

F B I / O A S - C E N
A S S E S S M E N T

524-K-601

UNCLASSIFIED

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D.C. 20523

NICARAGUA

PROGRAM ASSISTANCE PAPER

AID/LAC/P-034

PAAD-524-K-601

UNCLASSIFIED

SEP 27 4 48 PM '75 DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
EXECUTIVE SECRETARIAT WASHINGTON, D. C. 20523

SEP 28 9 31 AM '75

ASSISTANT
ADMINISTRATOR

EXECUTIVE SECRETARIAT

DEPUTY

ACTION MEMORANDUM FOR THE ACTING/ADMINISTRATOR

THRU: ES
THRU: AA/PPC, Charles Paolillo *Paolillo*
FROM: AA/LAC, Edward W. Coy *Edward W. Coy* (Acting)
SUBJECT: Program Assistance Approval Document for
Nicaragua

Your approval is required for an emergency cash transfer of \$8.0 million from the Economic Support Fund to Nicaragua for reconstruction and rehabilitation activities.

Discussion: The recent civil strife in Nicaragua has strained that country's financial resources and left its economy in shambles. The purpose of the \$8.0 million emergency cash transfer is to provide immediate budgetary support for critical reconstruction and rehabilitation activities and to provide much needed foreign exchange to help maintain economic stability and ameliorate balance of payment problems. Local currency generated by the grant will be used to support a grain stabilization program (\$6.0 million) and a shelter program (\$2.0 million). The local currency generated will finance the purchases of rice, sorghum, beans and corn, supplies and equipment for the grain stabilization program as well as construction materials and contract services to repair or replace homes that were destroyed in the recent civil war.

Waivers: Section 604(e) of the Foreign Assistance Act, as amended, prohibits the procurement of any agricultural commodity outside the United States when the domestic price of such commodity is less than parity. Rice, corn, beans and sorghum, all parity items, currently are selling for less than parity. Section 604(e) seeks to assure that the foreign assistance program is not managed in such a way as to depress the market for U.S. agricultural products. Under section 614(a), the President has the authority to waive FAA section 604(e) when it is important to the security of the U.S. The proposed transactions are clearly necessary to support the long term political and economic stability of

6610017

Nicaragua. The President has signed the Waiver. In addition, because of the critical timing involved in implementation of these activities, your approval is requested to permit procurement of off-the-shelf items having their origin in countries included in AID Geographic Code 935.

Justification to Congress: Congress held hearings on the proposed program on September 11, 1979. The 653(b) and Advice of Program Change waiting periods expired on August 10, 1979, and August 15, 1979, respectively. The objection to the reprogramming request was withdrawn on September 13, 1979.

Recommendation: That you sign the attached PAAD Facesheet.

Approved: JK

Disapproved: _____

Date: 9/27/79

Clearances:

LAC/DR, M. Brown	<u>SO</u>	date	<u>9/27/79</u>
LAC/CEN, R. Gomez	(Subs)	date	<u>9/25/79</u>
GC/LAC, J. Kessler	<u>JK / M W</u>	date	<u>9/26/79</u>
FM, D. Stafford	(Subs)	date	<u>9/26/79</u>
SER/COM, W. Schmeisser	<u>WSS</u>	date	<u>9/27/79</u>
PPC/PDPR, B. Sidman	(Subs)	date	<u>9/25/79</u>
GC, M. Ball	<u>MA / - 46</u>	date	<u>9/26/79</u>
LAC/DR, C. Leonard	(Draft)	date	<u>9/25/79</u>
LAC/DR, I. Levy	<u>IL</u>	date	<u>9/25/79</u>
LAC/DR, R. Mathia	(Draft)	date	<u>9/25/79</u>

LAC/DR:SJacobson:ew:9/26/79:x23404

AID TITLE (9 NSI) PAAD	DEPARTMENT OF STATE AGENCY FOR INTERNATIONAL DEVELOPMENT PROGRAM ASSISTANCE APPROVAL DOCUMENT	1. AGENCY 524-K-601 2. COUNTRY NICARAGUA 3. CATEGORY Cash Transfer 4. DATE September 29, 1979
6. TO: Administrator	5. OVERCHARGE NO. LAC-79-106	
7. FROM: AA/LAC, Abelardo Valdez <i>Abelardo Valdez</i>	8. OVD INCREASE \$8,000,000 TO BE TAKEN FROM Near East Bureau	
9. APPROVAL REQUESTED FOR COMMITMENT OF \$ 8,000,000	10. APPROPRIATION - ALLOTMENT 72-1191037; 937-55-598-00-50-91	
11. TYPE FUNDING <input type="checkbox"/> LOAN <input checked="" type="checkbox"/> GRANT <input checked="" type="checkbox"/> IMPROV <input type="checkbox"/> FORMAL <input type="checkbox"/> NONE	13. ESTIMATED DELIVERY PERIOD 9/28/79 - 9/28/80 14. TRANSACTION EFFECTIVE DATE September 28, 1979	
15. COMMODITIES FINANCED Commodities to be procured with the local currency proceeds of the cash grant include rice, sorghum, beans, scales, motors, pumps, corn, temperature sensing devices, irrigation pumps, belts, screws, vehicles, seeds, fertilizers, cement, and other construction material		
16. PERMITTED SOURCE U.S. only: _____ Limited F.W.: _____ Free World: _____ Cash: \$8,000,000	17. ESTIMATED SOURCE U.S.: _____ Industrialized Countries: _____ Local: \$7,000,000 Other: \$1,000,000	

18. SUMMARY DESCRIPTION:
 The recent civil strife in Nicaragua has strained that country's financial resources and left its economy in shambles. In addition to physical damage to many of the urban centers, there has been severe disruption of economic activity resulting from extensive losses suffered by the country's banking, commercial and industrial enterprises. Unemployment is estimated to be as high as 50% of the labor force. Agricultural production has been sharply reduced and credit is virtually nonexistent. Capital flight has left the country's foreign exchange reserves at a precariously low level. The country is virtually bankrupt.

