicative columns include central bank and central government debt.

3/ Measured on a continuous basis.

4/ On a cash basis.

Table 2. Nicaragua: Fourth Program Review—Prior Actions, Structural Performance Criteria, and Benchmarks

Measures	Original Program /1	Revised Program /2	
	Expected Date of Implementation	Date of Implementation	Status of Implementation
I. Prior Actions for Completion of Fourth Review			
Approval by the assembly of the 2004 budget, consistent with a combined public sector deficit (after grants) equal or less than 3.8 percent of GDP (C$2,555 million).		Mid-December 2003	Done
II. Performance Criteria			
1. Asset Recovery Plan			
(i) End of the asset auction process.	End-June 2003	End-June 2003	The last auction took place in late August. Outsourcing firm completed tasks assigned in contract in mid-September.
(ii) Conclude implementation of asset recovery plan for assets received from intervened banks. 3/	End-September 2003	End-September 2003	Virtually all asset proceeds were collected by end-September. 3/ Transfer of all residual assets from the BCN to the ministry of finance was completed by end-October. Staff supports a waiver for this PC.
2. Grant legal protection to staff of the Superintendency of Banks.			
(i) Submission of a draft law to the assembly (SMEFP paragraph 12).		End-2003	Done
(ii) Approval of a law by the assembly (SMEFP paragraph 12).		Mid-May 2004	
3. Fiscal responsibility law.			
Submission to the assembly (SMEFP paragraph 7).		June 2004	
III. Benchmarks			
Fiscal			
1. Revised Tax Code.			
(i) Submission to the assembly.		End-2003	Submitted in November.
(ii) Approval by the assembly.		End-March 2004	

Table 2. Nicaragua: Fourth Program Review—Prior Actions, Structural Performance Criteria, and Benchmarks

Measures	Original Program /1	Revised Program /2	
	Expected Date of Implementation	**Date of Implementation**	**Status of Implementation**
2. Approval by the assembly of the law on domestic and external public indebtedness.		End-2003	Done
3. Strengthen tax administration through:			
(i) adoption of an action plan for DGA (customs) for 2004–06; and	End-June 2003	End-March 2004 4/	Authorities requested TA for DGA.
(ii) adoption by the DGI (internal tax administration) of an action plan for 2004–06;	End-June 2003	End-2003	Done
(a) strengthen the tax office's large taxpayers unit.		March 2004	
(b) present a three-year strategic IT plan.		September 2004	
4. Commission on the quality of public spending to advise the government on how to improve the effectiveness of public spending to generate growth and reduce poverty.			
(i) Agree on terms of reference and establish the commission.		Mid-June 2003	Commission established. Terms of reference completed in August.
(ii) Present the findings and recommendations for 2004 budget.		Mid-September 2003	Completed in September.
(iii) Review public spending with the aim of improving efficiency of MINSA, MEC, MTI, INIFOM, IDR, and FISE.		March 2004	
5. Law on fiscal responsibility.			
Approval by the assembly.		December 2004	
6. Decentralization. 5/			
(i) Issue a presidential decree to modify the municipality law's regulations.		September 2004	
(ii) Establish a legal framework that redefines the responsibilities of the FISE and INIFOM.		September 2004	
Financial Sector			
7. Approval of new on-site technical and administrative procedures for banking supervision, including the inspection manual and regulatory actions for noncompliance with norms in effect, in line with Basel Core Principles.		End-2003	

Table 2. Nicaragua: Fourth Program Review—Prior Actions, Structural Performance Criteria, and Benchmarks

Measures	Original Program /1	Revised Program /2	
	Expected Date of Implementation	Date of Implementation	Status of Implementation
8. Approval of prudential norms to limit risks derived from maturity mismatches between assets and liabilities.	End-March 2003	End-November 2003	Approved in October.
9. Submission to the assembly of amendments to financial sector laws in line with Basel Core Principles for effective bank supervision and for changes in FOGADE.	End-September 2003	Mid-May 2004	Awaiting FSAP recommendations.
10. Grant legal protection to staff of the Central Bank of Nicaragua.			
(i) Submission to the assembly.		End-2003	Done
(ii) Approval by the assembly.		Mid-May 2004	
Privatization			
11. Divest the remaining government stake in ENITEL.	End-September 2003	End-2003	Investment bank has been selected and divestment is expected by mid-January 2004.
Governance			
12. Judicial reform.			
(i) Complete and make public authorities' proposal.		End-September 2003	Completed in September.
(ii) Launch national consultation process.		End-2003	Done
(iii) Present an action plan.		June 2004	

