International Monetary Fund

Nicaragua and the IMF

Press Release:
IMF Executive Board Completes Second and Third Reviews Under Poverty Reduction and Growth Facility Arrangement with Nicaragua
November 2, 2009

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Nicaragua: Letter of Inten and Technical Memorandum of Understanding

October 16, 2009

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

October 16, 2009

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C.

Dear Mr. Strauss-Kahn:

1. The Nicaraguan economy has been seriously affected by the global economic and financial crisis which began at the end of last year. The Government of Reconciliation and National Unity (GRUN) has adjusted its 2009-10 economic program with the aim of mitigating the effects of the crisis, while safeguarding macroeconomic stability. Accordingly, and in response to reduced revenue estimates relative to the original budget proposal (4.0 percent of GDP), the General Budget (PGR) for 2009 has been adjusted on several occasions (with planned spending cuts totaling 2.1 percent of GDP), in an effort to rationalize expenditures, while protecting public investment linked to economic growth.

2. The Government remains committed to the Poverty Reduction and Growth Facility (PRGF) agreement. All the quantitative performance criteria through December 2008 were met, with the single exception of the (adjusted) net international reserves accumulation target; which fell by about US$30 million (compared with a US$40 million increase under the program). This was the result of lower external financing and a slowdown in money demand growth. At the same time, there has been progress in implementing the supplementary agenda, although there were delays in the approval of the renegotiation of bank bonds (*structural performance criterion*, September 2008). Waivers are requested for this delay and shortfall in the reserves accumulation target.

3. As part of the second and third reviews, quantitative performance criteria have been established for December 2009 and June 2010, as well as indicative criteria for end-2010. Benchmarks were also agreed for the supplementary agenda, including specific aspects related to the strengthening of public financial management, the Central Bank (BCN), as well as the tax and pension systems. The latter reforms are necessary to comply with the 2010 fiscal targets and safeguard the sustainability of public finances. The fourth review, which will coincide with the Article IV consultation scheduled for February 2010, will focus on assessing compliance with the agreed targets for end-2009 and progress in adopting the policy commitments for 2010.

Macroeconomic framework for 2009-10

4. Real GDP is projected to fall by about 1 percent (3.2 percent increase in 2008) on account of a decline in exports and remittances, as well as a tightening in external financing conditions product of the global economic crisis. Although improvements in terms of trade are expected to help to mitigate declines in external demand, the strengthening of macroeconomic balances in recent years has put Nicaragua in a better position to cope with the crisis, enabling the country to loosen its fiscal stance in 2009. Real GDP is projected to increase by 1 percent in 2010, in line with a gradual recovery in global conditions. Inflation is estimated to decline from

its level of 13.8 percent at end-2008 to 2–3 percent in 2009, increasing to 3–5 percent in 2010 with the recovery in commodity prices. Against this backdrop, the government will seek to ensure that increases in the minimum wage will not be higher than cumulative inflation and real economic growth.

5. The external current account deficit is projected to narrow to about 15 percent of GDP in 2009 (24 percent of GDP in 2008), reflecting a contraction in imports that is expected to more than offset projected declines in exports (9 percent) and remittances (6 percent). The current account deficit is expected to be financed primarily through foreign direct investment and official aid, allowing gross international reserves to increase by roughly the amount of the recent allocations of Special Drawing Rights (US$165 million). For 2010, a small increase in the current account deficit is expected, in line with the economic recovery and higher oil prices.

Nicaragua: Macroeconomic Indicators

	2007	2008		2009	2010
		Prog.	Prel.		
Real GDP growth (in percent)	3.2	4.0	3.2	-1.0	1.0
Inflation (end of period, in percent)	16.9	15.0	13.8	2-3	3-5
Inflation (period average, in percent)	11.1	18.1	19.9	4.0	4.2
Overall balance of Combined Public Sector after grants (in percent of GDP)	0.9	-1.8	-1.5	-4.6	-3.2
External current account deficit (in percent of GDP)	17.6	25.7	23.8	15.0	18.1
Gross International Reserves (US$ million) 1/	1,103	1,230	1,141	1,307	1,332
in months of imports of goods (excluding maquilas)	3.2	3.0	2.9	4.1	3.9
Net international reserves (program definition, US$ million)	737	797	710	655	635

1/ Includes new SDR allocation for SDR 105.1 million (US$165 million).