The purpose of the \$8.0 million cash transfer is to provide immediate budgetary support for critical rehabilitation activities and to provide much needed foreign exchange to help maintain economic stability and ameliorate balance of payments problems. Local currency generated by the grant will be used to support a grain stabilization program (\$6.0 million) and a shelter program (\$2.0 million). The local currencies generated will finance the

19. CLEARANCES LAC/GEN: RGomez - 9/25/79 LAC/GC: JKessler - 9/26/79 EN: DStafford - 9/26/79 SER/COM: BSchweisser - 9/26/79 PRC/PDR: BSidman - 9/26/79 AA/PPC: CPacillo - 9/26/79 CG: MBall - 9/26/79	20. ACTION <input checked="" type="checkbox"/> APPROVED <input type="checkbox"/> DISAPPROVED <i>J. S. ...</i> 9/27/79 AUTHORIZED SIGNATURE Acting Deputy Administrator
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CLASSIFICATION
 LAC/DR: MBrown 9/27/79
 ARA/HCP: GLamberty 9/27/79

Continuation of PAAD form - Section 18.

purchase of agricultural commodities, and supplies and equipment for the grain stabilization program as well as construction materials and contract services to repair and replace homes that were destroyed during the recent civil war.

It is contemplated that because of the emergency nature of these activities, procurement of most commodities (other than motor vehicles) will occur in Nicaragua. Approval of procurement of off-the-shelf commodities, having their origin in countries included in A.I.D. Geographic Code 935 (Free World), is requested. Exclusion of procurement from free world countries would seriously impede attainment of U.S. foreign policy objectives and objectives of the foreign assistance program.

EMERGENCY CASH TRANSFER - NICARAGUA

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* The GRN changed the name of INCEI to Empresa Nacional de Alimentos de Basico (ENADAS). The new entity will have similar responsibilities to those of INCEI.

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II. Summary and Recommendations

A. Grantee

The Grantee is the Government of Nicaragua (GRN). A Grant Agreement will be signed by the GRN and USAID providing up to \$8 million to the GRN in Economic Support Funds (ESF). The USAID will sign separate activity agreements with the Ministry of Housing (MDV) for \$2.0 million to implement emergency repair and reconstruction of houses damaged or destroyed by the recent war and with the Instituto de Comercio Exterior e Interior (INCEI) for \$6 million to finance a grain stabilization program, undertake needed repairs to silos and other equipment damaged by the war, and purchase additional equipment to maintain the grain distribution system.

B. Goal and Purpose

The purposes of the \$8 million cash grant are to provide immediate budgetary support for critical rehabilitation activities and to provide much needed foreign exchange to help maintain economic stability and ameliorate balance of payments problems. The GRN will use the cash grant to establish a local currency account that will be used to: (1) permit INCEI to purchase rice, sorghum, beans, and corn from small farmers in Nicaragua in order to ensure stable and reasonable prices for both consumers and farmers; and (2) support a shelter sector program for approximately 9,000 urban and rural poor people who are largely without shelter as a result of the recent civil strife. The goal of the cash grant is to contribute to the short-term recovery of the Nicaraguan economy.

C. Outputs

Major anticipated outputs will be: (1) a viable program of purchasing and selling basic foods through the Instituto de Comercio Exterior e Interior (INCEI); and (2) approximately 1,500 new or rehabilitated homes located principally in the Managua and Masaya area. On a more general level, the project should help the GRN control its balance of payments problems.

D. Beneficiaries

Approximately 1,500 rural and urban families in the Masaya and Managua areas, most of whom are currently without shelter, will benefit from the housing program. More than 400,000 small farmers will benefit from the grain stabilization program, as will the vast majority of the urban poor population, estimated at 250,000 people, who will be able to buy basic grains at a reasonable price.

E. Inputs

The \$8 million cash grant will be disbursed to the Central Bank as soon as the agreement is signed. Local currency will then be utilized for critical rehabilitation activities such as those described below:

1.. <u>Instituto de Comercio Exterior e Interior</u>	
<u>(INCEI)</u>	
a. Local purchase of grains	\$5,000,000
b. Emergency repairs and procurement	<u>1,000,000</u>
Sub-total	\$6,000,000
2. <u>Ministry of Housing (MDV)</u>	
a. Small repairs	\$ 70,000
b. Major repairs and rehabilitation	1,430,000
c. Reconstruction	<u>500,000</u>
Sub-total	\$2,000,000

INCEI will purchase approximately 32,000 metric tons of corn, beans, rice and sorghum. The crops will be stored in approximately 100 storage depots and two terminals and will be sold at 23 distribution points in rural and urban areas. Up to \$1 million will be used by INCEI to repair silos damaged by the recent fighting and to purchase spare parts and equipment that were either damaged or stolen during the war.

The \$2 million will be used by the MDV to hire foremen and other personnel to supervise reconstruction and to pay for construction contracts between the MDV and private contractors. The MDV also will establish a materials bank consisting of cement block, sheet roofing, beams, etc. purchased from local suppliers.

F. Disbursement Procedures

The \$8 million grant is being provided as an emergency cash grant to the GRN. The GRN will set up an 80 million cordoba account in the Central Bank and all disbursements for INCEI and the MDV will be from this account. The Central Bank will be required to follow normal financial reporting requirements showing how the local currency is used.

G. Procurement Procedures and Waivers

Goods and services financed with the local currency proceeds of the cash grant will be procured consistent with sound commercial practice. Most purchases are expected to be made off-the-shelf in Nicaragua or from neighboring Central American countries. The eligible source and origin of off-the-shelf commodities will be the Free World (Code 935)*. All motor vehicles purchased will be of U.S. manufacture. Commodities to be financed under the cash grant include rice, sorghum, beans, corn, scales, motors, pumps, temperature sensing devices, belts, screws, vehicles, seeds, fertilizers, cement, and other construction materials.

Approximately \$5 million of the cash grant will be used to purchase 32,000 metric tons of agricultural crops, including corn, sorghum, rice and beans. Section 604(e) of the Foreign Assistance Act of 1961, as amended, prohibits the use of foreign assistance funds for the procurement of any agricultural commodity outside the United States when the domestic price of such commodity is less than parity. The market price of corn, beans, rice and sorghum is below the agricultural support level. Section 614(a) of the Act permits the President to authorize the use of funds made available under the Act for offshore procurement of agricultural commodities without regard to Section 604(e) if it is determined to be important to the security of the United States.

The needs of the people of Nicaragua are immediate, and pressing, and the purpose of the cash grant can be achieved only if the U.S. Government can respond rapidly to those needs.

The President has determined that the purchase of the agricultural commodities in Nicaragua is important to the security of the United States and approved the waiver request. (See Annex 2c).