1/ As indicated in EBS/02/194 (November 20, 2002). The specific requirements for the implementation of these measures are specified in the Technical Memorandum of Understanding (TMU).
2/ The specific requirements for the implementation of these measures are specified in the TMU.
3/ The receipt of the proceeds for one sale (amounting to US$480,000) is pending the resolution of a legal dispute initiated by a bidder.
4/ Specific measures will be determined at the time of the adoption of the plans.
5/ Both of these measures aim at balancing, in the medium term, the resource transfers with the corresponding transfers of expenditure responsibilities to municipalities. The broad objective is to improve the efficiency of public spending by ensuring greater participation and accountability at the local level for spending decisions.

NICARAGUA—TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This technical memorandum incorporates all previous understandings between the Nicaraguan authorities and the Fund relating to the monitoring of the Poverty Reduction and Growth Facility (PRGF) arrangement into one document. No substantive changes have been made relative to previous understandings.

2. **For 2004, the quantitative performance criteria and indicative targets** will be defined as cumulative flows from January 2004.

Fiscal Targets

3. **Coverage of fiscal accounts**

(a) Nonfinancial public sector (NFPS) includes the central government, the Nicaraguan social security institute (INSS), the municipality of Managua, and two public sector enterprises: ENTRESA (electricity transmission) and ENACAL (water and sewage company).[1]

(b) Savings of the combined public sector (CPS) includes the savings of the NFPS and the operating result (quasi-fiscal balance) of the Central Bank of Nicaragua (BCN).

(c) The deficit of the CPS includes the deficit of the NFPS and the operating result of the BCN.

4. **Interest on the domestic debt** includes cash interest, except for the cost of the zero-coupon CENIs issued for bank resolution, which are shown on an accrual basis for 2003 (Table 1). Beginning in 2004, all interest payments will be shown on a cash basis, since the zero-coupon CENIs have either been repaid or replaced with coupon bearing BCN *letras*.[2] For 2004 and beyond, the targets for savings and net domestic financing (NDF) of the CPS will be based entirely on cash interest payments. For 2004, this requires that the third review program targets be modified by the difference between accrued interest in the program and cash interest in the revised program (Table 2, column D)—to the extent that this difference is negative (positive), savings are adjusted upward (downward) and net domestic financing is adjusted downward (upward). Net repayment of the sum of the domestic debt of the central

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[1] Starting in 2005, all operations of the electricity holding company (ENEL), the telecommunications regulatory agency (TELCOR), and the port company (ENAP) will be included in the program. During 2004, they will be included on an indicative basis. As complete and timely information becomes available for other public sector entities, the government intends to expand the definition of the public sector.

[2] The BCN and the central government are taking steps to improve their debt statistics in order to be able to calculate all interest on an accrual basis, as recommended by the GFS manual.

bank and central government will be increased (decreased) to the extent that cash interest payments in the revised program are lower (higher) than in the original program (see Table 2, column E). Tables 1 and 2 below are for illustrative purposes only; program performance will be evaluated using actual data.

Table 1. Financial Cost of Bank Resolution 1/

(In millions of córdobas)

	Accrual	Cash	Adjustment
2003	[891]	[889]	2

1/ Corresponds to the interest and dollar-indexation cost associated with the issuance of CENIs due to the bank resolution.

Table 2. Accrual Versus Cash Interest Payments

(In millions of córdobas)

	Program 1/		Revised Program		
	Accrual	Cash	Cash	Difference	Difference
	A	B	C	D = C-A	E = C-B
2004	**481.3**	**606.3**	**473.7**	**-7.4**	**-132.6**
QI	129.6	404.4	0.0	-129.6	-404.0
QII	120.0	0.0	220.4	100.4	220.4
QIII	117.0	201.9	35.8	-81.2	-166.1
QIV	114.7	0.0	217.6	102.9	217.6

1/ As stated in EBS/03/138.

5. **Interest on the external debt** presents cash payments and interim HIPC assistance. After reaching the HIPC completion point, and termination of interim debt relief, only cash payments will be shown.

6. **Total primary expenditure of the central government** is defined as the sum of wages and salaries, other goods and services, current and capital transfers, capital expenditure, and net lending.

7. **Savings of the CPS** is defined as the difference between current revenue and current expenditure of the nonfinancial public sector, plus the operating result of the BCN.