Social policy

6. The updated summary of the National Human Development Plan (PNDH) has been completed. This plan has been the subject of consultations with Nicaraguan civil society and the donor community. The summary of the PNDH describes in detail the government's social and economic policy, which aims to improve the coverage and quality of delivery of goods and services in the areas of health, education, nutrition and safe drinking water. Under the PNDH, and despite existing constraints with respect to external financing, the share of poverty-reducing expenditure is expected to remain above 40 percent of public sector spending, while improving the effectiveness of programs to protect the more vulnerable members of society.

7. Despite the adverse macroeconomic environment, health and education indicators have improved as a result of the government's social policy. In 2008, maternal mortality fell significantly, reaching 67 per 100,000 live births (target of 94 per 100,000 live births); the number of children older than one year immunized against measles, mumps and rubella (MMR) was 11 percent higher than programmed; and illiteracy rates fell from 20.2 percent in 2007 to 7.5 percent in 2008. Goals of the PNDH include: (i) raising the primary school retainer rate from the 89.6 percent recorded in 2008 to 91.5 percent in 2011; (ii) lowering the maternal mortality rate from 67.0 per 100,000 live births in 2008 to 55.0 in 2011, and reducing the infant mortality rate from 29 per 1,000 live births recorded in 2006 to 25 in 2011; and (iii) increasing the effective coverage of potable water in urban areas from 70 percent in 2008 to 86 in 2011. In the case of the government's social program *Hambre Cero*, the provision of assets (*bonos*

productivos) is expected to expand by over 43,000 families during the next three years. The second progress report on meeting the social indicators under the program was published in October 2009.

Fiscal policy

8. Fiscal policy in 2008 remained prudent and the cumulative overall deficit for the consolidated public sector was lower than the programmed targets. This favorable performance was the result of disciplined execution of expenditure against a background of lower-than-programmed government revenues (tax collections and grants). In addition, public enterprises had a stronger-than-anticipated performance, partly reflecting significant adjustments in public utility rates, which averaged 25 percent in water and 2.8 percent in electricity (the latter increased by 30 percent between January and October 2008 reflecting oil price trends). This helped to offset increased expenditure on pension and health services by the Nicaraguan Social Security Institute (INSS).

9. In 2009, fiscal policy aims to support growth and protect social expenditure, while continuing to ensure macroeconomic stability against the background of the global crisis. The program includes a temporary increase in the Consolidated Public Sector (CPS) deficit target from 1.5 percent of GDP in 2008 to 4.6 percent in 2009. To achieve this target and offset the reduction in revenue relative to the levels projected in the approved 2009 PGR, the National Assembly approved in July spending cuts equivalent to 0.6 percent of GDP, and an additional round of cuts equivalent to 0.5 percent of GDP were approved in October (in February an adjustment equivalent to 1 percent of GDP was made to the original draft budget). These cuts focused on: (i) reducing expenditure on goods and services; (ii) modifying budget appropriations for those capital expenditures with low levels of execution; and (iii) adjusting constitutional and statutory transfers in line with the revised levels of tax revenues and expenditures. In spite of these adjustments, Central Government spending is expected to grow by 4.6 percent in real terms in 2009.

10. For 2010, the government will consolidate the fiscal position with the aim of preserving the sustainability of public finances, while protecting infrastructure and social spending. The CPS deficit will be reduced to 3.2 percent of GDP, through strict expenditure control, a concerted strengthening of the tax system and improvements in the finances of the pension system.