III. Background

A. Introduction: The Disaster in Perspective

The damage to the Nicaraguan economy from the recent war is incomparably greater than that of the 1972 Managua earthquake. While the amount of physical damage is comparable - the damage in both disasters falls within the \$500-\$800 million range - the economic consequences of the recent war are considerably more severe. The Managua earthquake destroyed the capital's commercial center and some of its housing; the recent war has seriously interfered with economic activity nationwide, including the planting of cotton and

*We estimate that approximately 27,000,000 will be procured locally. Our ability to meet urgent needs by purchasing local supplies and equipment for INCEI and the MDV is critical to the success of the proposed activities.

food crops, the conduct of commercial and industrial activity through looting and destruction of inventories, and destruction or damage to many of the country's industrial installations. Housing, particularly in the cities of Esteli, Managua, Leon, and Masaya, was also hard hit (see Table 1). The war's impact on the balance of payments, the Gross Domestic Product, the fiscal deficit and employment is particularly severe.

While the aforementioned effects of the war can be quantified, several other equally serious consequences cannot. Examples of the latter include departure of many of the country's entrepreneurs, managers and technicians; the disruption entailed by the nationalization of Somoza's estates and the need to reorganize and restaff the enterprises that he owned; the confusion and uncertainty concerning the new government's policies, intentions, and direction; and the restructuring of several key Nicaraguan institutions. These factors are having, and will continue for some time to exert a profound impact on the level of investment and economic activity. Moreover, the war comes at a time when the Nicaraguan economy was already beset by difficult economic problems. While the 1972 earthquake found Nicaragua in a rather strong balance of payments position, the recent catastrophe came at a time when Nicaragua is confronting a very serious debt servicing problem as a result of a substantial amount of short-term borrowing from foreign banks incurred by both the private and public sectors in recent years. The maturing of over \$500 million in short-term loans in 1979 would have raised serious concern even without the war and its after-effects.

As a result of the convergence of these various factors, Nicaragua now finds itself in a most desperate situation that it only can hope to cope with by means of massive foreign economic assistance from all prospective donors. Equally important is the formulation by the new government of a set of policies capable of inspiring the confidence of the country's entrepreneurs, managers, professionals, and technicians whose full cooperation is essential to Nicaragua's reconstruction.

B. Physical Damage Estimates

Preliminary estimates of the physical damage resulting from the recent war is recapitulated in Table 2. The total damage comes to about U.S. \$580 million, with heaviest damage to the commercial sector (\$270 million) and to manufacturing industry (\$200 million). Note the heavy damage to inventories: \$235 million for both the commercial and industrial

Table 1

DAMAGE TO URBAN BUILDINGS BY CITY AND SECTOR
(In Thousands of Cordobas)*

Departments	Commerce	Industry	Services	Housing	Total
Estelí	47,834	15,592	35,060	118,847	217,333
Matagalpa	18,094	-	19,631	12,022	49,747
Rivas	9,877	-	11,285	12,254	33,416
Managua	12,414	104,746	4,058	80,764	201,982
Chinandega	4,474	-	1,622	1,823	7,919
Chichigalpa	400	-	252	388	1,040
Masaya	51,540	9,356	850	43,556	105,302
León	53,846	1,722	27,286	44,511	127,365
TOTAL	198,479	131,416	100,044	314,165	744,104

Source: Study prepared by the Vice Ministry of Planning, Ministry of Housing and Settlement

* 10 Córdoba = US\$1dollar

Table 2

NICARAGUA: PHYSICAL DAMAGE RESULTING FROM CIVIL WAR
(In Millions of U.S. Dollars)

Housing		42.7
Infrastructure		35.3
Education	10.3	
Health	10.6	
Urban Infrastructure	6.2	
Telecommunications	2.2	
Power	1.1	
Transport	5.0	
Livestock		27.7
Manufacturing Industry		200.0
Machinery and Equipment	80.0	
Buildings and Installations	20.0	
Inventories	60.0	
Frozen Uncollectable Accounts Receivables	40.0	
Commercial Sector		270.0
Buildings	20.0	
Furniture and Equipment	5.0	
Inventories	175.0	
Accounts Receivables	70.0	
Other		<u>5.0</u>
		580.7

Source: CEPAL - Nicaragua: Proyecciones Económicas de los
Acontecimientos Políticos Recientes, August 14, 1979 on
the basis of data supplied by the Government of
Nicaragua

TABLE 3

AGRICULTURE PRODUCTION

(1958 Cordobas converted to US\$)

Year	1977/1978	1978/1979	1979/1980	Percent Change	
				1/2	3/2
	1	2	3	4	5
Total	\$143,020	\$164,050	\$103,460	14.7	-36.9
Export Products	106,870	120,110	67,670	12.4	-43.7
Sesami	520	650	650	25.0	-
Cotton	47,490	52,750	9,980	11.1	-81.1
Cotton Seed	6,560	7,430	1,410	13.3	-18.2
Banana	6,320	6,760	5,390	7.0	-20.3
Coffee	35,160	41,460	41,020	17.9	- 1.1
Sugar Cane	9,530	10,020	8,500	5.1	-15.2
Tobacco	1,290	1,040	720	-19.4	-30.8
Domestic					
Staples	36,150	43,950	35,790	21.6	18.6
Rice	6,090	7,540	6,380	23.8	-15.4
Beans	5,400	7,270	5,550	34.6	-23.7
Corn	6,620	9,280	4,200	40.2	-54.7
Sorghum	1,950	2,910	2,940	49.0	1.0
Tobacco	730	820	590	12.3	-28.0
Other	15,360	16,130	16,130	5.0	-

Source: CEPAL Repercussions Economicas de los Acontecimientos Politicos Recientes, 14 de Agosto de 1979.

sectors. In the industrial sector, damage to machinery and equipment is heavy. Damage to buildings is only a fraction of the damage to inventories in both sectors.

The CEPAL report estimates that of the four hundred industrial enterprises that were in operation before the conflict, about one hundred have suffered serious damage which in some cases resulted in total destruction of the buildings, installations, machinery and inventories. About half of these are medium and large. Particularly severely affected are the industries located on the Northern Highway of Managua. These include plants in the areas of bottling, plastic manufacture, paints, farm tools, ceramics, paper and printing. Substantial damage to manufacturing establishments occurred in Esteli and Masaya.

The economic impact of the war on the agriculture sector is equally as serious especially given the country's extraordinary dependence upon agriculture. The agriculture sector and particularly coffee, cotton and cattle account for 60% of the exports. Forty-six percent of the economically active population works in the agriculture sector, and a high percentage of industrial investment is found in the agricultural transformation and agricultural service industries.