8. **Adjusters**: The floor of the CPS savings will be adjusted: (a) upward (unlimited) in the event of additional revenues associated with delays in the implementation of the privately managed pension funds, assumed to take place on July 1, 2004; (b) downward in the event of

lower revenues because implementation of the privately managed pension funds occurs before July 2004; and (c) downward in the event of higher cash due interest payments in case of delays in the termination of interim HIPC arrangements.

9. **Net domestic financing (NDF) of the CPS.** For 2003, NDF of the CPS comprises the operating result of the BCN, the adjustment of the cost of the bank resolution CENIs from cash to accrual, and the change from their respective stocks at the end of the previous year of the sum of (a) the outstanding stock of debt of the NFPS to the domestic financial system (BCN, commercial banks, and the *Fondo Nacional de Inversiones* (FNI)) net of deposits (including arrears that correspond to obligations considered eligible for refinancing or rescheduling, or other debt reduction mechanisms) with the foreign currency part of the net debt to the banking system converted into córdobas at the program exchange rate (of C$15.1 per U.S. dollar for 2003 and C$15.9 per U.S. dollar for 2004); (b) the outstanding stock of domestically-issued public sector debt held by the private residents and nonresidents with the foreign currency part converted into córdobas at the program exchange rate (of C$15.1 per U.S. dollar for 2003 and C$15.9 per U.S. dollar for 2004); (c) the outstanding stock of suppliers' credits; and (d) the outstanding stock of floating debt. For 2004 onward, the same definition applies. However, since all interest is on a cash basis, the adjustment described in the first sentence of this paragraph is not applied.

10. **Adjusters**: The ceiling on the cumulative NDF of the CPS will be adjusted: (a) upward by up to US$30 million, US$35 million, and US$15 million in the last quarter of 2003, the first quarter of 2004, and the second quarter of 2004, respectively, in the event of lower disbursements of balance of payments support and/or privatization receipts than the amounts shown in Table 4; (b) downward (unlimited) in the event of higher disbursements of balance of payments support and/or privatization receipts than the amounts shown in Table 4; (c) downward (unlimited) in the event of additional revenues associated with delays in the implementation of the privately managed pension funds; and (d) upward in the event of lower revenues because implementation of the privately managed pension funds occurs before July 2004.

11. **Deficit of the CPS (before grants)**. Defined as the savings of the combined public sector (as given in paragraph 7) plus capital revenue less capital expenditure and net lending of the nonfinancial public sector.

12. **Reporting**: The BCN will send to the IMF monthly electronic information on the detailed operations of the CPS. The monthly information will be provided no later than six weeks after the end of each month.

Monetary Targets

13. **Net international reserves (NIR) of the BCN**. For program purposes, NIR is defined as the difference between the (a) gross foreign assets of the BCN that are readily available; and (b) short-term reserve liabilities of the BCN (including purchases and credits

from the IMF), plus arrears on foreign debt service, plus foreign currency reserve requirement deposits of commercial banks at the BCN.

14. Readily available **foreign assets of the BCN** exclude those that are pledged or otherwise encumbered, including, but not limited to, reserve assets used as collateral or guarantee for a third-party external liability.

15. **Net repayment of the domestic debt of the BCN and the central government (CG).**[3] For program purposes, it is defined as the difference between new placements and redemptions of: (i) the BCN CENIs, TEIs, TELs, BOMEX, standardized *letras* and any other BCN paper held by institutions outside the CG; and (ii) the CG's treasury bonds, BPIs, and any other obligations owed to institutions or individuals outside the CG, except the BCN. It also includes all domestically placed paper held by residents and nonresidents. This amount will be converted into U.S. dollars at the program exchange rates (of C$15.1 per U.S. dollar for 2003 and C$15.9 per U.S. dollar for 2004).

16. **Adjusters:** The net repayment of the domestic debt of the BCN and the CG will be adjusted: (a) downward by up to US$30 million, US$35 million, and US$15 million in the last quarter of 2003, the first quarter of 2004, and the second quarter of 2004, respectively, in the event of lower disbursements of balance of payments support and/or privatization receipts than the amounts shown in Table 4; (b) upward (unlimited) in the event of higher disbursements of balance of payments support and/or privatization receipts than the amounts shown in Table 4; and (c) downward to the extent that the NIR target is exceeded.

17. **Net domestic assets (NDA) of the BCN** are defined as the difference between the change in the stock of currency issued and net international reserves, valued at the program exchange rate.