- **2010 Budget:** Total Central Government spending will be kept constant in nominal terms in relation to 2009, through policies designed to: (i) rationalize capital spending, focusing on investment in productive and social infrastructure; (ii) protect the more vulnerable segments of society by maintaining targeted subsidies on water, electricity, and public transportation; (iii) ensure that public utility tariffs (electricity, water and sanitation) fluctuate in line with costs to safeguard the finances of public enterprises; and (iv) adjust the wage bill to reflect expected inflation. A draft 2010 PGR in line with the program objectives has been submitted to the National Assembly and its approval will be sought by year-end (*structural benchmark*).
- **Strengthening the tax system**: To offset the declines in tax revenues and safeguard fiscal sustainability, the government, in consultation with the private sector, has prepared a proposal for strengthening the tax system. The proposal seeks to implement a

new tax regime that enhances progressivity and broadens the tax base, with the following key features: (i) it introduces a dual system of income taxation, that separates income from labor and capital (interest, dividends, and capital gains) sources; (ii) it establishes regulations on transfer pricing practices; (iii) it modifies the special regimes governing small-scale taxpayers; and (iv) it rationalizes exemptions and exonerations. To maintain spending at programmed levels, the proposal is expected to yield at least 0.7 percent of GDP in 2010, with any additional revenues earmarked for social and infrastructure spending. The draft tax law has been submitted to the National Assembly in conjunction with the 2010 budget and the government will seek its approval by year-end (*structural benchmark*) so that it can enter into force in January 2010.

- **Strengthening the pension system**. The INSS is expected to approve by end-2009 a 1 percentage point increase in the social security contribution rate with a view to its entering into effect in January 2010. This measure will be accompanied by a spending policy on pensions and health services consistent with improving the finances of the system by ½ percent of GDP in 2010. To achieve a more comprehensive strengthening of the system, a new actuarial study will be completed by end-October 2009, upon which the Inter-Institutional Commission (consisting of the INSS, BCN and MHCP) will propose by end-2009 a set of options for improving the system's financial position and gradually correcting its actuarial deficit (*structural benchmark*). The proposals derived from this study will be the focus of broad-based public consultation during 2010, prior to its submission to the National Assembly.

Nicaragua: Consolidated Public Sector Fiscal Accounts

(in percent of GDP)

	2007	2008		2009	2010
		Prog.	Prel.		
Overall balance of CPS (a+b+c+d)	0.9	-1.8	-1.5	-4.6	-3.2
Primary balance	2.4	0.0	-0.3	-3.2	-1.8
Interest	1.5	1.8	1.2	1.5	1.5
a. Central government	0.4	-1.3	-1.2	-3.5	-2.0
Revenue	19.5	18.5	19.0	17.9	18.6
Tax	18.0	17.1	17.6	16.6	17.2
Other	1.0	1.0	1.0	0.8	0.7
Expenditure	22.8	23.9	23.2	24.3	22.9
Current	15.7	16.7	17.1	18.3	17.1
Capital	7.1	6.9	6.0	6.0	5.8
Grants	3.7	4.1	2.9	2.8	2.3
b. INSS and ALMA	1.7	1.6	1.2	1.0	1.5
c. Public enterprises	-0.9	-1.3	-0.8	-0.9	-1.6
d. Central bank	-0.3	-0.9	-0.7	-1.2	-1.1

11. The Government remains committed to consolidate public finances over the medium term, with a view to gradually reduce public debt as a share to GDP. This will be achieved through a prudent management of current spending, a strengthening in tax administration and additional measures to improve the finances of the pension system.

Monetary and financial policy

12. The 2009–10 monetary programs will be consistent with maintaining an adequate level of international reserve coverage to support the crawling peg regime. Given the considerable impact of the global crisis and the associated slowdown in monetary aggregates, the monetary

program is based on a small (US$75 million) decline in the (adjusted) net international reserves for 2009-10. To meet these objectives and manage financial system liquidity, the monetary authority will continue to conduct open market operations as necessary. The central bank will maintain the rate of crawl of the exchange rate at 5 percent, and will use the recent allocations of Special Drawing Rights to strengthen international reserves and its financial position.

