

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

NICARAGUA

IDB COUNTRY STRATEGY (2012-2017)

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ABBREVIATIONS

AECID	Spanish Agency for International Development Cooperation
BCN	Banco Central de Nicaragua [Central Bank of Nicaragua]
CABEI	Central American Bank for Economic Integration
CFC	Common Fund for Commodities
CNHHN	National Council Twinning Nicaragua and the Netherlands
CRI	Cash recovery index
DSF	Debt Sustainability Framework
EBITDA	Earnings before interest, taxes, depreciation, and amortization
ECLAC	Economic Commission for Latin America and the Caribbean
EIB	European Investment Bank
ENATREL	Empresa Nacional de Transmisión Eléctrica [National Electricity Transmission Company]
ENDESA	Demographic and Health Survey
ENEL	Empresa Nicaragüense de Electricidad [Nicaraguan National Electricity Company]
FAO	Food and Agriculture Organization
FDI	Foreign direct investment
FOMAV	Fondo de Mantenimiento Vial [Road Maintenance Fund]
GCI-9	Ninth General Increase in the Resources of the Bank
GEF	Global Environment Fund
IAEA	International Atomic Energy Agency
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
INE	Instituto Nicaragüense de Energía [Nicaraguan Energy Institute]
INIDE	Instituto Nacional de Información de Desarrollo [National Development Information Institute]
INSS	Instituto Nicaragüense de Seguridad Social [Nicaraguan Social Security Institute]
IOM	International Organization for Migration
IRI	International Roughness Index
JICA	Japan International Cooperation Agency
KEXIM	Korean Eximbank
LAIF	Latin America Investment Facility
MHCP	Ministry of Finance
MINSA	Ministry of Health
MOSAFC	Modelo de Salud Familiar y Comunitaria [family and community health model]
MSBs	Microenterprises and small businesses
MTI	Ministry of Transportation and Infrastructure
NCB	National competitive bidding
NDF	Nordic Development Fund
NSG	Non-sovereign guaranteed

NTCI	Normas técnicas de control interno [Internal control technical standards]
ODA	Official development assistance
OEI	Organization of Ibero-American States
OMJ	Opportunities for the Majority
OPEC	Organization of the Petroleum Exporting Countries
PAHO	Pan American Health Organization
PGEAOD	Plan para la Gestión Estratégica de la Ayuda Oficial al Desarrollo [Official Development Assistance Strategic Management Plan]
PNDH	Plan Nacional de Desarrollo Humano [National Human Development Plan]
SG	Sovereign guaranteed
SILAIS	Sistema Local de Atención Integral de Salud [local comprehensive health care system]
SIVIN	Sistema Integrado de Vigilancia de Intervenciones Nutricionales [Integrated System for Nutrition Program Monitoring]
UNCDF	United Nations Capital Development Fund
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFPA	United Nations Population Fund
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
WFP	World Food Programme
WHO	World Health Organization

EXECUTIVE SUMMARY

Economic and social context	Nicaragua's economy grew at an average of 2.8% a year between 2007 and 2011, in line with the Central American average. Progress was made in the social area in terms of reduced levels of poverty and inequality, although significant gaps still exist in rural areas, where 63.3% of the total population lives in poverty and 26.6% in extreme poverty.
Development challenges	The energy and transportation sectors remain the biggest bottlenecks for economic growth. Electricity prices are the highest in Central America and the service's national coverage is low. Nicaragua has the lowest road density in Central America and only 27.5% of the national network is in good condition. The incidence of poverty in rural areas highlights the need for actions to raise the population's income and improve access to social services in these areas.
Sector priorities	The Bank's country strategy for the period 2012-2017 ¹ will focus on the following sectors: (i) energy; (ii) transportation; (iii) health; and (iv) comprehensive care in early childhood. The strategy will pay particular attention to rural zones in which poverty is concentrated and where there is potential to develop production chains. The strategy sectors will take into account gender, diversity and climate change-related issues, where applicable. The Bank will also continue supporting efforts to strengthen country financial administration and public procurement systems. For their part, the private sector windows will support the priority sectors of energy, health, and transportation, this latter through public-private partnerships.
Lending framework	The base-case financial scenario assumes that the allocation of resources from the Fund for Special Operations (FSO), and its blend with Ordinary Capital resources remains the same as the allocation approved for the two-year period 2011-2012 (i.e. a 50/50 mix), with annual allocations of US\$171.2 million. The Bank's share of multilateral debt will drop slightly towards the end of the Strategy period, from 46.1% in 2012 to 45.7% in 2017.
Main risks	The main risks for implementation of the strategy are: (i) macroeconomic, linked to fiscal sustainability and external shocks; (ii) institutional, relating to the executing capacity of local counterparts; (iii) financial, linked to a reduction in the bilateral sources of financing; and (iv) risks deriving from the possible occurrence of natural disasters.

¹ This country strategy will be in force from its approval by the Board of Executive Directors until December 2017.

I. COUNTRY CONTEXT

- 1.1 Nicaragua's economy grew at an average of 2.8% a year between 2007 and 2011, in line with the Central American average. This growth was led by the export sector and increases in foreign direct investment (FDI).^{2,3} Nicaragua has also made progress towards consolidating a stable macroeconomic framework, and has made efforts to reduce the fiscal deficit. Between 2007 and 2011 the average consolidated public sector fiscal deficit was 0.8% of gross domestic product (GDP),⁴ and the level of government debt dropped from 82% of GDP in late 2007 to 71.8% of GDP at the end of 2011.⁵
- 1.2 In the social area, poverty fell by six percentage points and extreme poverty by three percentage points between 2005 and 2009.⁶ As regards inequality, the country has seen a slight drop in its Gini coefficient—measured in spending terms—from 0.41 in 2005 to 0.37 in 2009. This change, although positive, remains insufficient given the prevalence of poverty, particularly in rural areas (63.3%), where the level is more than twice that of urban areas. In the case of extreme poverty, the disparities are wider still, with an extreme poverty rate of 26.6% in rural areas and 5.6% in urban areas.
- 1.3 The analysis suggests that the main obstacles to Nicaragua's achieving faster economic growth remain the state of its infrastructure, in particular energy and transportation infrastructure, together with microeconomic risks.⁷ The electricity sector stands out as having the highest electricity prices in Central America, with low service coverage, both nationally (74.6%)⁸ and in rural areas,⁹ and sustainability risks that are both financial, relating to its rate system,¹⁰ and operational. The main

² Despite the growth rate in recent years, faced with a fresh international crisis the economy might be affected either through its links to other economies or through other types of external shocks.

³ According to PRONICARAGUA, FDI was equivalent to 13.3% of GDP in 2011.

⁴ Ministry of Finance (MHCP). "Marco Macroeconómico al Mediano Plazo" [Medium-term macroeconomic framework], several years.

⁵ Banco Central de Nicaragua (BCN). "Informe de Deuda Pública de Nicaragua, IV Trimestre 2011" [Government debt report, Nicaragua. Q4 2011].

⁶ Poverty stands at 42.5% and extreme poverty at 14.6%. (INIDE), data to 2009.

⁷ The microeconomic risks are factors such as uncertain property rights that could drive up the operating costs of companies or reduce the likelihood of companies being able to fully receive the economic returns on their investment. (For more information on the methodology and the study's findings, see "Una Actualización del Diagnóstico de Crecimiento" [Update on the diagnostic assessment for growth], Inter-American Development Bank, 2012.)

⁸ Economic Commission for Latin America and the Caribbean (ECLAC). "Centroamérica: estadísticas del subsector eléctrico" [Central America: Electricity Subsector Statistics], 2010.

⁹ In 2005 electricity coverage was under 40% in rural areas, whereas it reached 92% of urban areas. (INIDE).

¹⁰ The regulator estimated that the average real increase in electricity rates in 2012 should be 20.2%. However, the authorities considered this increase would have a serious impact on the economy and limited it to 9%, making up the difference with subsidies.

challenge in the transportation sector is the low coverage of the road network,¹¹ particularly in rural areas.¹² Alongside these constraints, the concentration of poverty in rural areas suggests the need to promote actions to include rural small producers in productive chains that increase their income and the value added of their production.

- 1.4 The levels of poverty and inequality mentioned above reflect the need to improve social services in poor rural areas. There are significant gaps in access¹³ to quality basic health services in extremely poor regions, challenges in terms of maternal and infant mortality, and problems of chronic malnutrition, which affect 18% of children ages 0 to 5 countrywide, having an impact on their cognitive development as well as their health, together with a rapid rise in noncommunicable diseases.¹⁴
- 1.5 Nicaragua's new National Human Development Plan (PNDH) for 2012-2016¹⁵ is focused on three main areas: economic growth, infrastructure for development, and social development. These will serve as the framework within which to set sectoral public policies over the next four years. The plan pays special attention to reducing poverty and implementing social and economic programs that contribute to this aim, such as Programa Amor [Program of Love] and Hambre Cero [Zero Hunger].

II. THE IDB IN NICARAGUA

- 2.1 Between 2008 and 2011 the Bank consolidated its position as Nicaragua's most important multilateral cooperation agency,¹⁶ with total approvals of US\$579 million and total disbursements of US\$555 million. The IDB Group's share of loans to the public sector went from 45% in 2007 to 60% in 2011. Including grants, the IDB's share rose from 17% in 2007 to 31% in 2011. At the end of 2011, the country's total debt with the Bank came to US\$967.7 million, representing 23.8% of public external debt and 46.9% of multilateral external debt.

¹¹ Nicaragua has the lowest road density in Central America (181.37 km/1,000 km²). What is more, road quality is poor, as only 23% of the national network is in good condition.

¹² Unpaved roads account for 86.68% of the total national road network. Ministry of Transportation and Infrastructure (MTI). "Red Vial Nicaragua 2011."

¹³ Nationally the number of physicians per 1,000 inhabitants is less than one, and the number of nurses is lower still, as the ratio is 1.7 physicians per nurse. This ratio is the inverse of what international evidence suggests is desirable.

¹⁴ Diabetes mortality has risen five-fold from 5.6 per 100,000 inhabitants in 1990 to 28.5 in 2010.

¹⁵ The PNDH 2012-2017 is currently being prepared and is due to be presented in late 2012.

¹⁶ In 2011 the country's debt to the IDB represented 46% of its total multilateral debt, compared with the World Bank's 23% and the Central American Bank for Economic Integration's 13%. The World Bank focuses its activities on health-care; urban production (MSBs); water and sanitation; education; and the Caribbean Coast. The Central American Bank for Economic Integration (CABEI) is present in the energy, foreign trade, transportation, housing, and rural production sectors.