18. **Reporting**: The BCN will send to the IMF (a) daily electronic mail containing information of daily accounts of the BCN (stocks and flows) within two days after the end of the last working day; (b) monthly electronic mail with information of monthly accounts of the BCN, commercial banks and FNI (stocks and flows), within four weeks after the end of the month; and (c) quarterly accounts of the BCN, commercial banks, and FNI (stocks and flows) within five weeks after the end of the quarter.

Structural Measures

19. **The procedures to be established in the new banking supervision inspection manual** will be complemented by inspection guidelines for specific areas of banking supervision in line with recommendations of the August 2003 MFD mission. The extent to which supervisory action, penalties, and regulatory actions for noncompliance with

[3] This definition applies starting in 2004. For 2003, the definition of net repayment of the domestic debt of the BCN remains as stated in EBS/02/194.

regulatory norms are enforced will be determined by the peer review of banking supervision to be conducted in the context of the FSAP mission.

20. **The changes to the legal framework, which are in line with Basle Core Principles for effective banking supervision,** will (a) introduce legal protection for supervisors (Principle 1); (b) establish a mechanism to review and reject any proposals to transfer significant ownership in existing banks to other parties (Principle 4); (c) grant supervisors the ability to do supervision on a consolidated basis (Principle 20); and, (d) grant supervisors adequate supervisory measures to bring about timely corrective action when, among other reasons, banks fail to meet prudential requirements (Principle 22). In addition, the revised legal framework will eliminate the Superintendency's restrictions on sharing information with similar institutions in other countries; and remove secrecy on bank assets. Finally, new legislation will be prepared to set up a banking resolution framework that would provide adequate incentives and safeguards for an effective and transparent resolution mechanism.

21. **Strengthen the tax office's large taxpayers unit** will be understood to mean update the database on large taxpayers and reduce the percentage of nonfilers to 3 percent of total persons required to pay taxes.

Safeguards Assessment

22. **To address the vulnerabilities identified during the stage one safeguards assessment of the BCN and the updated review completed in August 2003 by the Fund's Finance Department (FIN),** we propose the following timetable:

Table 3. Nicaragua: Timetable for the Implementation of FIN's Recommendations

Measures	Expected Date of Implementation
1. International Accounting Standards (IAS)	
a. Disclose the differences between IAS and the BCN accounting practices:	
(i) in the 2002 financial statements.	October 2003
(ii) in the 2003 financial statements.	End-June 2004
b. Full adoption of IAS (beginning with the 2004 financial statements).	
– Initiate migration to IAS.	July 2004
– Complete migration of IAS.	December 2004
2. Adopt a Board resolution to appoint external auditors for three-year terms. The appointments should continue to be on an open competitive bidding basis by international auditing firms with expertise in International Standards on Auditing and IAS, in accordance with national legislation.	End-October 2003
3. Submit amendment of the BCN Law to the assembly to enhance the specificity of existing provisions for the removal of BCN Board members from office.	Mid-May 2004

To adopt the IAS, the BCN will establish a task force by end-2003 to ensure adequate training for the staff of the accounting department and identify the necessary changes to the central bank law.

External Sector Targets

23. **Borrowing on nonconcessional terms.** For the purpose of the ceiling on the contracting of nonconcessional external debt of the NFPS and the BCN, external debt limits apply to the contracting or guaranteeing of nonconcessional external debt by the public sector[4] and the BCN or any other agencies on their behalf. This limit applies not only to debt as defined in Point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted by the IMF on August 24, 2000 (see Appendix II), but also to commitments contracted or guaranteed for which value has not been received. External debt includes all current liabilities with a nonresident party, which are created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, at some future point(s) in time to discharge the principal and/or interest liabilities under the contract. This definition includes loans, suppliers' credits, and leases (operational and financial leases). The ceiling on contracting of nonconcessional external debt applies both to medium- and long-term debt defined as debt with maturity of one year or longer, as well as to short-term debt, defined as debt with maturity of less than one year. For program purposes, BCN instruments placed in the domestic market held by nonresidents, will be excluded from the ceiling on the contracting of nonconcessional external debt and included in the net repayment of the domestic debt of the BCN target.

24. **Excluded** from the ceiling on debt with a maturity of less than one year are import-related credits and BCN reserve liabilities. Borrowing from the Fund is excluded from the ceiling (maturities up to one year).