13. The BCN has taken a series of steps to protect the banking system from the risks associated with the global financial crisis. Earlier this year, it made available a new Special Financial Assistance Line (LAFEX) to banks, offering higher access limits and greater flexibility on the use of collateral. Additionally, in August the central bank signed with the Central American Bank for Economic Integration (CABEI) a 12-month contingent credit line of US$200 million, to protect international reserves in the event of a liquidity shock and to strengthen the deposit guarantee agency. At the same time, monitoring of the banks' loan portfolio, which suffered some deterioration due to the economic slowdown, has been intensified. In this regard, the Superintendency of Banks and Other Financial Institutions (SIBOIF) has redefined its strategy maintaining a supervision focused on analysis of major risks, with more frequent visits to supervised institutions. Prudential norms and regulations have been strengthened to safeguard financial system stability and maintain adequate provisioning.

14. The central bank's institutional framework was strengthened with the reestablishment of the Central Bank Board of Directors, which approved the bank bonds renegotiation agreements in February 2009. The SIBOIF, for its part, informed the banks (and the financial groups to which they belong) that this transaction will be recorded in accordance with the negotiated value, given that there is no active and liquid secondary market for these bonds. The SIBOIF remains committed to the full application of Nicaragua's accounting standards and will seek to achieve their harmonization with those of the region to bring about effective consolidated cross-border supervision. The Financial Sector Assessment Program (FSAP) will be updated in October 2009 with the participation of the World Bank and the IMF.

Financing

15. The 2009-10 economic program will continue to be financed manly with concessional resources from international donors, and strict supervision will continue to be exercised over nonconcessional borrowing to ensure public debt sustainability. Budget support in the amount of about US$95 million is projected for the remainder of 2009 and for 2010, and continued efforts will be made to obtain additional resources from multilateral institutions and the donor community. In addition, the INSS will invest a high proportion of its projected surplus in Treasury bills and maintain its investment position with commercial banks. The placements of Treasury bills with the private sector will be consistent with gradual development of the domestic debt market.

16. The government will continue negotiations to restructure pending external debt with official creditors under the terms offered by the Heavily Indebted Poor Countries (HIPC) Initiative. In April 2009, a restructuring agreement was reached with the government of Algeria representing a reduction of more than 4 percent of the stock of external public debt. In addition, the debt buy-back with private creditors was finalized in December 2008 and the audits relating to this operation were presented to the World Bank in July 2009.

17. Official foreign aid has helped Nicaragua deal with the challenges posed by the global environment. Financing from official sources reached US$1,050 million in 2008 (16.6 percent of GDP), of which over US$400 million were assigned to the public sector and the remaining US$650 million to the private sector, for private agroindustry and renewable energy projects, as well as to small-and medium-size enterprises through private cooperatives. For 2009-10, official flows are projected to decline slightly, partly on account of a decline in concessional financing to the private sector related to oil imports. Nevertheless, official assistance to the public sector will represent about 9 percent of GDP in 2009, financing over half of the external current account deficit. The monitoring of such flows will continue to be strengthened to ensure they are duly recorded in the balance of payments and the fiscal accounts. The second foreign official aid report with information for 2008 was published in June 2009, and the third report with information through mid-2009 is expected to be completed by November.

Supplementary Agenda

18. Progress was made in implementing the program's supplementary agenda focused on strengthening: (i) the electricity sector; (ii) the management and sustainability of public finances, including the reform of the pension system; and (iii) the institutional framework and finances of the Central Bank, inter alia.

19. **Strengthening the electricity sector.** Further progress was made in strengthening the finances and service of the electricity sector, and in expanding the supply of generation with the aim of normalizing the provision of energy and lowering its costs.