- 2.2 Over this same period, the Bank was the leading multilateral organization in multiyear/multidonor initiatives¹⁷ in the energy and transportation sectors, this being a form of financing that allows both donor coordination, and greater lending capacity; this is expected to continue in this strategy.
- 2.3 The currently available balance in the active sovereign guaranteed (SG) loan portfolio,¹⁸ distributed across 12 sectors, 19 executing units, and 31 operations totals US\$367 million, concentrated in energy (27%), transportation (11%), health and social protection (17%), water and sanitation (12%), and environment, rural development and natural disasters (18%).¹⁹ The Bank's non-sovereign guaranteed (NSG) portfolio totals US\$84.9 million, US\$28.5 million corresponding to operations by the Structured and Corporate Financing Department (SCF), US\$16.2 million to the Multilateral Investment Fund (MIF), and US\$39.9 million to the Inter-American Investment Corporation (IIC).²⁰ The Opportunities for the Majority (OMJ) window has total approvals of US\$15 million.

III. THE BANK'S STRATEGIC PRIORITIES FOR 2012-2017

- 3.1 The strategy's objective is to promote Nicaragua's inclusive social and economic development through initiatives enabling the main challenges to growth as regards infrastructure to be overcome, and the urban-rural divide in terms of poverty and access to services to be narrowed. To do so it will promote a comprehensive approach that aims to achieve: (i) improvements in basic health conditions and early childhood care by expanding and improving services; and (ii) improving basic productive infrastructure, particularly in the energy and transportation sectors. Moreover, support will be given to efforts to build local counterparts' institutional capacities, better target spending, and adapt the sector frameworks to facilitate investment implementation and sustainability.
- 3.2 To achieve tangible results, the strategy targets those sectors in which the greatest impact²¹ can be achieved and takes into account the areas of action of the World Bank and other donors.²² Based on these elements and the policy dialogue with the country, the strategy focuses on the following sectors: (i) energy; (ii) transportation;

¹⁷ The multiyear and multidonor programmatic financing scheme refers to medium-term projects in sectors with high resource demand in which two or more cooperation funding agencies take part.

¹⁸ Data as of 30 June 2012.

¹⁹ The remaining 15% corresponds to operations in the housing, fiscal, institutional capacity of the State, capital markets, and integration sectors.

²⁰ SCF is supporting initiatives in the energy and agroindustry sectors, and supporting Nicaraguan banks through Trade Finance Facilitation Program (TFFP) credit lines; the MIF has an active portfolio of support for micro and small businesses in the agroindustry, renewable energy, tourism, and water and sanitation sectors; and support is being given through the IIC to the manufacturing and agroindustry sectors; lastly, OMJ is supporting low-income housing and basic community infrastructure initiatives.

²¹ Selection of these sectors took into account findings on the main growth constraints, poverty conditions, execution capacity, and the Bank's experience and positioning.

²² For more information, see Annex IV on cooperation agency coordination.

(iii) health; and (iv) comprehensive early childhood care.^{23,24} In addition, the Bank will deepen its dialogue with the country in the housing, water and sanitation, and rural development/value chains sectors. In the latter area, the Bank will work to identify a multisectoral approach based on strengthening value chains of rural origin, by increasing the value added of production and inclusion of small producers, in order to boost their incomes.

A. Priority sectors

1. Energy

- 3.3 The main medium-term challenges include improving the financial and operational sustainability of the electricity sector by strengthening the sector framework and building the management capacities of the entities concerned. High energy costs threaten sector's financial sustainability. These costs are partly due to: (i) substantial losses of electricity from the system, with the highest loss rates in Central America;²⁵ and (ii) the high proportion of fossil fuels in the electricity matrix, currently accounting for 66% of total generation. Additionally, rates have been changed in a context of weak institutional management, based on economic transfers between generating and distributing entities to overcome the high electricity prices, in conjunction with the approval of subsidies and the high level of losses. This has caused a deterioration in the sector's financial situation, resulting in a deficit. These problems affect coverage and the reliability of supply. In terms of coverage, Nicaragua has the lowest index²⁶ in Central America, at 74.6% in 2010,²⁷ compared to a Central American isthmus average of 87% that year. This situation is more pronounced in the country's rural areas.²⁸ As regards service reliability,

²³ The targeted sectors are aligned with the National Human Development Plan 2012-2016. Moreover, the strategy will support the achievement of the Bank's priorities defined in the Ninth General Increase in the Resources of the Bank (GCI-9). The total amount in the operations approved during the strategy will contribute to meeting the lending target for "small and vulnerable countries." Interventions in the areas of health, comprehensive early childhood care, and energy could contribute to "poverty reduction and equity enhancement." Operations in the energy sector are expected to help meet the "climate change, sustainable energy and environmental sustainability" target. Finally, it is envisaged that the subjects of "regional cooperation and integration" will be addressed by operations in the energy and transportation sectors.

²⁴ The private sector windows will support priority sectors in health, energy (see footnote 31), value chains of rural origin, and transportation (which will be supported through public-private partnerships); as well as the areas currently addressed in the portfolio.

²⁵ According to the Instituto Nicaragüense de Energía [Nicaraguan Energy Institute] (INE), losses in 2010 amounted to 24.1%.

²⁶ The electricity coverage rate is the number of homes with access to electricity as a proportion of the total number of homes, expressed as a percentage.

²⁷ Economic Commission for Latin America and the Caribbean (ECLAC). "Centroamérica: estadísticas del subsector eléctrico 2010" [Central America: Electricity Subsector Statistics 2010], 2011.

²⁸ The low electricity coverage rate is particularly pronounced in rural areas. In 2005 the electricity system covered less than 40% of rural areas, whereas it reached 92% of urban areas. (INIDE), 2005 Census.

although the number of disconnections a year has been reduced,²⁹ there are still areas for improvement in the transmission system.

- 3.4 In the case of private investment, although a regulatory framework is in place, there are still aspects that need to be incorporated or improved in order to expand private participation in the energy matrix and promote diversification of energy sources.³⁰ Lastly, Nicaragua's participation in the Regional Electricity Market remains incipient, requiring additional efforts regarding energy imports and exports. For example, in 2010 exports came to 43.3 GWh and imports to 10.2 GWh, equivalent to 1.3% and 0.3% of net energy generated in the National Interconnected System, respectively.
- 3.5 The Bank's involvement in the energy sector aims to support the sectoral framework's adaptation to ensure its financial and operational efficiency and sustainability. This will help support the country's expansion of electricity coverage, improve the reliability and efficiency of supply, and increase the share of electricity generated from renewable energy sources. Actions to strengthen the sector framework for the Regional Electricity Market will also be supported.
- 3.6 Subject to the achievement of progress on the sector framework,³¹ the Bank will consider investments in intervention areas aiming to: (i) improve the financial and operational management of the system, and reduce energy losses; (ii) expand electricity service coverage, particularly in rural areas; (iii) improve the service's reliability; and (iv) transform the energy matrix to increase the share of renewable sources, as essential conditions to reducing energy costs and thus overcoming one of the constraints on the country's growth. The private sector windows will aim to finance energy generation and renewable energy investments.
- 3.7 The main risks these interventions face are: (i) delays in implementing changes to the sector framework that hinder the Bank's making investments in the sector; (ii) financial and operational management problems affecting entities in the sector that slow the implementation of reforms; and (iii) the absence of an effective mechanism to reconcile rates and reduce prices paid by end consumers. To mitigate

²⁹ Between 2006 and 2010 the number of disconnections a year fell from 220 to 125. Source: Empresa Nacional de Transmisión Eléctrica [National Electricity Transmission Company] (ENTATREL). "Presentación Evolución del Sector Eléctrico, Diagnóstico del Sistema Nacional de Transmisión y Requerimientos Futuros" [Presentation of Developments in the Electricity Sector, Diagnostic Assessment of the National Transmission System and Future Needs], 2011.

³⁰ The topics to consider include: reconciliation of distribution companies' and generators' shares of the charges; use of calls for tender on generation offering a transparent framework for investors; and implementing regional integration agreements that facilitate energy exports.

³¹ New SG and NSG investment operations in this sector will be subject to progress on indicators relating to the strategic objective of strengthening the sector framework to ensure financial sustainability and attract private investment: (i) ENEL's EBITDA margin: progress will be evaluated in 2014 and the value must be above 8%; (ii) ENATREL's EBITDA margin: progress will be evaluated in 2014, and the value must be over 1.6%; (iii) cash-recovery index of distribution companies DISSNORTE and DISSUR: progress will be evaluated in 2014 and the value must be above 75.9%; (iv) system's percentage of total losses: progress will be evaluated in 2014 and the value must be below 23.3%.

these risks, the Bank will provide technical and institutional strengthening support to accompany its operations, and will promote multiyear/multidonor financing mechanisms that, together with the IDB Group's support for private initiatives in the generation sector, will foster diversification of financing sources.

2. Transportation

- 3.8 Nicaragua has the lowest road density in Central America, with 181.37 km/1,000 km², compared to a regional average of 397.59 km/1,000 km². Moreover, just 27.5% of the basic paved highway network³² is in good condition,³³ and just 9.4% of the unpaved road network is in good condition. Access to good quality highways is more limited in rural areas than in Managua and other urban centers. In Managua and the Pacific region, 60% to 80% of all households have access to paved roads/highways, whereas in the Atlantic and Central regions, the proportion is 10 and 40 percent, respectively. Poor road conditions, particularly in the case of unpaved roads, are an active barrier to the country's development. This is especially true in rural areas, as they affect farming, which in 2011 represented 18.8% of GDP³⁴ and it limited the development of production chains in these areas.³⁵ What is more, the lack of rural connectivity restricts access to social services and helps perpetuate rural poverty. Studies suggest that households with access to rural roads are five times less likely to be living in poverty than those without.³⁶ The sector also faces institutional challenges in technical and management areas that are holding back the design and execution of works. Enhancing the technical capacity of the Ministry of Transportation and Infrastructure (MTI) is therefore a medium-term challenge. Additionally, the sector's budgetary allocations are limited, for example, in 2011 the MTI budget

³² Network defined by the MTI for the purposes of direct maintenance, rehabilitation, etc. In 2011 the basic national highway network totaled 7,985.25 kms. Source: MTI. "Red Vial de Nicaragua 2011" [Nicaragua's Highway Network 2011].