The war has seriously depleted Nicaragua's food reserves. The total supply is estimated at only 11,285 metric tons (6% of normal):

Food Reserves

Crop	Quantity (metric tons)
Corn	9,250
Beans	345
Rice	850
Sorghum	940
Total	<u>11,285</u>

The food crop situation is rather aggravated by shortages in fertilizer and seeds, supplies, insecticides, tools and other equipment, and the working capital required to plan the next season's crops. Supply is not expected to increase appreciably during the present harvest. Major fighting occurred in prime growing areas during April and May when the land preparation and planting season began, thereby reducing the spring harvest and delaying the fall planting. The latter is limited almost solely to sorghum.

Currently there appear to be adequate food crops planted to discount any possibility of major famine, but future supplies and price levels are uncertain. Much of the irrigated rice land was experimental and only part has been planted.

The above table also shows the negative impact of the war on traditional export crops. Cotton production, traditionally a small farm crop, is about 1/4 to 1/3 of normal and coffee production is expected to be off by up to 20%. As a result, foreign exchange earnings will drop significantly.

Dairy, beef, pork, and poultry production also suffered severe losses during the war. The following table gives estimates of losses in these areas that are related to the civil war:

Table 4

Meat and Dairy Losses

Type	Quantity
Dairy and Beef Production	
Bulls	300 head
Inventory reduction in female cows	100,000 head
Lost milk production	1,500,000 liters
Pork Production	
Boars	30 head
Sows	950 head
Market hogs	5,000 head
Poultry	
Laying hens	100,000 hens
Fryers	130,000 chickens

Source: CEPAL and Banco de Desarrollo Agropecuario

C. Impact on GDP and Employment

More significant than the amount of the physical damage are the consequences in terms of lost production. In the case of crop production alone, CEPAL estimates that the production in the crop year 1979-1980 will be 37% lower than the level of the preceding year as a result of the conflict. There is no comparable figure for industry. However, CEPAL estimates that as a result of the conflict, employment in manufacturing industry declined from 80,000 to 45,000. Additional allowance should be made for income foregone due to the paralysis of business establishments, for capital flight, and for the "plundering" of foreign exchange reserves by the previous government just prior to its departure. The total foreign exchange losses through capital flight or illicit withdrawals are estimated at about \$600 million. Thus, the total damage could be estimated at \$1.5 to \$2.0 billion, broken down as follows:

Physical Damage	\$580 million
Reduction in the Gross Domestic Product <u>1/</u>	\$630 million
Loss in foreign exchange reserves	<u>\$600 million</u>
Total	\$1810 million

The \$1.8 billion estimate exceeds (by 20%) the whole amount of the country's 1978 GDP 2/. The estimated value of the physical damage alone constitutes 39% of the 1978 GDP.

The Central Bank's projection of GDP in constant 1958 cordobas for the period 1979-80 appears in Table 6. Note that the country's Gross Domestic Product had already declined by 7% in constant terms in 1978, and is projected to decline by another 25% in 1979. All sectors are scheduled to decline this year - agriculture by 8%, manufacturing industry by 27%, construction by 54%, commerce by 42%, and tertiary activities generally by 29%.

A substantial recovery of the GDP (by 18%) is projected for 1980. The highest rates of recovery are projected for construction (106%), commerce (49%), power (20%), and other services (37%). The recovery projected for manufacturing industries in 1980 -- 13% -- might well be greater. On the whole, the 1980 projection strikes us as being plausible, though conservative. Rapid recovery in the two years following a disaster is in line with recent experience in other countries, notably during the post-earthquake period in the case of Nicaragua (1973-74), and Guatemala (1976-77), owing, in large part, to substantial activity in the construction industry and its ripple effects on other sectors. While the structural problems currently facing Nicaragua are obviously much more serious than in the case of these other disasters, a substantial recovery of GDP over 1980-81 can nevertheless be expected, provided the country receives prompt and substantial economic assistance and that the government is able to formulate a set of specific policies that are reassuring

1/ Calculated on the conservative assumption that the 1979 real GDP would have been identical to that of 1978 without the war.

2/ Equal to 15,026 million cordobas (in current prices) or US \$1,503 million at US \$1 = 10 cordobas.

Table 6

NICARAGUA: GROSS DOMESTIC PRODUCT
(In Millions of Constant 1958 Cordobas)

GROSS DOMESTIC PRODUCT					Percent Changes		
	1977	1978	1979	1980	1978/77	1979/78	1980/79
GROSS DOMESTIC PRODUCT	6,822.8	6,355.3	4,764.8	5,631.7	-6.9	-25.0	18.2
Primary Activities	1,497.2	1,594.4	1,392.4	1,450.1	6.5	-12.7	4.1
Agriculture	961.1	1,034.5	953.0	924.6	7.6	-7.9	-3.0
Livestock	411.9	464.1	378.8	454.2	5.0	-18.4	19.9
Silviculture	39.3	38.4	23.0	23.6	-2.3	-40.1	2.6
Marine Products	54.9	57.4	37.6	47.7	4.6	-34.5	26.9
Secondary Activities	1,958.5	1,817.0	1,280.9	1,530.7	-7.2	-29.5	19.5
Manufacture Industry	1,599.5	1,597.7	1,170.8	1,321.6	-0.1	-26.7	12.9
Construction	340.4	199.9	92.4	190.5	-41.3	-53.8	106.2
Mining	18.6	19.4	17.7	18.6	4.3	-8.8	5.1
Tertiary Activities	3,367.1	2,943.9	2,091.5	2,650.9	-12.6	-28.9	26.7
Commerce	1,468.1	1,261.7	737.8	1,102.4	-14.1	-41.5	49.4
General Government	344.6	384.1	377.0	395.9	11.5	-1.8	5.0
Transport and Communications	373.2	307.4	253.7	291.8	-17.6	-17.5	15.0
Banks, Insurances and Other Financial Institutions	225.6	210.7	179.1	184.1	-6.6	-15.0	2.8
Power and Potable Water	189.3	175.3	150.3	180.4	-7.4	-14.3	20.0
Housing	329.8	296.5	197.4	227.0	-9.8	-33.4	15.0
Other Services	437.5	308.2	196.2	269.3	-29.6	-36.3	37.3

Source: Central Bank of Nicaragua

to the private sector, its trained personnel, the international organizations and potential foreign investors and creditors.

While there is no reliable data on the number of people currently unemployed, it is known to be substantial. CEPAL estimated the average level of unemployment in 1979 (with projection for 1980) on the basis of production/employment ratios for the major economic sectors in the base year 1977. Its projections for 1979 and 1980 assumed constant productivity ratios throughout the period. On the basis of this methodology, the national unemployment rate (expressed as a percentage of the total labor force) was estimated at 33% in 1979 and 28% for 1980.