- Tariffs were adjusted in line with fuel prices, thus enabling the distribution company to reduce its arrears accumulated with generation companies during 2007-08. The Special Law on the Responsible Use of Basic Energy Services, has also been in effect since August 2008 and over 9,000 inspections have been carried out allowing a 3 percentage point reduction in distribution losses since January 2008. In line with the memorandum of understanding signed between the government and the private distribution company, tariff adjustments will continue to be made in line with input costs, and the necessary investments will be secured to improve electricity service and reduce the sector's technical losses.
- The supply of electricity generation has continued to expand with the participation of the private sector and the support of official donors. In 2008, the binational enterprise ALBANISA installed 60 MW of electricity generation based on fuel oil, and in February 2009 a private consortium installed 40 MW of wind power generation. It is expected that 160 MW of additional generation will be introduced by end-2010, thereby enabling less efficient units to be kept on standby, while changing Nicaragua's generation matrix to reduce its dependence on oil.

20. **Strengthening public financial management**. A Financial Management System Modernization Plan (PMSAF) was prepared for 2008–12, to promote the more effective and transparent use of public spending. With the financial support of the World Bank and the IDB, the program will seek to improve the systems for reporting, monitoring, and auditing the budget accounting records, while providing easier public access to the main fiscal statistics. The PMSAF's operating norms and conceptual framework are being developed so that its implementation can start in 2010. Meanwhile, progress is expected to be made in the following

areas: (i) following up the physical execution of the Public Investments Program and starting to publish this information monthly by March 2010 (*structural benchmark*); and (ii) improving the recording of the various expenditure stages by the preparation of manuals and procedures by end-2009, with the aim of improving expenditure management and preventing the accumulation of arrears.

21. **Strengthening the tax and customs administration.** Regional economic integration and the proposed introduction of the new tax system will require modernization of the revenue administration agencies. Administrative norms, as well as new procedures and forms, are being developed to ensure the effective and expeditious implementation of the proposal to strengthen the tax system. At the same time, an action plan is being developed (with assistance from the Regional Technical Assistance Center (CAPTAC-DR)) to strengthen information systems, as well as payment and control mechanisms. The plan is expected to be finalized by end-2009 with a view to its implementation in January 2010.

22. **Institutional strengthening of the central bank.** A draft law amending the Organic Law of the Central Bank was presented to the National Assembly in June 2009 with a view to (i) consolidating its institutional strength; (ii) ensuring greater accountability; (iii) improving the instruments of monetary policy; and (iv) creating the mechanisms to strengthen the bank's financial position. Approval will be sought by end-2009 and a plan to recapitalize the central bank will be completed by end-2010. Additionally, the 2006 audited financial statements of the central bank were published in August, and the audited financial statements for 2007 and 2008 are expected to be published by end-November.

23. **Reform and regulation of the microfinance sector**

- In May 2009 the law establishing the new state-owned bank *Produzcamos* was amended with a view of consolidating various state-owned funds to take advantage of economies of scale to provide financing to sectors not served by commercial banks. This bank will not accept deposits, and will be subject to the prudential and supervisory standards set by the SIBOIF in accordance with the law. It is expected that *Produzcamos* will enter into operation in 2010 upon completion of: (i) the audits of the funds to be consolidated and approval by creditors of the bank's proposal; and (ii) the regulation of the bank's operations. The World Bank and the IDB will be consulted on the preparation of the proposal.
- The SIBOIF will continue to strengthen supervision over microfinance entities that have become regulated financial entities and the authorities will continue to promote the conversion of the largest unregulated microfinance entities into its regulation and supervision. To ensure the sound development of credit markets in rural areas and safeguard the stability of the financial system, the government will seek consensus to encourage a voluntary and market-friendly restructuring of past due micro-credit loans. In addition, it will review the legal and regulatory framework for microfinance entities, with a view of strengthening oversight and competition of the currently unregulated financial sector.