³³ The classification includes the values good and very good. The MTI uses the International Roughness Index (IRI) to define the state of a paved road. According to the 2011 report on Nicaragua's highway network, the state of paved roads in terms of IRI (m/km) is defined thus: very good, 2-3; good, 3-4.5; average, 4.5-8; poor, 8-12; very poor, 12 or higher. The state of unpaved roads, in IRI terms (m/km), is defined thus: very good, 7-9; good, 9-13; average, 13-18; poor, 18-22; very poor, 22 or higher.

³⁴ BCN. Statistical Yearbook. Real Sector.

³⁵ Auguste and Manzano highlight that gaps in rural infrastructure, in terms of both roads and production, do not allow a dynamic process of competitive and flexible market access. They therefore see the need to increase and improve access by productive sectors to roads and highways of all types. Auguste and Manzano. "¿Tiempo de Cosecha?" [Harvest Time?], Inter-American Development Bank, 2012.

³⁶ ECLAC/IDB/FPRI. "Nicaragua: Análisis del Impacto de los Servicios de Infraestructura y las Condiciones de Vida en las Zonas Rurales" [Nicaragua: Analysis of the Impact of Infrastructure Services and Living Conditions in Rural Areas], 2011.

accounted for just 1.8% of GDP, which was insufficient to increase road density, improve roads or provide highway network maintenance.³⁷

- 3.9 The objective of the Bank's involvement in the sector is to support efforts to build, improve, and rehabilitate highways and rural roads and keep them in a good state of repair, so as to ensure productive sectors have access at all times to both domestic and export markets, with particular emphasis on the Meso-American region. The Bank will therefore support: (i) road network investments linking rural centers of production with the main corridors and border posts, interconnecting regions, and ensuring roads are passable all year round; while also facilitating the poor population's access to social services; (ii) institutional strengthening of the MTI and the FOMAV in terms of their technical, management and administration, with particular emphasis on the design of works to ensure efficiency, improved execution capacity, particularly in the administration of design, construction, and supervision contracts, together with program monitoring and evaluation. Given that the sector's needs are extensive and exceed the capacity of the public sector, public-private partnership initiatives will be explored to identify possible investments in this framework.³⁸
- 3.10 Achieving these physical targets could be affected by: (i) possible increases in input costs; (ii) the limited number of private companies; and (iii) the occurrence of natural disasters damaging infrastructure, which are the main risks identified. The Bank will continue building the MTI's and FOMAV's management capacities to develop execution arrangements taking into account the challenges in their institutional capacity and allow progress to be made on works; and will take into account in its projects, actions to adapt and reduce vulnerability to climate change.

3. Comprehensive early childhood care

- 3.11 Nicaragua's children, particularly those living in rural areas, face major poverty-related challenges. As many as 49.9% of children ages 0 to 6 are extremely poor and suffer from high rates of malnutrition and cognitive delays. This is a consequence of the poor population's limited access to early childhood care services.³⁹ Although the country has been running the "Amor para los Más Chiquitos" [Love for the Littlest Ones] program since 2010, which focuses on providing comprehensive early childhood care, service delivery gaps persist,

³⁷ The Road Maintenance Fund (FOMAV), which is the agency responsible for maintaining the basic highway network, has a deficit of approximately 50% of the resources it needs to maintain all of the maintainable road network.

³⁸ The current legal framework (Constitution of the Republic, Article 105, and Law on the Concession of Road Works, Law 264, 1997) envisages the possibility of investing in road works through concessions financed from tolls or subsidized by the State. In particular, the Law on Concessions allows private companies, whether domestic, foreign or mixed, to build, maintain, rehabilitate, improve, rebuild, and operate road works and their related facilities.

³⁹ Distance is one of the main reasons why the poor do not visit centers.

especially in areas of high vulnerability,⁴⁰ which are compounded by budgetary restrictions and government agencies' limited execution capacity. Service coverage for children ages 0 to 3 years reaches just 7.6% of the total population in this age group.⁴¹ The quality of interventions suffers from deficiencies in care protocols, infrastructure and human resource capacities, along with shortcomings in the adaptation of the services to the needs of indigenous and Afro-descendant groups. Public spending on early childhood is low and not well targeted. Investment in early childhood in 2011 accounted for just 1.13% of central government spending, and recent studies show that 58% of children served by the Programa Amor were not poor.⁴² Bearing in mind that emotional, cognitive, and nutritional lags are prevalent from a very early age in Nicaragua, particularly in rural and urban fringe areas, and that the coverage of comprehensive services is particularly low, the most appropriate strategy combines frequent home visits backed up with effective referral to community health and nutrition promotion.

- 3.12 The Bank's involvement in this sector aims to improve access and increase the use of comprehensive early childhood⁴³ services in areas of high social vulnerability, by: (i) expanding coverage and diversifying quality comprehensive services for early childhood; (ii) strategic and institutional strengthening of the early childhood welfare system.
- 3.13 The risks identified in this sector concern: (i) a possible lack of coordination between entities entrusted with promoting comprehensive services for the 0-3 year age group; and (ii) possible budgetary restrictions in the sector affecting service coverage and quality. To mitigate these risks, the Bank will accompany its actions with efforts to promote an interagency dialogue to facilitate coordination of activities in the sector, and technical support on monitoring the quality of the services delivered.

4. Health

- 3.14 The rate of chronic child malnutrition in Nicaragua is 22.6% in rural areas compared to 12.3% in urban areas. As regards infant mortality, neonatal mortality has remained unchanged since 2001, causing 73% of infant deaths in 2008. Similarly, maternal mortality remains above the average for Latin America and the Caribbean, particularly in rural areas and areas with scattered populations.⁴⁴

⁴⁰ Areas of extreme poverty and highly dispersed populations are defined as vulnerable (i.e. those in rural and urban fringe areas).

⁴¹ INIDE. Standard of Living Survey (EMNV) 2009.

⁴² Idem.

⁴³ Focused particularly on the thousand day window. The first 1,000 days include the nine months of pregnancy and the first two years of life.

⁴⁴ Local comprehensive health care systems (SILAIS) in rural and sparsely populated areas still have maternal and perinatal mortality rates well above national averages. They also have a great proportion—between 20% and 30% higher—of causes relating to maternal and perinatal health, nutritional deficiencies, and communicable diseases.

Regarding the rate of teenage pregnancies in Nicaragua, 25.4% of pregnancies in 2011 were among women ages 15 to 19,⁴⁵ which is above the average for Latin America and the Caribbean (18%).⁴⁶ Risk factors also exist relating to noncommunicable chronic/degenerative diseases, particularly overweight and obesity, which are increasing rapidly, particularly among women of childbearing age.⁴⁷ These issues represent the country's most serious health problems and are primarily due to limited care availability and serious coverage gaps, reflecting inequities in access and uneven service quality. The lowest levels of coverage are found in rural areas where the population is more scattered and service utilization is low.⁴⁸ Coverage is particularly low in the Caribbean region and the Central macroregion, with levels of exclusion of over 90%, compared with 57.7% nationally.

- 3.15 Challenges also persist in the case of human resources, infrastructure, and technology. The density of physicians is low, at less than one per 1,000 inhabitants. This situation is even worse on the Caribbean Coast and in the Center-North zone, where there is an even bigger shortfall in numbers of medical practitioners per inhabitant.⁴⁹ As regards infrastructure, although the Ministry of Health (MINSa) care network has grown by 15.8% over the last five years (rehabilitation and building of health units), there are still population centers in the Center-North and Atlantic regions lacking access to a primary unit. The quality of care is low, particularly in terms of the correct application of care protocols. An audit in 2011 on eight local comprehensive health care systems (SILAIS) revealed that only 47% of basic perinatal clinical records were completed in compliance with standards.⁵⁰ This is one of the other challenges to be tackled in the medium term. Since 2008 the country has been implementing the family and community health model (MOSAFC),⁵¹ which emphasizes grassroots health promotion activities, and family

⁴⁵ MINSa. "Informe de Gestión 2011" [Management report].

⁴⁶ WHO. "Boletín de la Organización Mundial de la Salud" [World Health Organization Bulletin], volume 87, 2009.

⁴⁷ Over half of the population is overweight, with a body mass index (BMI) of over 25 kg per m², and 28.8% of women are obese. The fact that women are disproportionately affected is related to the prevalence of undernourishment during childhood, which results in short stature, combined with early and multiple pregnancies, and unhealthy eating habits.

⁴⁸ Coverage of prenatal checkups is below the national average in half the municipios of the three SILAIS in Jinotega, the Autonomous Region of the North Atlantic, and Matagalpa, which are among the most rural.

⁴⁹ Matagalpa, the Autonomous Region of the North Atlantic, and Jinotega are the SILAIS with the biggest deficits, with 0.25 nurses per thousand inhabitants in Matagalpa (vs. 0.52 nationally) and 0.5 physicians per thousand inhabitants (vs. 0.85 nationally).

⁵⁰ GESAWORLD. MINSa performance audit, 2009 and December 2011 reports.

⁵¹ As a model of care, MOSAFC takes an integrated network approach, emphasizing strengthening clinical and management mechanisms to integrate service network levels, and thus foster improvements and in quality and longitudinality of care.

- health registration and assessment,⁵² and gives priority to ensuring essential health care services reach more vulnerable areas and families.
- 3.16 The Bank's involvement in the sector will be aimed at improving maternal, neonatal, and perinatal health, reducing risk factors for chronic degenerative conditions (in particular obesity), and cutting child malnutrition, in particular chronic malnutrition among children under 3. It envisages (i) investments in the MOSAFC regarding health care infrastructure and equipment; prevention and health promotion, efficiency of spending focused on caring for vulnerable population groups,⁵³ together with support for the Amor para los Más Chiquitos program in the field of chronic child malnutrition among children ages 0 to 3; (ii) improving quality assurance mechanisms by strengthening human resources and using communication technologies to support the service. Synergies with the private sector will also be sought in the area of improvements to service delivery capacity, particularly in the case of hospital infrastructure investments and human resource training.
- 3.17 The main risks identified concern: (i) possible problems prioritizing investments, in a context of limited resources; and (ii) difficulty introducing changes in the design and evaluation of the interventions that allow for improvements in quality and effectiveness. Mitigating these risks will require building MINSA's management capacities, promoting quality measurement and outcome evaluation systems, coordinating actions with other cooperation agencies, and enhancing public-private partnership so as to increase the financing available to the sector.
- B. Crosscutting action areas**
- 3.18 Three sectors in the strategy will be crosscutting all interventions: (i) climate change vulnerability reduction, adaptation and mitigation; (ii) gender; and (iii) diversity. Specifically, in the transportation and energy sectors, a vulnerability reduction and climate change adaptation focus will be applied to the design of road systems and renewable energy. A gender and diversity perspective will also be incorporated in the health care and comprehensive early childhood care where possible. The mechanisms of inclusion of these areas in the Bank's programs and initiatives will be defined during strategy implementation.