25. **Concessionality** will be based on a currency-specific discount rate based on the 10-year average of the OECD's commercial interest reference rates (CIRR) for loans or leases with maturities greater than 15 years and on the six-month average CIRR for loans or leases maturing in less than 15 years. Maturity will be determined on the basis of the original loan contract. Under this definition of concessionality, only debt with a grant element equivalent to 35 percent or more will be excluded from the debt limits.

26. **New loan reporting**: A loan-by-loan accounting of all new loans contracted or guaranteed by the public sector, including detailed information on the amounts, currencies,

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[4] As regards external sector targets, the public sector comprises the nonfinancial public sector as defined under fiscal targets, as well as all other public sector entities and enterprises including ENITEL (as long as the government stake is at least 50 percent), the airport, the lottery, CORNAP, and ENAP.

and terms and conditions, as well as relevant supporting materials, will be transmitted on a quarterly basis within four weeks of the end of each quarter by the BCN.

27. **External payments arrears.** External payments arrears are defined as overdue debt service obligations arising from external debt contracted or guaranteed by the public sector, except on external debt subject to rescheduling or restructuring. For purposes of this performance criterion, liabilities arising from the Bonds for the Payment of Indemnification ("Indemnity Bonds") are excluded.

28. **External arrears reporting:** The accounting of nonreschedulable external arrears by creditor (if any), with detailed explanations, will be transmitted by the BCN on a monthly basis within four weeks of the end of each month.

29. **Domestic arrears reporting:** The accounting of domestic arrears by creditor (if any), with detailed explanations, will be transmitted by the BCN on a monthly basis within four weeks of the end of each month.

Other Definitions

30. **Privatization receipts** are defined as payments received by the government in connection with the sale of state assets net of any fee. The programmed amounts consistent with this definition are showing in Table 4. Privatization revenues in foreign exchange are those recorded as such in the balance of payments.

31. **Balance of payments support.** Official external untied financial assistance is defined as loans and grants provided by foreign official entities that are received by the government for unrestricted budgetary use. The amounts assumed in the program consistent with this definition are shown in Table 4 attached.

32. **Accounting of HIPC assistance**. Interim HIPC assistance from multilateral creditors is identified as grants and shown in the public sector operations under grant revenues, and in the balance of payments table under current transfers. Interim HIPC debt relief from bilateral creditors is presented as exceptional financing in the public sector and in the balance of payments tables. Following completion point, only cash payments to multilateral and bilateral creditors are shown.

Table 4. Cumulative Program Financing
(In millions of U.S. dollars)

	Privatization	BOP Support	Asset Recovery 1/
Cumulative from October 2002			
2002			
QIV	11	35	4
2003			
QI	11	35	6
QII	11	76	5
QIII 2/	12	76	29
QIV	52	95	0
Cumulative from January 2004			
2004			
QI	0	38	0
QII	1	63	0

1/ Corresponds to the receipts of asset recovery net of the administration cost. This cost should not exceed US$5.6 million. Includes US$11 million received in BPI (face value), which for program purposes are recorded at market value (36 percent of the face value).
2/ Through September 2003, adjusters were calculated using the information shown in Table 2 of EBS/03/73 (June 4, 2003).

1/ Corresponds to the receipts of asset recovery net of the administration cost. This cost should not exceed US$[5.6] million. Includes US$11 million received in BPI (face value), which for program purposes are recorded at market value (36 percent of the face value).
2/ Through September 2003, adjusters were calculated using the information shown in Table 2 of EBS/03/73 (June 4, 2003).

Statement by the IMF Staff Representative
January 23, 2004

This statement provides additional information that has become available since the staff report was issued. The information does not alter the staff appraisal.

1. **Growth and inflation**. The monthly index of economic activity (IMAE) for October was 2.4 percent higher than a year earlier. This is in line with the modest recovery assumed in the program. The 12-month inflation rate in December was 6.5 percent, slightly higher than the program target of 6 percent. However, core inflation (excluding volatile items such as fuel) was only 3.7 percent.

2. **Fiscal developments.** Preliminary data through November 2003 indicate that the fiscal program remains on track.

3. **Interest rates**. Interest rates have continued to trend downward. At end-2003, average dollar deposit and lending rates were 5.7 percent and 12.1 percent, respectively.

4. **International reserves**. At end-2003, net international reserves were US$33 million higher than programmed, with gross reserves at US$504 (2.9 months of projected 2004 imports).

5. **Privatization**. The foreign company managing ENITEL (a state-owned telecommunications company) has decided not to match the offer received by the government in mid-December. Thus, the sale of ENITEL to the private sector (a floating completion point trigger) is now final. The authorities received the proceeds (US$49.6 million) on January 21.