While the unemployment rate may well be around 33% in the second half of 1979, it appears unlikely that it should remain at close to that high level in 1980 if it can be assumed that (a) a substantial amount of economic assistance becomes available, (b) that much of it can be quickly disbursed, and (c) that the government will adopt appropriate policies. While it may not be possible to return in 1980 to the 15% unemployment rate that prevailed in 1978, the substantial recovery of GDP that is projected for 1980 might be consistent with a reduction of the unemployment rate to a range of 20 to 25 percent.

D. The Balance of Payments and the External Resources Gap

Nicaragua's balance of payments situation is projected in summary form in Annex 1, with supporting data on pages 4, 5, and 7. Two significant points should be borne in mind in interpreting this projection: first, it is "requirements" oriented. It seeks to answer the question, "what would imports have to be in 1979, 1980, and 1981 to enable the economy to replenish its inventories, make essential repairs, get economic activity back to normal, and generally get the reconstruction process off to a good start?" Thus, the projection assumes that sufficient foreign exchange will become available to meet the economy's basic requirements.

Secondly, the presentation is designed to reveal the magnitude of the external resource gaps. Official net capital inflows

show only disbursements of existing loans that have already been signed without making provision for new loans expected or under negotiation; in addition, all amortization payments that fall due during 1979-81 are included for private and official capital, regardless of whether they are owned by private banks, foreign governments or international financial institutions. The overall balance of payments deficit is approximately US \$826 million in 1979, then declines sharply to \$312 million in 1980 and to \$145 million in 1981. Over the three year period, 1979-81, external resources gap is approximately \$1.3 billion.

Suggestions as to how this deficit will be financed are extremely hypothetical at this time. Annex 1, Table 4 shows the projected financing from all donors (plus refinancing of the maturing debt) at \$532 million for 1979, leaving an unfinanced gap of \$794 million. Over the three year period the unfinanced gap is \$317 million.

The reasons for this large balance of payments gap are numerous.

1. A very substantial private capital outflow: according to the Central Bank's still very preliminary estimates, capital flight comes to some \$377 million for 1979. While this amount is treated as a private outflow, it includes the foreign exchange resources withdrawn by officials of the Somoza government just prior to its collapse.

2. A substantial amount of short-term private debt contracted by both the private non-banking and the financial sector due in 1979. The sum is estimated at \$323 million (See Annex 1 Table 4).

3. A substantial amount of short-term public debt also matures in 1979. This debt was contracted for the most part by autonomous public institutions such as the housing bank 1/ and the National Bank which had overextended themselves and realized large operating losses as a result of poor management and political interference. According to available official estimates, total public sector loans falling due in 1979 amount to \$281 million, of which \$147 million 2/ is short-term debt.

1/ BAVINIC

2/ Includes obligations of commercial banks that were recently nationalized.

4. Finally, exports are expected to be seriously depressed in 1979 as a result of reduced coffee prices and a substantial decline in manufacturing exports.

On the assumption that amortization payments due in 1979 will be refinanced (i.e., converted into medium-term loans), and that capital flight will cease, the balance of payments problem in 1980 will be limited to the current account. However, the current account deficit will deteriorate drastically in that year. It is expected to change from a \$36 million surplus in 1979 to a \$239 million deficit in 1980. Exports are expected to decline again in 1980 to \$524 million, or 19% below the 1978 level. The main factor behind this decline is the fact that the 1980 cotton crop is expected to be some 66% below the normal level owing to the unavailability of fertilizer and insecticides at planting time as well as interference with planting as a result of fighting and threats. 3/

Imports should be expected to rise substantially in 1980 on the assumption that the international community will make foreign exchange available to finance reconstruction and minimum consumption requirements - substantial increases are projected in the importation of intermediate and capital goods for both industry and agriculture to replenish inventories and provide spare parts and replacement machinery essential to reactivate the economy. Total imports are expected to increase from \$459 million in 1979 to \$760 million in 1980 and \$798 million in 1981.

E. The Fiscal Gap

The war is expected to have a substantial impact on government revenues and on the fiscal deficit in both 1979 and 1980. During the first semester of 1979, revenue collections declined by 13% in comparison with the first semester of 1978 in spite of government efforts to raise receipts through new tax measures and improved enforcement. The outlook for the second half of the year is considerably worse.

Current revenues in 1979 as a whole are expected to decline by nearly 30% in relation to 1978 as a combined result of reduced agricultural and industrial production, depressed business activity, lower incomes, and a substantial reduction

3/ Many planters were discouraged from planting by direct threats of violence during the months preceding the collapse of the Somoza government.

in the importation of non-essential consumer goods throughout the year. Moreover, the tax administration machinery simply ceased to function in June and July and was still in a confused state in August.

In the area of current expenditures, the Central Bank's projection shows a slight increase in 1979, but only because of the substantial increase in interest payments on the external public debt. If we subtract interest payments from current expenditures, the projected level is about \$166 million for 1979 and slightly higher in 1980. The capital account projection for 1979 is about \$1.8 billion cordobas (\$180 million). This includes fairly high amortization payments to the commercial banking system.

The Central Bank projections and the CEPA projections both indicate a fairly drastic cutback in capital expenditures, other than debt amortization payments, from \$87 million to \$11 million. (See Annex 1, Table 5).

Current revenues according to CEPAL are expected to show a 10% increase in wage payments over the 1979 level as well as moderate recovery in other items. The Government expects to improve revenue collection procedures in 1979 and 1980 and projects that the deficit in current account operations will decline from 900 million cordobas in 1979 to 485 million cordobas in 1980. (See Annex 5, Table 2) Capital expenditures, other than debt amortization are expected to return to the 1978 level in 1980, while the overall budgetary deficit is forecast at US \$140 million, or slightly below the 1978 level.

Although based on preliminary estimates the facts that clearly emerge from this analysis are: (a) current revenue collections in 1980 will be at least US \$50 million below the 1978 level; (b) the US \$76 million in external debt amortization charge that falls due in 1979 cannot be paid and will require refinancing; (c) even after the drastic cutback in actual capital expenditure, the overall 1979 budgetary deficit will reach US \$180 million, or 15% above the 1978 deficit level and double that of 1977. Thus, the government is facing a serious fiscal problem at a time when additional resources are required to reactivate the economy and begin the reconstruction task.