IV. LENDING FRAMEWORK

- 4.1 **Fiscal and external debt situation.** The ratio of government debt to GDP has dropped from 195.6% in 2003 to 71.8% in 2011 owing to debt relief and efforts to reduce the fiscal deficit, combined with the country's economic growth. The central government deficit, after grants, decreased from 2.5% of GDP in 2009 to 0.6% in

⁵² Health promotion strategy that includes house-to-house visits to ascertain and classify families' health profile and risk level and use this information to prioritize follow up of each family by MINSA.

⁵³ Areas of extreme poverty and highly dispersed populations are defined as vulnerable (i.e. those in rural and urban fringe areas).

2010, turning into a surplus of 0.7% of GDP in 2011. The consolidated public sector shifted from a deficit of 3.1% of GDP in 2009 to a surplus of 0.1% in 2011.⁵⁴ The central government aims to keep close to a balanced budget over the medium term, while the consolidated deficit will remain below 2% of GDP.

- 4.2 **Borrowing needs and financial scenario.** The country's gross borrowing requirement will total US\$1.273 billion over the period 2013-2015.⁵⁵ The Bank will provide approximately 42% of this and 27% of capital expenditure. The base-case scenario assumes that during the period covered by the strategy the allocation of resources from the Fund for Special Operations (FSO), and its blend with Ordinary Capital resources (a 50/50 blend) remains the same as the allocation approved for 2011-2012. This scenario projects approvals of US\$856 million over the period 2013-2017.⁵⁶ IDB debt will grow slightly as a share of external government debt, and IDB debt as a ratio of GDP will rise from 14.1% in 2012 to 18.2% in 2017. The financial scenario presented in Table 1 is consistent with a Debt Sustainability Analysis⁵⁷ based on the Debt Sustainability Framework (DSF). According to the debt sustainability model, the risk of external public debt distress is moderate, as classified by the DSF.⁵⁸

⁵⁴ MHCP and International Monetary Fund, Article IV.

⁵⁵ MHCP. "Marco Presupuestario de Mediano Plazo 2012-2015." [2012-2015 Medium-term Budgetary Framework].

⁵⁶ The approval levels under this scenario are contingent on the biannual concessional resource allocation exercises (DSF/EPBA, document GN-2442). The FSO allocation in those exercises depends on variables such as population, per capita GDP, and performance in terms of policy and execution of the Bank's portfolio for eligible countries. The 2015-2016 exercise will take into account the results of the update of Nicaragua's national accounts system for 2006, which could change the estimates for Bank lending to the country. A change in the blend of FSO and OC resources for Nicaragua that increases the proportion of OC resources could result in higher levels of approvals than those presented in the lending framework. Such a change in the blend requires Board approval and could be proposed during the biannual allocation period, provided the proposed change is consistent with the Debt Sustainability Framework (DSF) analysis.

⁵⁷ Inter-American Development Bank. Macroeconomic Sustainability Assessment, April 2012.

⁵⁸ This classification is consistent with the conclusions of the sustainability assessment recently carried out by the International Monetary Fund. Nicaragua has consistently maintained this classification since the IDB introduced the DSF in 2007.

Table 1. Overall total financing and flows in relation to the IDB 2012-2017
(US\$ millions)

	2012	2013	2014	2015	2016	2017	2013-2017
Approvals^{1/}	235.4	171.2	171.2	171.2	171.2	171.2	856.0
Disbursements	153.3	167.0	178.9	190.2	204.8	195.8	936.6
Repayments	15.9	17.2	19.6	25.2	31.0	39.2	132.2
Net loan flows	137.4	149.8	159.3	165.0	173.8	156.5	804.4
Subscriptions	2.0	2.0	2.0	2.0	2.0	2.0	10.0
Net capital flows	135.4	147.8	157.3	163.0	171.8	154.4	794.4
Interest and fees	15.8	18.3	20.5	22.5	24.9	27.8	114.0
Net cash flow	119.6	129.5	136.8	140.5	146.9	126.8	680.5
Debt with IDB	1,105.1	1,254.9	1,414.2	1,579.2	1,753.0	1,909.5	
IDB debt/GDP (%)	14.1	15.1	16.0	16.9	17.7	18.2	
IDB debt/external public debt (%)	25.5	26.8	28.0	29.2	30.4	31.2	
IDB debt/external multilateral debt (%)	46.1	45.6	45.5	45.4	45.8	45.7	

^{1/} Amounts subject to the availability of the Bank's finance capital and FSO allocations. Source: IDB.

V. STRATEGY IMPLEMENTATION

- 5.1 **Measures to enhance portfolio execution.** Achievements during the period 2008-2012⁵⁹ were limited by difficulties in project execution, in particular: (i) complex operation designs that were mismatched with the prevailing institutional constraints, impacting on contract award prices and hindering contract administration; (ii) lack of rigor in the budgetary planning exercise (State budget), and lack of correlation between budgets and the plans submitted to the Bank in the annual work plans; (iii) execution of fiduciary processes delaying execution of works; (iv) the need for the Bank to monitor project execution more closely and high staff turnover in the executing units; (v) delays in fulfilling disbursement projections; (vi) limited supply of consulting firms able to meet top international quality standards; and (vii) difficulties in execution processes due to the separation between program design and implementation, affecting portfolio performance.
- 5.2 In light of these difficulties, the Bank will implement the following actions during the strategy period to ensure improved execution of both the portfolio and loans approved in the future: (i) introduction of planning and management by results processes at the level of the executing agency; (ii) budgetary review and participation in decisions on program budgets; (iii) promoting quarterly and semiannual accountability among project teams on the delivery of committed targets and fulfillment of disbursement projections; (iv) sustained support to loan executing units to improve their fiduciary capacities; and (v) adaptation of fiduciary

⁵⁹ Increase in national electricity coverage, from 64% in 2008 to 74% in 2010; approximate reduction in losses by 2% between 2008 and 2010; expansion of road network through the construction and rehabilitation of 500 km of highway; improvements in maternal/infant health care service coverage, by increasing comprehensive health-care services for 12,000 pregnant or breastfeeding women, and provision of micronutrients to 80,000 children to combat chronic malnutrition; construction and rehabilitation of primary hospitals in municipios suffering from extreme poverty and with highly scattered populations.

procedures to local counterpart capacities so as to facilitate fulfillment of program outcome indicators.

- 5.3 **Use of country systems.** The Bank currently utilizes the following country systems for management and supervision of its operations: budget, treasury, accounting and reports,⁶⁰ together with the procurement information system. During the strategy period, for financial administration, the country will be given support in improving its budget and treasury subsystems, in order to increase the operating efficiency of the country's financial administration and hence of Bank-financed operations.⁶¹ Support will also be provided for strengthening the accounting and reports subsystem, to extend its use to the entire portfolio, together with the internal auditing subsystem, to bring it in line with international standards and have it gradually contribute to comprehensive supervision of the operations the Bank finances in the country.⁶² With respect to procurement, the government will receive support in making improvements to the e-procurement system, to expand its scope and functionality.⁶³ The table below summarizes the status of Nicaragua's country systems and anticipated developments during the strategy period.

Table 2. Country systems

Use of country systems ⁶⁴	Baseline 2012	Estimated use in 2017	Planned actions
Financial management			
Budget	100%	100%	Supporting the government in making improvements to the financial administration system.
Treasury	100%	100%	
Accounting and reports	88%	100%	
Internal audits	0%	0%	Supporting the country in strengthening the subsystem—aligning internal control technical standards (NTCI) with international standards (COSO).
External audits	0%	0%	N/A

⁶⁰ The budget, treasury, accounting and reports systems together comprise Nicaragua's financial administration system.

⁶¹ Support for implementation of improvements to the financial administration system.

⁶² The internal audit subsystem needs to be strengthened for potential use of the subsystem. No use targets have yet been set during the country strategy period.

⁶³ These actions are expected to allow for gradual use of the shopping method in Bank-financed operations.

⁶⁴ Use: Percentage of the active portfolio of Bank loans (operations) that are managed using country systems.

Use of country systems ⁶⁴	Baseline 2012	Estimated use in 2017	Planned actions
Procurement			
Information system	100%	100%	Support for implementation of the Framework Agreement ⁶⁵
Shopping	0%	20%	
Individual consultants	0%	0%	N/A
Partial NCB	0%	0%	N/A
Advanced NCB	0%	0%	N/A

- 5.4 **Donor coordination.** The Bank is an active member of cooperation agency's technical roundtables and discussion forums. In particular, it leads the Energy, PRORURAL, and Health technical roundtables. Participation in these forums is expected to continue throughout the strategy period.
- 5.5 During strategy implementation, there will be close coordination with the World Bank, and the IDB will continue to work in coordination with other donors, taking a multiyear/multidonor programmatic lending approach, in the following sectors: (a) Energy: Nordic Development Fund (NDF), Korean Eximbank (KEXIM), Spanish Agency for International Development Cooperation (AECID), Latin America Investment Facility (LAIF), European Investment Bank (EIB), Central American Bank for Economic Integration (CABEI), Japan International Cooperation Agency (JICA), and the OPEC Fund for International Development; (b) Transportation: CABEI, NDF and JICA; (c) Environment and natural disasters: NDF; (d) Urban development and housing: National Council Twinning Nicaragua and the Netherlands (CNHHN) and CABEI; (e) Reform and modernization of the State: World Bank and the European Union; and (f) Social investment: Organization of the Petroleum Exporting Countries (OPEC). In coordination with other donors, the Bank will also continue to promote measures for transparency and improving spending in the programs to support the country.