6. **Structural benchmarks.** On January 16, 2004, new on-site technical and administrative procedures for banking supervision were approved (structural benchmark for end-2003).

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FOR IMMEDIATE RELEASE
January 23, 2004

International Monctary Fund
Washington, D.C. 20431 USA

IMF Completes Fourth Review of Nicaragua's PRGF-Supported Program, Completes Financing Assurances Review, and Grants Waivers

The Executive Board of the International Monetary Fund (IMF) today completed the fourth review of Nicaragua's performance under a three-year, SDR 97.50 million (about US$144.6 million) Poverty Reduction and Growth Facility (PRGF) arrangement that was approved on December 4, 2002 (see Press Release No. 02/53). In completing the review, the Executive Board approved Nicaragua's request for waivers of the nonobservance of performance criteria. In addition, the Executive Board completed the financing assurances review under Nicaragua's PRGF arrangement. These decisions enable the release of a further SDR 13.93 million (about US$20.7 million) to Nicaragua, which brings the total amount approved under the program to SDR 41.79 million (about US$62 million).

The PRGF is the IMF's concessional facility for low-income countries. It is intended that PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners, and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent, and are repayable over 10 years with a 5½-year grace period on principal payments.

Following the Executive Board's discussion on Nicaragua, Agustín Carstens, Deputy Managing Director and Acting Chairman, said:

"Nicaragua's recent economic performance continues to be commendable. Prudent macroeconomic policies and structural reforms have strengthened economic prospects and enabled the country to reach the enhanced HIPC Initiative completion point. Economic growth is recovering, inflation remains low, and the external position has improved. With economic growth projected to risc furthcr and the external environment becoming more favorable, the coming year presents an opportunity to capitalize on these hard-won achievements and move ahead forcefully with the reform agcnda.

"The authorities have adopted a strengthened growth strategy, which emphasizes private-sector-led growth and social equity. The public sector is expected to play a supportive role by providing the necessary basic infrastructure, improved education opportunities, and a more certain and transparent legal framework. Important strides have also been made in improving governance and strengthening public institutions. Sustaining these efforts will provide a favorable environment for growth and poverty reduction, in line with the objectives of the PRSP and the new National Development Plan.

"Notwithstanding these achievements, Nicaragua continues to face important challenges. In particular, widespread poverty remains a major concern; the public debt burden is still high, even after the enhanced HIPC Initiative completion point; and the highly-dollarized financial sector needs to be strengthened further. The authorities' medium-term economic program, embodied in the PRSP and the National Development Plan, addresses these challenges through the continued implementation of prudent macro economic policies and structural reforms. In carrying the program forward, it will be important to deepen the broad political and social consensus that has supported enhanced HIPC Initiative completion point, in particular by strengthening further transparency and governance in public sector operations and by extending the national consultation process, " Mr. Carstens said.

Statement by Luis Martí, Executive Director for Nicaragua and Roberto Simán, Senior Advisor to Executive Director January 23, 2004

Our Nicaraguan authorities would like to convey their appreciation to the staff for the valuable policy advice and for the constructive discussions and the support received in the preparation of this review.

They are particularly thankful to staff and senior management for the close cooperation over the past two years that has proved exceptionally valuable in advancing many key reforms and for reaching the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative.

Background

Since taking office in January 2002, the government of President Bolaños moved quickly to stop the severe economic deterioration that had taken place during the preceding two years. Faced with a large fiscal deficit and a domestic debt burden, the authorities implemented measures to reduce the fiscal deficit, tightened monetary policy, improved bank supervision, initiated the process to refinance the domestic debt and took decisive steps to address corruption and governance problems. These measures succeeded in stabilizing the reserve position of the country and laid the foundations for the comprehensive reform program supported by the three-year PRGF arrangement approved in December 2002.

The adjustment has not been easy. The reform program has been carried out in a very difficult political situation and against strong resistance from some stakeholders. Nevertheless, our authorities have demonstrated strong ownership and political will to implement the program and move forward to a new era. The authorities' efforts to establish a national dialogue, involving many different stakeholders, is a key factor behind their success in advancing major policy initiatives. Additionally, the authorities have always had strong support from multilateral creditors and from the international community.