24. In view of the progress made under the PRGF-supported program and the framework presented for implementing the remaining policies, the government requests the approval of the second and third reviews of the program, including the corresponding waivers and rephasing of the disbursements under the agreement. Going forward, the government will continue to consult with Fund staff on all matters relating to policies included in the program.

Sincerely yours,

/s/	/s/
Antenor Rosales Bolaños	Alberto Guevara Obregón
President	Minister
Central Bank of Nicaragua	Ministry of Finance and Public Credit

LOI Table 1. Nicaragua: Quantitative Performance Criteria and Indicative Targets, 2008-10 1/

	2008						2009		2010	
	Jan-Jun			Jan-Dec			Jan-June	Jan-Dec	Jan-Jun	Jan-Dec
	Prog.	Adjusted	Prel.	Prog.	Adjusted	Prel.	Prel.	Prop. Prog.	Prop. Prog.	Prop. Prog.
Performance Criteria (Jan-Dec 2008, Jan-Dec 2009, Jan-June 2010, indicative targets otherwise)										
					(In millions of Córdobas)					
1. Floor on combined public sector overall balance, after grants 2/	-1,036	-1,403	822	-2,340	-2,922	-1,872	-634	-5,934	-736	-4,415
2. Ceiling on change in net domestic assets of the central bank 2/ 3/	-849	-409	-526	416	998	494	-766	1,118	-906	763
					(In millions of US dollars)					
3. Floor on change in net international reserves of the central bank 2/	22	-1	-14	40	10	-27	-17	-55	-10	-20
4. Continuous ceiling on nonconcessional external debt contracted or guaranteed by the consolidated public sector	0	0	0	0	0	0	0	0	0	0
5. Continuous ceiling on the accumulation of new external arrears of the combined public sector	0	0	0	0	0	0	0	0	0	0
Indicative targets										
					(In millions of Córdobas)					
1. Ceiling on central government primary expenditure 4/	13,552	13,552	12,012	29,114	29,114	27,131	13,079	29,277	13,236	29,160
2. Floor on poverty-related expenditures of the central government 5/	8,061	6,945	7,207	18,558	17,044	16,468	6,791	16,215	7,452	16,863
Memorandum items										
Stock of NIR (adjusted, US$ millions)	759	736	723	797	767	710	692	655	645	635

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

1/ Cumulative flows starting at the beginning of the calendar year. Definitions are specified in the TMU.
2/ Adjusted for shortfalls in grants up to a maximum of US$ 30 million in 2008 and US$ 40 million in 2009 as specified in TMU.
3/ Defined as the difference between currency and net international reserves at an accounting exchange rate specified in the TMU.
4/ Defined as the difference between expenditures and interest.
5/ Adjusted for shortfall in external loans and grants as specified in TMU.

LOI Table 2. Nicaragua: New Structural Benchmarks, 2009–10

	Date
1. Approval by Assembly of an agreed 2010 budget consistent with a combined public sector deficit of 3.2 percent of GDP.	End-Dec. 2009
2. Approval by Assembly of an agreed tax reform yielding at least 0.7 percent of GDP.	End-Dec. 2009
3. Finalize technical proposal on options to reform the pension system and reduce its actuarial gap.	End-Dec 2009
4. Initiate publication of monthly report monitoring the physical execution of the public investment program.	End-Mar. 2010

NICARAGUA—AMENDMENTS TO THE TECHNICAL MEMORANDUM OF UNDERSTANDING OCTOBER 16, 2009

All aspects of the Technical Memoranda of Understanding (EBS/07/103, Supplement I and EBS/08/101, Supplement I) issued on September 4, 2007 and August 28, 2008, respectively, remain in effect, except for the new revisions incorporated in the letter of intent of October 16, 2009 and those indicated below.

A. Program Targets

1. The program targets for the quantitative performance criteria for end-December 2009 and June 2010, as well as the indicative targets for end-December 2010, are *established* and shown in detail in Table 1.