VI. RISKS

- 6.1 **Macroeconomic risks.** Implementation of the strategy faces two main types of potential macroeconomic risks: (i) external shocks affecting external sustainability and economic growth; and (ii) internal shocks affecting fiscal sustainability. Although Nicaragua's external sustainability has been strengthened over the last decade, the current account deficit remains high by international standards, ranging between 13% and 25% of GDP in recent years. The high cost of oil imports is partly met by funds from Venezuela. Possible changes in the receipt of these flows could have an impact on the balance of payments and force an adjustment in levels of private consumption and investment. Moreover, a global recession could affect

⁶⁵ Through the Framework Agreement mechanism, the Bank could consider its use for procurement under the shopping and national competitive bidding methods for standardized goods.

the country's economic growth. Although Nicaragua has made efforts to improve its fiscal policy, these could be undermined in the medium term if it does not introduce reforms in the social security system or if the country assumes contingent liabilities. The occurrence of the aforementioned shocks could reduce levels of public financing, affecting fulfillment of the scheduled targets in some of the strategy's priority sectors. The Bank will use its macroeconomic monitoring tools to follow the aforementioned risks closely.⁶⁶

- 6.2 **Institutional risks.** The main risk is related to the local counterparts' executing capacity. This could slow the rate of execution and have an impact on portfolio performance. To mitigate this risk the Bank will support institutional strengthening actions to identify new program design and execution arrangements tailored to local capacity. The Bank will also continue working on strengthening Nicaragua's country financial administration and public procurement systems in order to boost program transparency and maximize the impact of its support.
- 6.3 **Financial risks.** The potential reduction in bilateral sources of financing could change flows of funds to the country and increase demand for Bank financing. To mitigate this risk, the Bank's actions have been targeted on a limited number of sectors in which other donors participate, in order to maximize the use of resources.
- 6.4 **Natural disaster risk.** The presence of active volcanoes, high seismic activity, and tsunami risk mean Nicaragua is exposed to a variety of geophysical hazards. The country has high vulnerability indices, associated with environmental degradation and a lack of urban planning programs and weaknesses regarding disaster risk management performance, particularly due to institutional weakness and limited interagency coordination. The occurrence of a natural disaster could affect the achievement of the outcomes proposed in the strategy. Therefore, the Bank will maintain a dialogue with the country in order to identify natural disaster risk mitigation measures based on financial mechanisms such as contingency lines of credit, among other things.

⁶⁶ Under the mandate in the framework of the agreement of the Report on the Ninth General Increase in the Resources of the Inter-American Development Bank, macroeconomic sustainability assessments of borrower countries are being carried out annually.

RESULTS MATRIX⁶⁷

Government priority	Sector	Strategic objective	Expected outcomes	Indicators	Baseline	Indicative target
Ensure the stability and sustainability of the electricity sector, providing an appropriate legal framework for it to perform properly.	Energy ⁶⁸	Strengthen the sector framework to ensure financial and operational sustainability and attract private investment.	Strengthening the sector framework	ENEL's EBITDA margin ⁶⁹	5.4% (2011)	10% (2016)
				ENATREL's EBITDA margin ⁷⁰	-3.3% (2011)	5% (2016)
				Distribution companies' cash recovery index ⁷¹	71.8% (2008)	80% (2016)
				% total system losses ⁷²	25.4% (2010)	21.15% (2016)
Increase national electricity coverage through rural electrification and normalization of electricity service in settlements. Transform the electricity generation matrix, promoting and stimulating investments in projects based on domestically produced renewable sources and developing the transmission system in a harmonized and reliable way.		Increase electricity coverage	Electricity coverage increased	% homes with electricity coverage	74.6% (2010)	85.5% (2016)
		Change the energy matrix by promoting electricity generation from renewable sources and improve service reliability.	Increased electricity generation from renewable sources	% share of electricity generation from renewable sources	34% (2011)	56.4% (2016)
				Improved electricity service reliability	km of transmission lines	2,190 (2011)	2,811 (2016)
		Increase in service reliability through strengthening of transmission system (outage rate = no. outages /year / 100 km)	6.38 (2011)		6.10 (2016)	

⁶⁷ Indicative targets will be revised or replaced, as appropriate, by means of the country programming documents to be developed during the country strategy period.

⁶⁸ New SG and NSG investment operations in this sector will be subject to progress on indicators relating to the strategic objective of strengthening the sector framework to ensure financial sustainability and attract private investment.

⁶⁹ Earnings before interest, taxes, depreciation, and amortization (EBITDA) divided by the company's total revenue. Progress on this indicator will be evaluated in 2014. The value must stay above 8%, and future energy sector investment operations will be contingent on it.

⁷⁰ Earnings before interest, taxes, depreciation, and amortization (EBITDA) divided by the company's total revenue. Progress on this indicator will be evaluated in 2014. The value must stay above 1.6%, and future energy sector investment operations will be contingent on it.

⁷¹ This value is calculated as Energy sold / Energy generated * Energy paid / Energy billed. The average for the companies DISSNORTE / DISSUR will be taken. Progress will be evaluated in 2014, and the value must be above 75.9%.

⁷² Energy losses as percentage of the system total: Progress will be evaluated in 2014, and the value must be below 23.3%.

Government priority	Sector	Strategic objective	Expected outcomes	Indicators	Baseline	Target 2012-2017
Improvement of the highway network to expand access to basic services and the market.	Transportation	Build, improve, and rehabilitate highways and rural roads and keep them in a good state of repair, so as to ensure productive sectors have access at all times to both domestic and export markets, with particular emphasis on the Meso-American region.	Road infrastructure built, improved and maintained, particularly in the case of rural roads and access for producers.	1. Increase in number of kilometers of paved road built (km) ⁷³	3,150.76 km ⁷⁷	4,293.76 km
				2. Increase in national coverage of paved roads (km/km ²). ⁷⁴	0.024 km/km ²	0.033 km/km ²
				3. Increase in the percentage of the basic highway network ⁷⁵ that is in “good” or “very good” condition.	27.5%	48.4%
				4. Increase in number of kilometers of paved road maintained by FOMAV ⁷⁶	3,000 km	3,500 km

⁷³ Corresponds to the national target of extending the paved road network by 1,143 km that is not currently paved. This has been defined by the MTI in accordance with the medium-term budgetary framework. It involves several sources of funding.

⁷⁴ Calculated by dividing the total length of the paved road network by Nicaragua's surface area of 130,737 km². This indicator refers to the GCI-9 results framework (document AB-2764).

⁷⁵ The universe of comparison is the 7,985.25 km of the Basic Highway Network reported by the MTI in “Red Vial 2011.” According to the MTI, the *good* and *very good* state of the paved network corresponds to an international roughness index of less than 4.5m/km. Achieving this target entails refurbishing and maintaining 526 km of the paved network and building 1,143 km of new paved roads.

⁷⁶ This involves several sources of funding.

⁷⁷ The 3,150.76 km correspond to the paved road network. Includes asphalted, cobbled, and concrete surfaced roads (“Red Vial Nicaragua” [Nicaraguan Road Network]. MTI, 2011)

Government priority	Sector	Strategic objective	Expected outcomes	Indicators ⁷⁸	Baseline	Indicative target
Improve maternal, neonatal, and perinatal health.	Health	Help reduce maternal and neonatal mortality, particularly in rural areas of the country.	Maternal and neonatal mortality reduced thanks to access to essential health services.	Percentage of births in units offering emergency obstetric care in the 10 SILAIS presenting highest maternal mortality rates in 2010. ⁷⁹	60%	75%
			Improve use of comprehensive health services (including counseling) by teenagers.	Unmet demand for family planning services among teenagers drops.	19% (2006-2007)	10% (2016)
Reduction in chronic malnutrition among children under 3		Reduce chronic malnutrition among children in the 1,000 day window in poor rural and urban fringe communities.	Chronic malnutrition among children under 3 reduced through use of good quality comprehensive early childhood care services in rural and urban fringe areas.	Percentage coverage of comprehensive health care services for children under 3 in households living in extreme poverty increases, in the universe of the 37 priority municipios for service under the Programa Amor para los Más Chiquitos.	30%	60%
				Chronic malnutrition rate among children ages 0 to 5 in the prioritized areas.	22.6 (2006-2007)	20% (2016)
				Incidence of anemia among children aged under 2 decreases.	10,5% (SIVIN, 2009)	7% (SIVIN 2016)

⁷⁸ During implementation of the Bank's strategy, work will be done on identifying and including gender and diversity indicators in its programs.

⁷⁹ Targeting these SILAIS is appropriate given the need to prioritize attention for areas with widest disparities and inequalities where, consequently, health care services are most limited.

Government priority	Sector	Strategic objective	Expected outcomes	Indicators ⁸⁰	Baseline	Indicative target
Increased home care coverage for children ages 0-3.	Comprehensive early childhood care	Improve access to and use of comprehensive services for early childhood in areas of high vulnerability. ⁸¹	Coverage of monthly home visits by qualified agents to families of children ages 0 to 3 living in high vulnerability communities.	Percentage of children ages 0 to 3 living in high vulnerability communities who have received 12 or more visits complying with care standards over the last year.	TBD ⁸²	80% (2016)

⁸⁰ During implementation of the Bank's strategy work will be done on identifying and including gender and diversity indicators in its programs.

⁸¹ Areas of extreme poverty and highly dispersed populations are defined as vulnerable (i.e. those in rural and urban fringe areas).

⁸² The baseline will be taken when interventions are designed.

MATRIX OF COUNTRY SYSTEMS⁸³

Strategic objectives	Expected outcomes during CS	Indicator	Baseline	Indicative targets	Frequency
Strengthening the country system or subsystem	Country information subsystem (i) strengthened; and (ii) its use at central and municipal level consolidated.	Indicator 5(a) of the MAPS diagnostic	Result of indicator 5(a), score: 1	Result of indicator 5(a) fulfills the classification criteria required for a score of 2.	At the end of the country strategy period
		MAPS indicator 11(a) (information is published and distributed over available media with IT support when feasible)	Results of indicator 11(a), score: 2	Results of indicator 11(a) in Nicaragua comply with classification criteria required to obtain a score of 3.	
		% municipal government entities implementing the use of the information subsystem	0%	At least 30% of the 153 municipal authorities use the subsystem	At the end of the strategy period
	Internal audit subsystem strengthened	Internal control technical standards (NTCI) adapted to international standards	NTCI not adapted to international standards	NTCI adapted to international standards	At the end of the strategy period
Use of country fiduciary systems	Use of the shopping subsystem in the sovereign-guaranteed (SG) loan portfolio	% of the SG portfolio using the shopping subsystem	(a) No diagnostic assessment (b) Intervention following diagnostic assessment of shopping subsystem (c) % of the SG portfolio using the shopping subsystem	(a) Diagnostic assessment carried out (b) Confirmation of fulfillment of possible recommendations deriving from the diagnostic assessment (c) 20% of the portfolio using the shopping subsystem	At the end of the strategy period
	Increase use of the accounting and reports subsystem in the SG loan portfolio	% of the SG portfolio using the accounting and reports subsystem	88% of the SG portfolio using the accounting and reports subsystem on 31-Dec-11	100% of the SG portfolio using the accounting and reports subsystem at end of strategy period	Annual

1/ It is assumed that a PEFA is not conducted in 2012. If one is done, an additional application would be considered at the end of the strategy.

⁸³ Measurable outcome indicators for the strategy period (2012-2017).