After just two years in office, our authorities have an outstanding record of restoring macro stability and implementing important structural reforms. Despite severe external shocks, Nicaragua's macroeconomic indicators have continued to improve. Real GDP growth has started to recover, from 1 percent in 2002 to 2.3 percent in 2003, and over the medium term it is expected to average about 5 percent. Prudent policies have kept inflation under control and formal employment has been growing at an annual rate of almost 4 percent. International reserves have surpassed the program targets and the fiscal program is on track.

It is important to note that macroeconomic stability has been achieved and, at the same time, poverty indicators have improved in recent years. As reported in the JSA of the second annual PRSP Progress report, important progress has been made in the implementation of the PRSP. Interim HIPC relief has allowed Nicaragua to significantly increase public spending in social areas. Furthermore, there has been a substantial improvement in the tracking of poverty-reducing expenditures.

Recent developments

a) Domestic debt

Since the last review, further progress has been made in restructuring the domestic debt. In this context, the Central Bank has reduced its outstanding securities during 2003 with a net repayment of by US$70 million. At the same time, it completed the negotiations with the largest holders of bank resolution bonds (CENIs). These agreements allowed the Central Bank to exchange, on a voluntary basis, bonds for new standardized instruments bearing a lower interest rate and longer maturity. The total amount of the bonds falling due in 2003-04 was US$350 million, and the maturity was extended up to 10 years and interest rates reduced from 18-20 percent to approximately 8 percent.

b) Privatization of public utilities

As the staff highlights, Nicaragua has advanced substantially in the implementation of its divestiture program. The international bidding process, which privatized the remaining 49 percent of shares held by the state-owned telephone company (ENITEL), was concluded last December and the closing is expected to be finalized by the end of this week.

Regarding the electricity sector, significant progress has been made in divesting several electricity generating units and in attracting new private investment to expand electricity services. The divestiture of the remaining two power generating units, as agreed with the World Bank and Fund staff, is not advisable at this time since it would create an undesirable concentration of market power and generate financial problems in the power sector.

Our Nicaraguan authorities remain committed to continue strengthening the financial and operational conditions of state enterprises. In the case of the water and sewerage company (ENACAL), the authorities have developed a strategy to improve the efficiency of water and sewerage operations while expanding the coverage of these services. With assistance from the IDB, they will develop a medium-term strategy for improving the overall efficiency of its operations.

c) National Development Plan (NDP)

Our Nicaraguan authorities remain fully committed to the PRSP process and the PRGF-supported program. With a great sense of ownership, they want to incorporate the lessons of two years of implementing the 2001 PRSP into an updated PRSP. Toward this end, authorities have developed a long-term vision for Nicaragua under the NDP, which was well received by donors in the Consultative Group Meeting last October.

The NDP shows the government's commitment to continue identifying actions and reforms needed to achieve higher levels of economic growth. As pointed out in the Consultative Group Meeting, Nicaragua's authorities consider the NDP as the basis toward the updating of their PRSP, which is consistent with the PRGF and incorporates territorial and migration analysis to public policies. The plan was prepared after extensive public consultations with the main stakeholders, through regional workshops. It presents in detail the policies and actions that should be the engine of broad-based economic growth, which is needed in order to reach the country's poverty-reducing goals.

d) Trade

Nicaragua in recent moths has continued actively moving toward trade liberalization and regional integration. Last December, jointly with other three Central American countries, it concluded the negotiations with the U.S. for Central American Free Trade Agreement (CAFTA). In addition to improving trade flows with its largest trading partner, CAFTA is likely to improve the investment climate, increase investment opportunities, and consolidate the regional integration with the other Central American countries. In the medium term, Nicaragua expects CAFTA to be one of the main engines of growth and it should help to "lock-in" trade liberalization and other structural reforms undertaken by Nicaragua under the program.

Governance

For many years, governance has been a major problem in Nicaragua, which has contributed to a lack of trust in public institutions. As the staff notes in the Completion Point Document, the authorities have fully complied with the implementation of key governance strengthening measures. These reforms are: i) the recently approved civil service law that will promote stability, professionalism and continuity in the public sector by reducing political influences in the appointments of civil servants; ii) the new system of management and public procurement; iii) the implementation of the program to modernize the comptroller's office, and iv) the new laws on penal procedures and public prosecutors.

Moreover, one of the main pillars to achieve governance is through the strengthening of the Judicial System. The Government is committed to promote an integral judicial reform focused on achieving independence and depoliticize the Judicial System in Nicaragua. In order to achieve these goals, after having finished the consultation process, our authorities will submit to Congress a project for the Judicial Career Law that will incorporate the adoption of an impartial mechanism for the election of the Judges and Magistrates.