F. Rationale for Use of Cash Grant

The cash grant mechanism is the fastest and most efficient way in which the U.S. Government can respond to both the priority needs of urban and rural Nicaraguans and to the country's pressing economic requirements. The country is bankrupt, both with

respect to foreign exchange reserves and fiscal resources. The situation is especially precarious in the agriculture and construction sectors. Approximately 25,000 people are now homeless as a result of the war. Food shortages are becoming more common, even with contributions from the international donor community. Although corn and rice are now being harvested, the commercial and government banking systems do not have the resources to purchase these products and distribute them throughout the country. Thus, the country faces the very real possibility of farmers leaving the harvest to rot in the field and consumers facing spiraling prices for agriculture products.

The proposed cash grant will help alleviate the situation. It will provide approximately \$2.0 million for materials for rebuilding homes damaged or destroyed during the civil war and approximately \$5.0 million for working capital for INCEI, the grain stabilization institution, to purchase part of the harvest. An additional \$1.0 million from the cash grant will be used by INCEI to repair silos and procure vehicles and other equipment.

The country's needs are immediate. An effective grain stabilization policy will enable the GRN to purchase needed agriculture products - at a reasonable cost and distribute these products to the rural and urban population. Delays in executing this program may lead to unforeseen hardship, food shortages coupled with a high rate of inflation in the short run and jeopardize the new government's ability to develop new programs and policy that will benefit the rural and urban poor.

G. Implications of the Analysis for the U.S. Economic Assistance Program

To have maximum impact on the economy's recovery prospects, the cash grant should meet the following criteria:

1. Immediacy: the most desperate need is for foreign exchange NOW. Aid received during the next six months (beginning September, 1979) has a greater value to the Nicaraguan economy than assistance received a year from now.
2. The program should, if at all possible, contribute to the reduction of both the balance of payments and the government's fiscal deficits.
3. Funds should be channelled into programs that generate immediate employment. The unemployment problem is expected to be particularly severe during the balance of 1979 and the first quarter of 1980.

4. Help in removing bottlenecks to the resumption of economic activity in both the agricultural and manufacturing sectors. There is an urgent need for the importation of a broad variety of raw materials and intermediate goods to feed current production and rebuild inventories. There is also an urgent need for replacement parts for vehicles and machinery and for new machinery to replace that which was seriously damaged or destroyed.

H. Policies of the Government of National Reconstruction (GRN)

Austerity, production, and equity are the principal themes of the GRN's approach to the monumental problems it faces.

Public sector salaries have been slashed, and the number of employees is being steadily reduced as the government identifies superfluous workers, including the "fantasmas," who received salaries from the Somoza Government but performed no work.

The Central Bank is pursuing a non-inflationary credit policy, carefully equilibrating credit expansion with acquisition of foreign exchange. It has temporarily deflated the economy by sterilizing 500- and 1000-cordoba notes for six months, thereby permitting it to channel more credit to highest priority needs. Virtually all of the little credit that can be safely created is being dedicated to production.

The government has accorded highest priority to agricultural production and has made a concerted effort to get as much grain sowed as possible in the few remaining weeks of the planting season. The Minister of Agrarian Reform has repeatedly emphasized that his principal concern is production and that agrarian reform programs must not undermine the urgent national need to produce.

The banking system is also promoting and facilitating the recuperation of the industrial sector as its pinched resources permit.

Equity considerations permeate the policies of the GRN. The 9 July 1979 "Program of the Junta of the Government of National Reconstruction" contains the following words:

"This program...sets the foundation of the new Nicaragua and of a democratic state committed to social justice, and it initiates a revolutionary and nationalistic process of profound transformation which will assure full participation of all sections in the political life, reconstruction, and integral development of the nation and in the humanist transformation of Nicaraguan society...

(The goal is) the substitution of the traditional paternalistic principals of government, with respect to the economy, with governmental action which promotes and stimulates individual and collective participation of all Nicaraguans in the solution of their own problems...

A medium-term plan of reconstruction, transformation, and socio-economic development will be elaborated and executed. Its goal will be the substantial improvement of the level and quality of life of our people, based on the expansion of national production and on equitable distribution of wealth."

I. Strategy

By far the biggest constraint on Nicaragua's economic recovery is the shortage of foreign exchange. High priority import needs -- e.g. for agricultural inputs, agricultural and industrial machinery, raw materials and transport -- far exceed its miniscule reserves, and in the best of circumstances, there are going to be shortages for some time to come.

In order to relieve these serious foreign exchange shortages, the U.S. is tentatively planning an FY 79-81 program which will disburse about \$175 during this period. This will be broken down as follows:

	<u>Assistance</u>	<u>Obligations</u>	<u>FY 79-81 Disbursements</u>
1. FY 80 supplemental package			
a. CIP		75	75
b. Development loans		20	17
2. FY 81 development loans		30	5
3. Title I PL-480 (FY 79-81)		38	38
4. Eximbank and OPIC (FY 79-81)		40	40
Total		<u>203</u>	<u>175</u>

However, even before any large-scale relief effort, the U.S. is planning an \$8.8 million emergency program in FY 79. This will be made up of \$800,000 for operational program grants and \$8 million for a cash grant, which is the subject of this PAAD.

J. Other Donor Programs

1. Export Import Bank and OPIC

Eximbank and OPIC lending and guarantees will reach at least \$40 million during the FY 79-81 period. As a first step, on August 23, Eximbank approved a \$7.5 million guarantee of a \$10 million Wells Fargo one-year loan for purchase of agrochemicals.

2. IDB

The IDB has developed a major program of reconstruction assistance for the GRN and it will commit \$100 million in new projects by the end of CY 79, as follows:

Agricultural credit	\$ 43.5*
Industrial credit	30.0
Small Projects (5 COOP loans)	2.0
From Venezuelan Trust Fund for counterpart**	20.0
Technical assistance	5.0
	<u>\$100.0</u>

The Bank is also actively working with the GRN on a public works reconstruction program for public buildings, schools, etc. on the order of \$50-\$65 million to be committed in late CY 79 or early CY 80.

The IDB also has a \$87 million pipeline for the Rio Blanco-Siuna highway, feeder roads, rural health, rural electrification, university education, agrarian reform, industrial credit, small city sanitary systems, and technical assistance.

3. IMF

The IMF has just approved \$21.5 million of compensatory financing for Nicaragua. We are estimating that an additional \$117 million will be disbursed between now and the end of CY 1981 from standby agreements, the Extended Fund Facility, and perhaps the Witteveen Facility.

* including \$12 million from IFAD.

** 25 years at 7%.

4. IBRD

The first post-revolution IBRD team is scheduled to visit Nicaragua in September. The IBRD is considering a \$50 million program loan which will start disbursing early in CY 1980. New projects are also likely in such areas as agriculture, power, water supply, and housing.