MAIN ECONOMIC AND SOCIAL INDICATORS

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Social indicators									
Population (thousands)	5,312	5,380	5,450	5,522	5,595	5,668	5,742	5,815	5,888
Poverty rate	...	...	48.3	...	...	...	42.5	...	...
Extreme poverty rate	...	...	17.2	...	...	...	14.6	...	...
Unemployment rate	7.0	6.5	5.6	5.2	5.9	6.1	8.2	7.8	6.3
GDP per capita (US\$)	772	830	894	947	1,012	1,124	1,082	1,133	1,239
Real sector indicators									
Real GDP (% growth)	2.5	5.3	4.3	4.2	3.6	2.8	-1.5	4.5	4.7
Nominal GDP (US\$ millions)	4,101	4,465	4,872	5,230	5,662	6,372	6,213	6,591	7,297
Fiscal indicators ^{1/} (% of GDP)									
Tax revenues	21.6	20.0	21.8	22.9	23.4	22.3	21.1	21.9	23.1
Tax expenditures	24.1	22.4	22.5	23.0	22.8	22.8	23.6	22.6	22.4
Capital expenditures	8.6	9.6	9.5	7.4	7.4	6.1	5.6	5.4	5.1
Overall balance	-2.5	-2.5	-0.7	-0.1	0.6	-0.5	-2.5	-0.6	0.7
Government debt	197.2	152.7	139.3	112.1	82.2	74.8	80.1	78.0	71.8
External debt	160.8	120.7	109.8	86.5	59.8	55.1	58.9	58.8	55.8
External indicators (% of GDP unless stated otherwise)									
Current account balance	-17.2	-15.4	-16.1	-16.2	-21.6	-23.7	-12.5	-13.4	-17.8
Foreign direct investment	4.9	5.6	4.9	5.5	6.7	9.8	7.0	7.7	13.3
Remittances	10.7	11.6	12.6	13.3	13.1	12.8	12.4	12.5	12.5
Gross international reserves (millions of US\$)	504	670	730	924	1,103	1,141	1,573	1,799	1,892
Monetary and exchange rate indicators									
Inflation rate (end of period)	6.5	9.3	9.6	9.4	16.9	13.8	0.9	9.2	8.0
Growth of monetary aggregates (M2)	12.2	14.3	9.4	9.0	17.8	8.4	10.4	24.7	9.4
Nominal exchange rate (average)	15.11	15.94	16.73	17.57	18.45	19.37	20.34	21.36	22.42
Real effective exchange rate (+ depreciation)	95.3	99.1	100.0	99.5	101.7	98.0	89.5	95.8	99.9

1/ Fiscal data are for the central government. Public debt data are for the public sector.

Source: Central Bank of Nicaragua (BCN), Ministry of Finance (MHCP) and National Development Information Institute (INIDE).

INDICATIVE LENDING FRAMEWORK

Borrowing requirement. The country's gross borrowing requirement will total US\$1.273 billion over the period 2013-2015.⁸⁴ The Bank will meet approximately 42% of this and 27% of capital expenditure.

Public Sector Borrowing Requirement (2013-2015)

	2011	2012	2013	2014	2015	2013-2015
Gross borrowing requirement	317.6	464.1	458.9	415.1	398.9	1,272.9
Combined overall public sector deficit (dd)	-9.7	152.6	138.1	106.5	76.9	
Amortizations	327.3	311.5	320.8	308.6	322.0	
External amortizations	72.9	88.8	96.9	113.8	139.1	
Internal amortizations	254.4	222.7	223.9	194.8	182.9	
External loans	262.3	327.7	391.4	390.8	390.8	1,173.0
IDB loans	154.7	153.3	167.0	178.9	190.2	536.1
Capital expenditure	529.2	560.1	655.6	673.8	678.5	2,007.9
IDB loans (% of borrowing requirement)	48.7	33.0	36.4	43.1	47.7	42.1
IDB loans (% of capital expenditure)	29.2	27.4	25.5	26.5	28.0	26.7

Source: MHCP, "Marco Presupuestario de Mediano Plazo 2012-2015." [Medium-term Budgetary Framework 2012-2015]; IDB, Disbursement Forecasts.

Financial scenario and debt ratio. The base-case scenario assumes that the allocation of resources from the Fund for Special Operations (FSO) and its blend with the Ordinary Capital remains the same over the duration of the strategy as the allocation approved for 2011-2012 (i.e. a 50/50 blend). Under this scenario, approvals of US\$856 million are forecast for 2013-2017. Borrowing from the IDB will rise slightly as a share of external government borrowing from multilateral lenders, and IDB debt as a ratio of GDP will rise from 14.1% in 2012 to 18.2% in 2017.

⁸⁴ MHCP, "Marco Presupuestario de Mediano Plazo 2012-2015." [Medium-term Budgetary Framework 2012-2015].

Total lending and flows in relation to the IDB 2012-2017
(US\$ millions)

	2012	2013	2014	2015	2016	2017	2013-2017
Approvals^{1/}	235.4	171.2	171.2	171.2	171.2	171.2	856.0
Disbursements	153.3	167.0	178.9	190.2	204.8	195.8	936.6
Repayments	15.9	17.2	19.6	25.2	31.0	39.2	132.2
Net lending flow	137.4	149.8	159.3	165.0	173.8	156.5	804.4
Subscriptions	2.0	2.0	2.0	2.0	2.0	2.0	10.0
Net capital flow	135.4	147.8	157.3	163.0	171.8	154.5	794.4
Interest and fees	15.8	18.3	20.5	22.5	24.9	27.8	114.0
Net cash flow	119.6	129.5	136.8	140.5	146.9	126.8	680.5
Debt to IDB	1,105.1	1,254.9	1,414.2	1,579.2	1,753.0	1,909.5	
IDB debt/GDP (%)	14.1	15.1	16.0	16.9	17.7	18.2	
IDB debt/external public debt (%)	25.5	26.8	28.0	29.2	30.4	31.2	
IDB debt/external multilateral debt (%)	46.1	45.6	45.5	45.4	45.8	45.7	

^{1/} Amounts subject to the availability of the Bank's finance capital and FSO allocations.

Sustainability analysis. The financial scenario presented above is consistent with a debt sustainability analysis⁸⁵ based on the Debt Sustainability Framework (DSF). According to the debt sustainability model, the risk of external public debt distress is moderate, as classified by the DSF.⁸⁶ Under this base-case scenario, all the external public debt indicators remain below the threshold corresponding to policy quality. However, some of the debt indicators cross their thresholds under stress tests. (i) a one-time nominal depreciation of 30% from the base-case scenario; and (ii) less concessionality in new public sector loans.

⁸⁵ Inter-American Development Bank. Macroeconomic Sustainability Assessment, April 2012. Document for internal use.

⁸⁶ This classification is consistent with the conclusions of the sustainability assessment carried out by the International Monetary Fund. Nicaragua has maintained this classification since the IDB introduced the DSF in 2007.

DONOR COORDINATION

Over the last three decades Nicaragua has been one of the main recipients of international cooperation assistance in the Central American isthmus. In the wake of the damage caused by Hurricane Mitch in 1998, there was a stronger cooperation presence in the country, through agencies such as the Sectoral and Territorial Coordination Committees, which were set up in 2003 under the leadership of State agencies, civil society, and representatives of the international community.

In October 2010 the Government of Nicaragua approved the Official Development Assistance Strategic Management Plan (PGEAOD), putting forward the main guidelines and instruments for the effective channeling of official development assistance (ODA) resources. The PGEAOD structure for the various forums for dialogue between cooperation agencies and the government is as follows: (i) 11 programmatic dialogue platforms for technical/sectoral discussions on the alignment of resources with the medium-term priorities of various government agencies; (ii) the dialogue administration forum, which monitors agreements on aid effectiveness; and the (iii) global dialogue forum, the top level body in the cooperation community and government agencies address policy topics. The Bank participates in all the active sectoral roundtables, and leads the Energy, Health and PRORURAL Committee. The Bank also participates in each of the forums for dialogue with the government, the Monitoring Group, and the internal cooperation agency coordination roundtables, such as the Quintet and the Cooperation Agency Roundtables. The main sectors financed by bilateral donors include: health and education; rural and urban production; Caribbean Coast; and water and sanitation. The infrastructure and energy sectors are supported by multilateral cooperation agencies and some of the bilateral agencies with strongest presence in the country, achieving major efforts in terms of cofinancing.

The Bank has worked in Nicaragua to achieve greater alignment and harmonization with international cooperation agencies. Multiyear, multidonor loans have been designed in the transportation and energy sectors with bilateral and multilateral cooperation agencies, in an effort led by the Bank to leverage financial resources and reduce the country's transaction costs. In the current country strategy cofinancing programs have been approved for the climate change, financial administration system, municipalities and housing sectors. Over the course of the strategy, continuing use of this financing scheme is foreseen. In the health area, the Bank is managing a grant for the "Salud Mesoamérica" [Health Meso-America] regional initiative, with funds from the Bill and Melinda Gates Foundation, the Fundación Carlos Slim para la Salud [Carlos Slim Foundation for Health], and the Government of Spain. This operation has an investment tranche of US\$3.5 million, and if its targets are met within the period specified, will enable access to an additional financing tranche of US\$1.2 million.