Table 1. Nicaragua: Quantitative Performance Criteria and Indicative Targets, 2008-10 1/

	2008			2009		2010	
	Jan-Dec			Jan-June	Jan-Dec	Jan-Jun	Jan-Dec
	Prog.	Adjusted	Prel.	Prel.	Prop. Prog.	Prop. Prog.	Prop. Prog.
Performance Criteria (Jan-Dec 2008, Jan-Dec 2009, Jan-June 2010, indicative targets otherwise)							
			(In millions of Córdobas)				
1. Floor on combined public sector overall balance, after grants	-2,340	-2,922	-1,872	-634	-5,934	-736	-4,415
2. Ceiling on change in net domestic assets of the central bank 2/	416	997	494	-766	1,118	-906	763
			(In millions of US dollars)				
3. Floor on change in net international reserves of the central bank	40	10	-27	-17	-55	-10	-20
4. Continuous ceiling on nonconcessional external debt contracted or guaranteed by the consolidated public sector	0	0	0	0	0	0	0
5. Continuous ceiling on the accumulation of new external arrears of the combined public sector	0	0	0	0	0	0	0
Indicative targets							
			(In millions of Córdobas)				
1. Ceiling on central government primary expenditure 3/	29,114	29,114	27,131	13,079	29,277	13,236	29,160
2. Floor on poverty-related expenditures of the central government 4/	18,558	17,044	16,468	6,791	16,215	7,452	16,863
Memorandum items							
Stock of NIR (adjusted, US$ millions)	797	767	710	692	655	645	635

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

1/ Cumulative flows starting at the beginning of the calendar year. Definitions are specified in the TMU, including adjustors.
2/ Defined as the difference between currency and net international reserves at an accounting exchange rate specified in the TMU.
3/ Defined as the difference between expenditures and interest.
4/ Adjusted for shortfall in external loans and grants as specified in TMU.

B. Definitions

2. The quantitative and indicative performance criteria will be defined as annual cumulative flows for 2009 and for 2010, except for the targets for Adjusted Net International Reserves (NIR-Adjusted) and Net Domestic Assets (NDA), which will be defined as cumulative flows from January 1, 2009.

3. The definition of the central bank's Adjusted Net International Reserves (NIR-Adjusted) (paragraph 11 of the September 2007 TMU) is modified to also exclude: (i) the general SDR allocation that took effect on August 28, 2009 in the amount of SDR 98.3 million (US$150.7 million); and (ii) the special SDR allocation (pertaining to the entry into force of the 4th Amendment of the Articles of Agreement) that took effect on September 9, 2009 in the amount of SDR 8.9 million (US$13.7 million).

4. The following wording will be added to Paragraph 21 of the Technical Memorandum of Understanding of September 2007:

> "The ceiling excludes the 12-month contingent credit line contracted on August 20, 2009 by the Central Bank of Nicaragua (BCN) with the Central American Bank for Economic Integration (CABEI) for US$200 million."

C. Adjustors

5. The accumulation of NIR-Adjusted for the period 2009-10 will be adjusted *downward* to reflect the cumulative amount of any *shortfall* in external untied loans and grants relative to the programmed amount up to a maximum of US$40 million. Accordingly, the NDA target will be adjusted *upward* to reflect the cumulative amount of any *shortfall* in external untied loans and grants relative to the programmed amount up to a maximum of US$40 million.

6. The NIR-Adjusted accumulation target for the period 2009-10 will be adjusted *upward* by the cumulative amount of any *excess* of untied loans above the programmed amount. In the same way, the NDA target for the period 2009-10 will be adjusted *downward* by an amount equivalent to any *excess* of untied loans above the programmed amount.

7. The target for the consolidated public sector overall balance for 2009 and 2010 will be adjusted *downward* by the cumulative amount of any *shortfall* in external untied grants relative to the programmed amounts.