The IBRD carries a \$40 million pipeline: \$18 million in power, \$9 million in education, \$10 million in Managua water supply, and \$3 million in rural sanitation.

5. Others

Several European countries have contributed to emergency relief programs, and some pledges have been made for reconstruction assistance by Germany (\$10.9 million), Spain (\$7.7 million), and Sweden (\$3 million). The UN High Commission on Refugees is making available \$3 million for housing, and Canada has offered \$5 million for agriculture, education, and health.

At least five donors in addition to A.I.D. have plans to help Nicaragua rebuild and repair homes. The United Nations will provide \$600,000 for new construction and repair of damaged homes in the Esteli area and possibly elsewhere. The Government of Venezuela will contribute cash and prefabricated homes for approximately 1,000 families. FUNDE and CEPAD are donating \$250,000 for self help projects using A.I.D. funds, and the IDB is discussing modification of its housing construction loan to include emergency construction.

IV. Detailed Description of Uses of Cash Grant

The proposed \$3.0 million emergency cash grant consists of two components: (a) up to \$6.0 million to finance a grain stabilization program, including the purchase of basic grains (\$5.0 million) and the financing of emergency repairs and equipment (\$1.0 million) for the Instituto de Comercio Exterior e Interior (INCEI); and (b) up to \$2.0 million for low-cost housing repair and reconstruction. The grant will be disbursed to the Central Bank as soon as the Project Agreement is signed. The USAID will sign activity agreements with the two implementing agencies, INCEI and the Ministry of Housing (MDV). INCEI will manage the grain stabilization program, and the MDV will be responsible for carrying out the housing repair and reconstruction program. The Mission is also requesting authority to transfer up to \$1.5 million between the two activities.

A. Grain Stabilization Program

INCEI's food reserves have decreased tremendously, in part because of general disruption within the commercial sector which began even before full scale fighting erupted and in part because its food stocks were looted and facilities and equipment damaged or stolen during the war. This has created short term food shortages. However, perhaps even more importantly, until INCEI reserves increase sufficiently to allow it to stabilize prices for consumers and farmers, Nicaragua will experience excessive price fluctuations which in turn discourage food grain production. Also, in the short run, there is the urgent problem of assuring the purchase and storage of the "primera" harvest, which commences within a few weeks, at a time when INCEI's purchasing power has been drastically reduced.

In order to deal with this problem, approximately \$5.0 million of the grant is for budget support to INCEI. It will be used to purchase rice, corn, sorghum, and beans from the date the agreement is signed through February 1980. This amount, coupled with sales during the period, should assure adequate reserves for the drawdown during the months of March through August.

INCEI plans to purchase up to 50% of expected crop production in its traditional areas of operation. The projected purchases are:

Crop	A.I.D.		Other		Total	
	Metric Tons	Value (US \$000)	Metric Tons	Value (US \$000)	Metric Tons	Value
Corn	14,912	\$1,809	10,555	\$1,274	25,447	\$3,083
Beans	3,068	1,046	2,168	740	5,236	1,786
Rice	5,110	1,043	3,878	737	8,988	1,780
Sorghum	8,829	1,102	6,716	779	15,545	1,881
Total	31,910	\$5,000	23,297	\$3,530	55,216	\$8,530

INCEI's most pressing needs over the next two years are:

1. Operating Capital
2. Budget Support
3. Repairs and Reequipment of Storage Facilities
4. Replacement of Heavy and Light Vehicles

1. Operating Capital

Only 12,000 metric tons of basic grains are currently stored in INCEI warehouses, about six percent of its total capacity. About 3,000 tons are privately owned, leaving INCEI with 9,000 tons of basic grains to control consumer prices. This is far less than is required. In order to control consumer prices, INCEI needs to purchase about 32,000 metric tons of basic grains (15,000 tons of corn, 9,000 tons of sorghum, 5,000 tons of rice, and 3,000 tons of beans). Procurement of these basic crops will cost about \$5 million. They will occupy about one-third of INCEI's storage capacity; private stocks will use an additional one-third of storage capacity and the remaining third will be available to handle food donations and/or surplus production.

2. Budget Support

While it is possible for a price stabilization program to break even or operate at a profit, most basic grain programs lose money, and INCEI has been no exception. Unwise price fixing, underestimation of costs of services, and political factors have contributed to its current debt of about \$21 million. It is virtually without cash. Its normal yearly operating budget is about \$1.5 million. INCEI must start its yearly acquisition cycle during September 1978, so that all operating/purchase costs must come from the budget and not from gross transaction margins. In essence, INCEI will run a budgetary deficit of \$700,000 for the last half of CY 1979 and about \$1,000,000 in CY 1980. Transaction margins should catch up and become fully available in CY 1981.

3. Repairs and Re-equipment of Storage Facilities

Reports from more than 100 storage areas and the three main terminals (total storage capacity of 3,320,000 qq) indicate an immediate need for equipment replacement, repairs and deferred maintenance totalling about \$1.0 million. Some of these repairs will be done in the September-December period, but most can probably be deferred until into 1980. All must be completed, however, by September 1980 in order for INCEI to achieve full operational status. The Mission has completed a detailed inventory of each storage facility. Each will be restored to its original condition so that it has sufficient materials and equipment to buy, test, clean and dry and store the basic grains. In addition to financing repair of the facilities, the cash grant will be used to purchase scales and electric motors that were stolen during the war, replace stolen or damaged temperature sensing devices, and replace belts and screws.

4. Vehicle Replacement

The cash grant also will be used to replace passenger vehicles and trucks that were rendered unservicable during the civil war. The dispersed nature of producing and consuming areas requires close supervision and frequent shifts of basic grains between collection and storage points.

B. Low Cost Housing Repairs and Reconstruction

Approximately \$2.0 million will be used for housing repairs for disaster victims who are poor or disadvantaged. No AID funds will be used to repair commercial structures.

The Ministry of Housing estimates that the damage to housing in Nicaragua is approximately \$36.2 million, including more than 4,149 homes destroyed. AID funded repair work will be located primarily in Managua and Masaya.

Housing repairs and construction to be financed by the cash grant fall into three categories:

1. Minor damage to be repaired through self-help methods by owner or occupant - \$70,000;
2. Major repairs and rehabilitation by a foreman and a small team of workers under MDV contract - \$1,430,000; and
3. Replacement with new construction of houses damaged beyond repair - \$500,000.

The Ministry of Housing will establish a materials supply fund to purchase basic materials, including cement block, sheet roofing, beams, etc., directly from local factories. The Ministry is designing three housing models that will conform to the post earthquake construction code.