The full scope and depth of the reforms that have strengthened governance and promoted stronger institutions is nicely summarized in Box 3 of EBS/03/177.

Despite these many achievements, Nicaragua's democracy is still young and it requires enhanced dialogue among the different actors in order to move ahead with the required planned reform agenda. Our authorities are committed to continue strengthening the democratic process by promoting broad and transparent dialogue with civil society and intense negotiations with Congress to build consensus. New channels of dialogue and communication have been opened among the government, the different political parties and the rest of the civil society toward attaining the necessary consensus for the approval of the 2004 envisaged program reforms, especially those related to legislation on governance, fiscal sustainability and financial modernization. Recently, this process culminated in a consensus to appoint a new board of directors in Congress, with participation of the different political parties.

Our authorities believe that underneath the political differences in Nicaragua, there is now a better understanding among the main stakeholders for the need to support the economic program and the legislation required to comply with it. Moreover, the Nicaraguan authorities would like to reiterate their commitment to fight corruption and to continue improving governance and transparency in all governmental activities.

Fiscal policy

As stated by the staff, Nicaragua's fiscal program is currently on track. The recently approved 2004 budget was prepared in line with the program and the authorities are aware that achieving long-term debt sustainability requires continued fiscal consolidation. Their medium-term plans include further strengthening of the tax administration, continued streamlining of public expenditures and further improvements in public enterprise management. They recognize that the civil service and pension reforms will have additional costs, which will be included in future budgets and that will need to be offset by additional fiscal measures, including further rationalization of current expenditures.

Financial sector

The authorities recognize the need to continue strengthening the prudential and supervisory framework of the financial sector. They have enhanced prudential norms and banking supervision and they continue working on several reforms of relevant financial sector laws, including legal amendments to grant legal protection to bank supervisors. The authorities will continue working on the implementation of new on-site technical and administrative procedures for banking supervision. They welcome the ongoing FSAP and expect that its recommendations will help them address the remaining vulnerabilities and identify specific actions.

Public sector debt

The authorities agree with the findings of the revised Debt Sustainability Analysis (DSA) included in the Completion Point document. They are committed to continue prudent fiscal and external borrowing policies in order to keep the public debt on a sustainable path. New laws on public debt and fiscal responsibility are designed to strengthen debt management and to ensure that debt sustainability remains a focus of fiscal policy. The authorities continue to rely on highly concessional external loans for financing social infrastructure and they are working closely with the World Bank in the selection of investment projects in order to meet the objectives of the PRSP.

Bilateral negotiations with all the Paris Club creditors to implement the Agreed Minute of December 2002 have been finalized with the exception of Israel. The authorities look forward to a stock-of-debt operation with the Paris Club that will secure the debt relief from this group of creditors as foreseen in the Completion Point Document. The authorities also appeal to non-Paris Club and commercial creditors who have not provided assurances of their participation in the HIPC initiative to do so, as participation from all creditors is crucial for reaching debt sustainability. Specifically regarding commercial debt, the authorities will vigorously seek to reach agreements with the remaining holders of Nicaraguan debt in order to secure their participation. To this end, the authorities welcome the support of the World Bank through the Debt Reduction Facility (DRF) for IDA-only countries to carry out a second buyback operation.

Conclusion

Based on the commitment of the government, the good performance under the PRGF arrangement, the substantial progress in the structural adjustment program as well as in the implementation of the PRSP, our authorities request that the Fund consider the Fourth Review as completed. They understand that they have also met all the conditions for reaching the completion point under the enhanced HIPC initiative.

Our authorities see the HIPC completion point as a major achievement for the Nicaraguan society but going forward they are well aware of the need to continue with sound and ambitious policies if the country is to reach a point along a path of high, equitable and sustained growth.

The task ahead is fraught with difficulties, not least to ensure that a framework of macroeconomic stability leads to persistent gains in real per capita growth. The authorities are openly committed to continue fighting poverty but know that, at the end of the day, only a growing economy will provide sufficient resources to guarantee the widespread improvement in living standards that would go all the way to meet the social aspirations of the population. The NDP and the initiative to move on to a revised PRSP are an attempt to address this challenge. Going forward, Nicaragua' sustained track record of sound policies should help the country attract new investment, both domestic and foreign, and reinforce its tremendous growth potential.

Our authorities are highly appreciative of the advice and recommendations so far given by donors and the Fund, in a spirit of close and effective collaboration, and hope that further support, adapted to the requirements of the growth process, will be available in the future.