8. The 2009 and 2010 consolidated public sector overall balance target will be adjusted *downward* by the cumulative amount of any *excess* of project-related external loans above the programmed amount. Should this amount exceed US$65 million, the authorities will analyze its use with IMF staff, taking into account its impact on aggregate demand and debt sustainability. This adjustor is only applicable to new projects (projects not included in the Public Investment Program of the PGR (General Budget of the Republic) for 2009 and 2010).

9. The adjustor associated with the external loans to the consolidated public sector (CPS) relating to the ALBA cooperation defined in Paragraph 4 of the Technical Memorandum of Understanding of August 2008 is *removed.*

10. The indicative target for primary expenditure of the consolidated public sector will be adjusted *upward* by the cumulative amount of any *excess* of external grants above the programmed amount, and by the cumulative amount of any excess of external project-related loans above the programmed amount, up to a maximum of US$65 million (TMU ¶8).

11. The adjustors related to external financing will be applied using the projections detailed in Table 2.

TMU Table 2. Programmed External Financing 2009-10
(in millions of US$)

	External loans	Budget support loans 1/	Project-related loans	**External grants**	Budget support grants	Project-related grants	**Total financing**	Budget support	Project-related
	(a=b+c)	(b)	(c)	(d=e+f)	(e)	(f)	(g=a+d)	(h=b+e)	(i=c+f)
Cumulative from January 2009									
Q3-09	198	38	160	113	1	112	312	39	272
Q4-09	330	78	252	194	15	179	524	93	431
Cumulative from January 2010									
Q1-10	41	0	41	29	0	29	70	0	70
Q2-10	92	0	92	75	0	75	166	0	166
Q3-10	214	43	171	130	0	130	344	43	301
Q4-10	310	43	267	190	0	190	500	43	457

1/ Excludes IMF.

12. The indicative target for poverty-reducing spending will be adjusted *downward* by the cumulative amount of any *shortfall* in external financing (grant or loan) connected with the poverty programs specified in Table 3. The indicative target on poverty-reducing spending will be adjusted *upward* by the cumulative amount of any *excess* in external grants.

TMU Table 3. Nicaragua: Central Government Poverty Spending and Financing Sources, 2008-10
(in C$ millions)

	2008		2009			2010	
	Jan.-Dec.		Jan.-Jun	Jan.-Sep.	Jan.-Dec.	Jan.- Jun.	Jan.-Dec.
	Prog.	Prel.	Prel.	Prog.	Prog.	Prog.	Prog.
Poverty Spending	**18,558**	**16,468**	**6,791**	**9,859**	**16,215**	**7,452**	**16,863**
Domestic Financing	8,740	8,170	4,199	5,675	9,387	4,947	10,132
External Financing	**9,818**	**8,297**	**2,592**	**4,184**	**6,828**	**2,505**	**6,731**
Grants	3,214	3,178	769	1,022	1,667	875	1,807
Loans	3,800	2,341	754	1,409	2,295	669	2,227
Debt Relief	2,804	2,778	1,070	1,753	2,865	961	2,697

Source: Ministry of Finance and Public Credit.

D. Reporting and Monitoring

13. Monitoring of private external debt. Publish results of the 2006 and 2007 survey of private sector external debt by end-March 2010.

E. Safeguards

14. Some safeguards recommendations have been implemented and a new agenda for additional measures to be taken through end-2009 has been established (Table 4).

TMU Table 4. Safeguards Implementation of Recommendations Timetable, 2009

Measure	Date	Status	Proposed date
1. Introduction of periodic internal audits in the area of international reserves operations.	Jul-08	Done	
2. Publication of audited financial statements and auditor's opinion for 2006.	Aug-09	Done	
3. Presentation of semi-annual status reports on the implementation of International Financial Reporting Standards (IFRS).	Sep-08	Pending	Oct-09
4. Publication of audited financial statements and auditor's opinion for 2007 and 2008.	Nov-08	Pending	Nov-09
5. Completion of the audit of the financial statements of 2007 and 2008.	Dec-08	Done	