Table 1. Multiyear, multidonor operations approved between 2008-2012

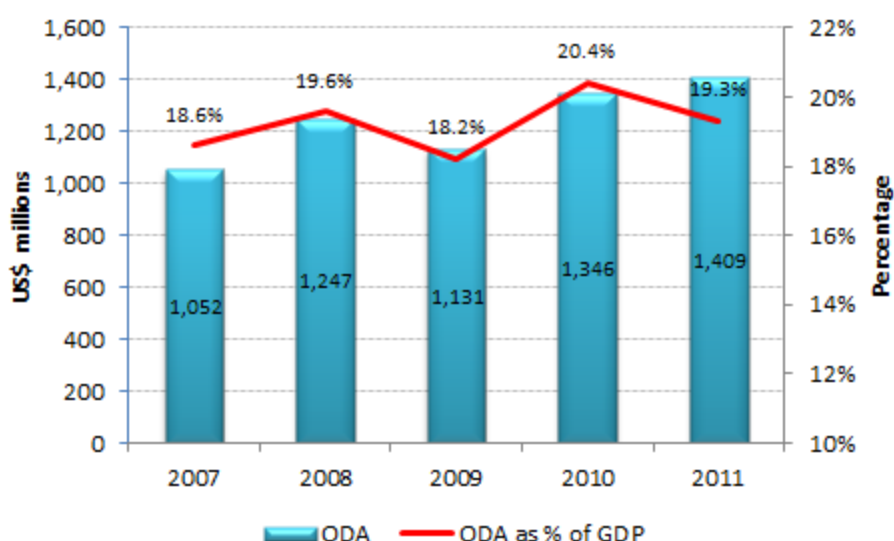
Sector	Operation No.	Name	IDB approved amount (US\$ millions)	Co-financier	Co-financing amount (US\$ millions)
MULTIYEAR AND MULTIDONOR PROJECTS					
Energy	NI-L1040	National Sustainable Electrification and Renewable Energy Program I (PNESER)	30.5	1. Nordic Development Fund (NDF)	5.9
	NI-L1050	PNESER II	22	2. Korean Eximbank (KEXIM)	27.2
	NI-L1063	PNESER III	25	3. Latin America Investment Facility (LAIF)	9.6
				4. European Investment Bank (EIB)	70
				5. Central American Bank for Economic Integration (CABEI)	75
				6. Japan International Cooperation Agency (JICA)	12
				7. Organization of Petroleum Exporter Countries International Development Fund 1	16
				8. Organization of Petroleum Exporter Countries International Development Fund 2	4
				9. Third parties *	26.1
Energy	NI-L1021	Electricity Sector Support Program I	32.7	1. CABEI	25.4
	NI-L1022	Electricity Sector Support Program II	40.2	2. EIB	20.4
	NI-L1036	Electricity Sector Support Program III	20		
Transportation	NI-L1049	Transportation Sector Support Program I	20.2	1. NDF	5
MULTIDONOR PROJECTS					
Environment and natural disasters	NI-L1048	Environmental Program for Disaster Risk and Climate Change Management	10	NDF	3
Transportation	NI-L1006	Acoyapa - San Carlos - Costa Rica border Road Integration Program under the Puebla - Panamá Plan	49.5	1. JICA	31.2
				2. OPEC	4.6
Social investment	NI-L1008	Municipal Social Investment Program - ESIF	45	1. Organization of the Petroleum Exporting Countries	4
Reform/ Modernization of the State	NI-L1033	Public Sector Financial Management System Modernization Project	10	1. World Bank	10
				2. European Union	2.4
Urban housing and development	NI-L1053	Housing and Comprehensive Habitat Improvement Program	20	1. CABEI	9
				2. National Council Twinning Nicaragua and the Netherlands (CNHHN)	8

* The "third parties" heading includes contributions from program executing agencies receiving contributions/subsidies, and reimbursement reinvested in the program.

Operations in 2012 program.

Between 2008 and 2012, 37 cooperation agencies and multilateral organizations (of which 24 are bilateral) were operating in the country. However, nine of these bilateral cooperation⁸⁷ agencies have either withdrawn or announced their gradual withdrawal from the country. Their reasons include focusing their assistance on Africa and the fact that Nicaragua has become a middle -income country. In 2007 these cooperation agencies contributed 21.6% of the total official resource the country received, but by 2011 this percentage had shrunk to 10.4%. Official cooperation funding (grants and loans to both the public and private sectors) have represented almost 20% of gross domestic product (GDP) in the last five years.

Figure 1. Official Development Assistance in Nicaragua, 2007-2011



* Source: Central Bank of Nicaragua (BCN). “Informe de Cooperación Oficial Externa 2011” [External Official Cooperation Report 2011].

Although ODA flows increased in 2011 by more than 30% over 2007, the composition of cooperation assistance has changed considerably over this period. Although multilateral cooperation assistance to the public sector has remained stable since 2007 (with the exception of 2008, due to the outbreak of the financial crisis), bilateral cooperation suffered a substantial drop (almost 50%) from 2007. By contrast, bilateral cooperation assistance to the private sector has increased significantly, rising from US\$226 million in 2007 to US\$748 million in 2011.

⁸⁷ Austria, Denmark, Finland, Germany, Iceland, Norway, the Netherlands, Sweden, and the United Kingdom.

Figure 2. Official Cooperation Assistance to the Public Sector

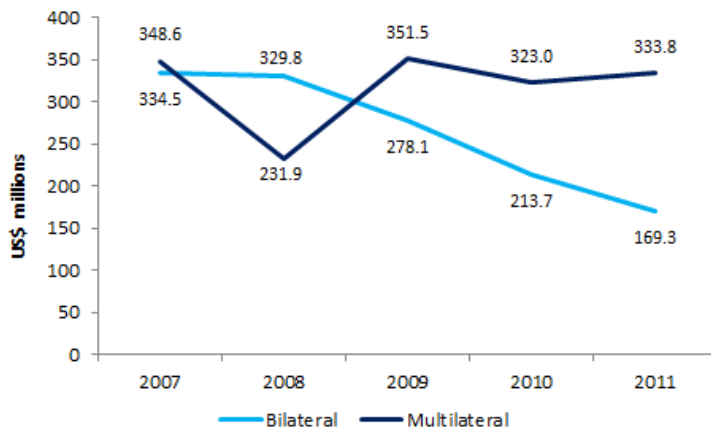
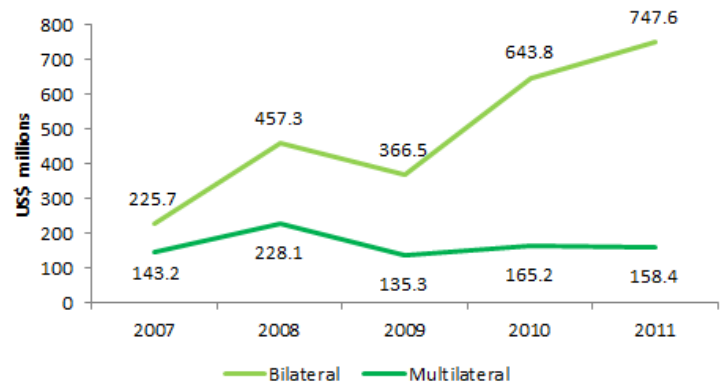


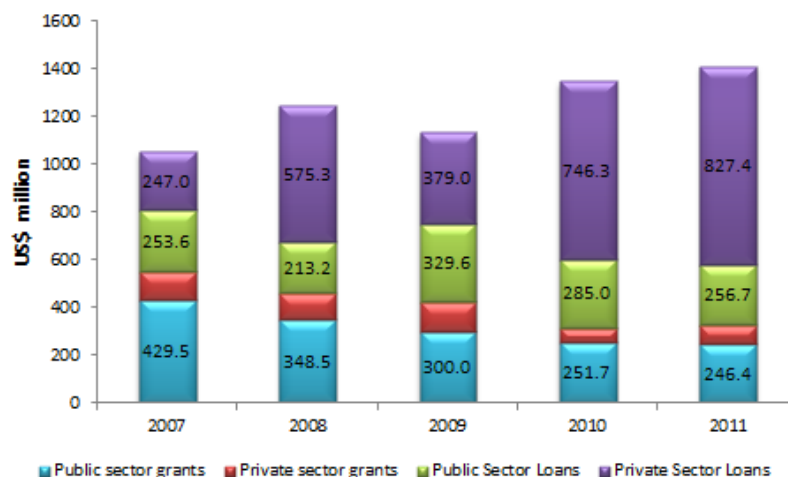
Figure 3. Official Cooperation Assistance to the Private Sector



* Source: Central Bank of Nicaragua (BCN). "Informe de Cooperación Oficial Externa 2011" [External Official Cooperation Report 2011].

There has also been a change in the structure of cooperation, with more resources now concentrated in loans rather than grants, particularly in the public sector. Thus, in 2007 over 52% of official aid received was in the form of grants and the main beneficiary was the public sector, receiving almost US\$430 million. However, grants to the public sector fell by almost half in five years, and grants to the private sector fell by 35% over the same period. As Figure 4 shows, public sector loans (mainly from multilateral sources) have remained stable, while loans to the private sector have more than tripled, rising from US\$247 million in 2007 to US\$827 million in 2011.

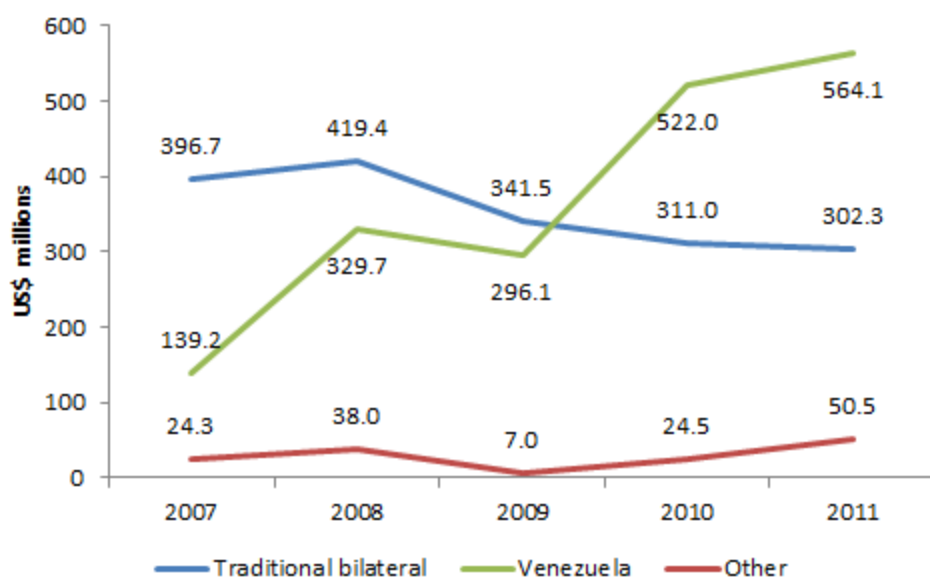
Figure 4. Structure of ODA



* Source: Central Bank of Nicaragua (BCN). "Informe de Cooperación Oficial Externa 2011" [External Official Cooperation Report 2011].

Venezuela's cooperation, which is channeled through the Bolivarian Alliance for the Americas (ALBA), has been largely responsible for the increase in total flows of official cooperation assistance. In 2011 this even exceeded the total assistance the public sector received from both multilateral and bilateral cooperation agencies.

Figure 5. Trends in bilateral cooperation



* Source: BCN. "Informe de Cooperación Oficial Externa 2011" [External Official Cooperation Report 2011].

The increase in the oil price partly explains the increase in oil cooperation under ALBA, which rose from US\$69 million in 2007 to US\$557 million in 2011. In the same vein, Nicaragua went from importing from Venezuela 23% of the oil it consumed in 2007 (US\$190.9 million) to importing 90% (US\$1,132.5 million) in 2011.

Table 2. Donor Map. Main Areas of Intervention (US\$ millions)

Country	Agency	Sector Supported										
		Education	Health	Rural Production	Urban Production (MSMEs)	Water and sanitation	Caribbean Coast	Energy	Environment, Climate Change and Risk Management	Tourism	Citizen Security and Justice	Infrastructure
BILATERAL												
Germany	GIZ											
Austria	Embassy											
Canada	Embassy											
Korea	Embassy											
Denmark												
Spain	AECID											
United States	USAID											
Finland	Embassy											
France	Embassy											
Iceland	Embassy											
Italy	Embassy											
Japan	JICA											
Great Britain	DFID											
Grand Duchy of Luxembourg	Embassy											
Norway	Embassy											
Netherlands	Embassy											
Sweden	ASDI											
Switzerland	COSUDE											
MULTILATERAL												
CABEI	Multilateral											
World Bank	Multilateral											
IMF	Multilateral											
OAS	Multilateral											
OEI	Multilateral											
UN **	Multilateral											
European Union	Multilateral											
* Source: Informe de Cooperación Oficial Externa 2011 [External Official Cooperation Report 2011]. Central Bank of Nicaragua												
** Includes the following agencies: UNCTAD, CFC, UNFPA, UNCDF, UNICEF, GFATM, IFAD, GEF, UNIDO, FAO, UNESCO, IAEA, IOM, PAHO/WHO, UNDP, and WFP.												
	Support areas under PGEAOD 2010-2013.											

MACROECONOMIC RISK ANALYSIS

There are two main types of potential macroeconomic risks that might affect implementation of the strategy: (i) external shocks affecting external sustainability and economic growth; and (ii) internal shocks affecting fiscal sustainability.

One of the main external shock risks is that of a global recession, which could have a negative impact on the country's economic growth. Nicaragua's economy would be affected primarily through reduced international demand for Nicaraguan exports, a decline in foreign direct investment flows, and a reduction in flows of family remittances. The performance of the U.S. economy is of the utmost importance not only because Nicaragua is highly dependent on it, but also because Nicaragua's other main trading partners comprise Central America and Mexico, which are in turn closely linked to the United States.

Furthermore, the country is still highly dependent on concessional funding flows from various sources, in a context in which these flows are at risk. The exit of bilateral cooperation agencies has led to dependence of both the public and private sector being concentrated on those that remain. The foregoing represents a greater exposure to each source, amplifying the impact of a loss of funding from any of them.

Another significant risk arises from the country's high current account deficit. This has fluctuated between 13% and 24% of GDP in recent years. Although the level has dropped somewhat in recent years and external sustainability has been strengthened, the current deficit is still high by international standards.

Also linked to external sustainability is the fact that Nicaragua is highly dependent on oil imports, exposing it to international oil price variations. A sustained rise in oil prices would increase spending on imports and could lead to difficulties of external sustainability if it leads to imports rising faster than exports.

Inflation is particularly sensitive to oil and food prices. A bigger increase in these prices would create inflationary pressures affecting the internal market and external competitiveness.

The main risks also include internal shocks that could affect fiscal sustainability. Although Nicaragua has made efforts to reduce its fiscal deficit in recent years, these could be undermined in the medium term if it does not introduce reforms in the social security system or if the government assumes contingent liabilities. The International Monetary Fund (IMF) estimates that the Instituto Nicaragüense de Seguridad Social [Nicaraguan Social Security Institute] (INSS) will be in deficit by 2017-2018 and insolvent by 2024 if a comprehensive reform of the sector is not undertaken.

The country is likely to try to strengthen its macroeconomic framework through a new program with the IMF. The Bank will use its macroeconomic monitoring tools to follow the aforementioned risks closely.

DEVELOPMENT EFFECTIVENESS MATRIX

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX

In August 2008, the Board of Executive Directors approved the Development Effectiveness Framework (document GN-2489) to increase the evaluability of all Bank development products.

The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."

COUNTRY STRATEGY: NICARAGUA 2012-2017

STRATEGIC ALIGNMENT (measures two dimensions: (i) the extent to which the strategy's objectives are consistent with the country's development challenges and the government's plans and priorities; and (ii) the use of a mix of products (financial, know-how, technical support) enabling the objectives to be achieved and other cooperation agencies and their areas of action to be identified).

Consistency of strategic objectives: The strategy identifies the following areas of work: (i) energy; (ii) transportation; (iii) health; and (iv) comprehensive care in early childhood. The strategy sectors will take into account the topics of gender, diversity and climate change, as appropriate. All the areas of work selected address the country's development challenges are consistent with the priorities set by the Government of Nicaragua. Additionally, these areas of work are the product of a dialogue between the country and the Bank.

Product mix and participation of other cooperation agencies: The strategy envisages the use of various of the Bank's instruments, such as sovereign guaranteed, non-sovereign guaranteed, and technical cooperation operations. The strategy envisages interventions by other donors, including the Nordic Development Fund, the European Investment Bank, and the Central American Bank for Economic Integration.

EFFECTIVENESS (extent to which it is expected that the country strategy will achieve its objectives based on a review of four dimensions: (i) quality of the diagnoses on which the Bank's action rests in each area of work; (ii) the quality of the strategy results matrix; (iii) the use and strengthening of country systems; and (iv) the analysis of the lending framework:

Dimensions of Effectiveness	%
I. Sectoral diagnoses	
- Main problems identified based on empirical evidence	100
- Main beneficiaries identified	100
- Identification and dimensioning of the factors contributing to the problems identified	100
- Policy framework and a sequence for the Bank's intervention set out	100
- The objectives set out in the strategy correlate to the diagnostic assessment	100
II. Results matrix	
- The expected outcomes are clearly defined	100
- The indicators measure outcomes and are SMART	100
- The indicators have a baseline	91

Five sector notes were submitted as part of the strategy. All the notes have been validated

- All the notes clearly identify the sector's main problems based on empirical evidence.
- All the notes identify the potential beneficiaries in each intervention area.
- All the notes raise or dimension the factors contributing to the problems identified.
- All the notes propose a policy framework and sequence for actions by the Bank.
- In all the notes there is a correlation between the topics raised and the Bank's strategic objectives.

Results matrix: The results matrix includes nine strategic objectives for the Bank's action and 22 indicators to measure progress towards the proposed objectives.

- 100% of the strategic objectives have a clear definition of the expected results;
- 100% of the indicators used are outcome indicators and are SMART;
- 91% of the indicators have a baseline.

Country systems: A diagnostic assessment is available for all the procurement subsystems. During the strategy period, the level of use of some of the financial management and procurement subsystems will be maintained (budget, treasury, information system). Various actions are also envisaged to support the country in improving some country subsystems (budget, treasury, information system) and strengthening others (accounting and reports, internal audit, shopping).

Lending framework: The strategy contains an analysis of the country's borrowing needs and sets out a base-case scenario assuming that the FSO and OC allocation (a 50%-50% blend) remains the same as the allocation approved for 2011-2012.

RISKS (measures three dimensions: (i) identification of the factors that affect or might affect the scope of the proposed objectives; (ii) definition of mitigation measures, and (iii) monitoring mechanisms):

The strategy envisages risks associated with the Bank's involvement in each of the sectors of intervention. Institutional risks, financial risks, and natural disaster risks are also considered.

**COMMENTS ON THE COUNTRY PROGRAM EVALUATION
NICARAGUA 2008-2012**

Recommendation	Management Response
<p>1. Undertake further diagnostic and analytic work to delineate the Bank's potential role and value-added in Nicaragua. The country's mixed record of economic performance, its dynamic political context, and the withdrawal of some international partners have left the Bank in a sensitive position. As the largest multilateral partner, the Bank needs to consider carefully where it can contribute most effectively to Nicaragua's economic development and take measures to focus its program accordingly. A highlight of the analytic work prepared for CS 2008 was the Growth Diagnostic. The Bank should update this body of work to fill in data and information gaps previously encountered.</p>	<p>Agreed. As part of the process of formulating the 2012-2017 country strategy, the Bank has updated the country knowledge, which included preparing policy notes and updating the Growth Diagnostic, complemented by studies in the energy and financial sectors. These studies have been relevant inputs for the policy dialogue with the country and for targeting the strategy towards those areas in which the Bank has the greatest value added.</p>
<p>2. Support Nicaragua in improving the efficiency of public expenditure, including in the electricity sector. The country's ability to expand public external indebtedness is likely to be limited in the future. The Bank could usefully assist the country in identifying and implementing reforms to increase the efficiency of public spending and improve the financial sustainability of public enterprises. One area of potentially high impact is the electricity sector, where there are large subsidies and significant non-technical losses.</p>	<p>Agreed. During the next strategy, support will continue to be provided to the country to improve the efficiency of public expenditure. The electricity sector is a priority area of the strategy, and the Bank's activities in the sector will help to adapt the sector framework to ensure its efficiency and financial and operating sustainability. Moreover, interventions in the social sector will aim to improve the efficiency and targeting of social spending.</p>
<p>3. Work with the Government of Nicaragua to strengthen the measurement and reporting of results at the project level. It is incumbent upon the Bank to document and track the results of its program with the country. It should give greater priority to strengthening project-level results measurement and reporting than to defining detailed targets for results in country strategies and annual programs, given the difficulty of attributing country-level results to Bank engagement.</p>	<p>Agreed. This recommendation is being incorporated into the portfolio review exercises, which are currently focused on results-based planning. As part of this exercise, Bank and executing unit staff have been given training on issues related to measuring results.</p>

<p>4. Enhance the sustainability of investment lending to Nicaragua by estimating the likely increase in recurrent costs, and as part of project design, request that government identify potential sources of financing for the continued provision of services beyond project completion.</p>	<p>Agreed. The Bank, in coordination with the country, will identify how to make loan sustainability and maintenance more viable, depending on the sector and specific characteristics of each operation. The corresponding analysis on the potential increase in costs will continue to be conducted.</p>
<p>5. Consider ways to provide D-2 countries with access to emergency lending facilities to meet fiscal needs in times of crisis. The use of policy-based lending to disburse emergency financial relief undermines the original intent of the PBP instrument to support deep policy reform. Short-term liquidity needs in crisis situations should be addressed with other instruments—not yet available in D-2 countries—to avoid compromising the role of policy-based lending.</p>	<p>Partially agreed. Although it is true that the Bank does not currently have an instrument for delivering emergency financial resources to D-2 countries, the integrity of policy-based loans has not been, and is not, undermined as a result. Management does not consider that the Bank used policy-based loans to disburse emergency financial relief. Each policy-based loan was presented according to the corresponding policies and rules, and the Board of Executive Directors of the Bank approved them after considering their technical merits and respective reforms.</p>