The recipients of new or remodeled housing will be expected to pay for the construction services on the following basis:

- a. No charge will be made for self-help projects restoring individual homes to original size and condition;
- b. Enlarged or improved construction will be reimbursed at cost; and
- c. New shelter construction will be reimbursed on the basis of ability to pay.

V. Implementation Procedures and Institutional Analysis

A. Implementation Period

The cash grant will be disbursed to the Central Bank immediately after signing the grant agreement. A.I.D. will sign activity agreements covering the proposed \$6.0 million for the grain stabilization program with INCEI and \$2.0 million with the Ministry of Housing. Both INCEI and the Ministry of Housing plan to disburse the cash grant within the next six to nine months.

B. Implementing Institutions

1. Instituto de Comercio Exterior e Interior (INCEI)

Under the Somoza Government, INCEI's primary responsibility was the regulation of commerce in agriculture production (principally basic grains) by interceding in the internal and export/import markets. INCEI's responsibilities have been expanded, and it now regulates the exportation of all agriculture products, including cotton, meat and coffee and the importation of agricultural inputs.

At present INCEI is undergoing reorganization and will probably be upgraded to cabinet level status. The central office will consist of a Minister and one assistant and two major staff offices, the Office of Studies and Plans and a Commercial Office. It plans to implement its programs through a series of Empresas, one for each major export crop, e.g. cotton, basic grains, coffee, or meat.

At this point, INCEI's operating policies with respect to export crops are still uncertain. The immediate problem is the continuing management of the Empresa de Productos Basicos essentially basic grains for domestic production.

2. Ministry of Housing

The Ministry of Housing will be responsible for rebuilding and repairing damaged homes and building new homes. The proposed project will be under the direct supervision of a Special Coordinator who reports directly to the Minister and Vice Minister. All activities will be channeled through the MDV Execution and Control Division which is under the control of the Vice Minister.

The MDV proposes to establish a materials bank which will purchase the materials needed for the project for local supplies. Minor damage will be repaired through self-help methods by owners and with materials provided by the MDV with MDV technical advisors. New construction will be done by construction contract supervised by MDV personnel.

Separate accounting and reporting will be maintained on the A.I.D. funds. Under the AID-MDV Agreement three operational steps will be followed to account for how A.I.D. funds are used!

1. Identification of specific work to be financed;
2. MDV formal request for funds with an approved work plan; and
3. Signed contracts to perform the work.

The above format already has been used by the MDV to rebuild and repair damaged homes and for new construction caused by the earthquake in 1977. No operational problems are expected in implementing the procedure. Coupled with this prior experience, the MDV is currently implementing a major new home construction project financed by the IDB. This experience adequately demonstrates that MDV personnel are qualified to undertake the purchase of construction materials, supervision of self-help construction, and contracting/supervision of other construction activities.

VI. Financial Plan

The \$3 million cash grant will be disbursed to the Central Bank as soon as the agreement is signed. The Central Bank will disburse the funds to INCEI and the MDV on the basis of signed activity sub-agreements between A.I.D. and the implementing organizations. The Mission estimates that the funds will be budgeted as follows:

	<u>Amount</u>
Ministry of Housing	
a) Minor Repairs	\$ 70,000
b) Major Repairs and Rehabilitation	1,430,000
c) Reconstruction	500,000
Sub-total	<u>\$2,000,000</u>
INCEI	
a) Purchase of Basic Grains:	
Corn	1,809,000
Bean	1,046,000
Rice	1,043,000
Sorghum	1,500,000
b) Repair and Reconstruction	700,000
c) Vehicles	300,000
Total	<u>\$8,000,000</u>

VII. Procurement and Disbursement Procedures and Waivers

A. Procurement with Local Currency Generations

The procurement of goods and services with the local currency proceeds of the cash grant will be made consistent with sound commercial practices. Off-the-shelf purchases will predominate and commodities of Free World (Code 935)* origin will be eligible. All motor vehicles purchased will be of U.S. manufacture. The GRN will be required to submit periodic reports on procurement and disbursement activities showing how the funds are being spent. The commodities to be financed with local currency proceeds under the cash grant include rice, sorghum, beans, corn (approximately 32,000 mt.), scales, motors, pumps, temperature sensing devices, pumps, belts, screws, vehicles, seeds, fertilizers, cement, and other construction materials. The purchase of basic agricultural products is authorized under the provisions of a waiver described below. Normal AID regulations covering the transport of goods and services will be followed.

B. Waiver

Section 604(e) of the Foreign Assistance Act of 1961, as amended, prohibits the procurement of any agricultural commodity outside the United States when the domestic price of such commodity is less than parity. Rice, sorghum, and corn, all parity items, are currently selling for less than parity in the United States. Section 604(e) seeks to assure that the foreign assistance program is not managed in such a way as to depress the market for U.S. agricultural products. The purpose of the proposed purchase is to permit the GRN to purchase basic agricultural products from small farmers in order to ensure stable and reasonable prices for both consumers and farmers. This will assure purchase of the current crop despite recent severe market disruptions and will eliminate excessive price fluctuations and will contribute to the interim recovery program for Nicaragua. Under FAA 614(a) the President has the authority to waive FAA 604(e) when it is in the best interest of the U.S. The proposed transactions are clearly necessary to support the long term political and economic stability of Nicaragua.

C. Disbursement Procedures

Since the needs for foreign exchange and budgetary support are so critical, the entire cash grant will be disbursed upon signature of the emergency cash agreement. Concerning the expected drawdowns of local currencies, INCEI will spend approximately \$2.5 million in October/November, 1979, and \$2.5 million in April/May, 1980, to purchase basic food crops. Most of the remaining \$1.0 million will be used to purchase badly needed equipment and supplies to reestablish its marketing and

*Procurement from Code 935 is critical to the success of the proposed activities. The requirements of INCEI and the MDV are urgent and can be met only by permitting the GRN to procure off-the-shelf and from neighboring countries.

distribution network. Under the MDV timetable, the \$2.0 million will be disbursed over a 7-month period. Most of the grant will be needed during the first 3-4 months to purchase supplies and equipment for a materials supply bank and to finance construction mobilization expenses. Thus, local currencies are expected to be utilized quickly, supporting the initial disbursement of the full \$8.0 million.

Upon deposit of the \$8.0 million with the Central Bank, a special local currency account for up to 80 million cordobas will be established. The Central Bank will submit periodic reports describing the commercial transactions to USAID.

ANNEX I
SUPPORTING ECONOMIC DATA

Table 1

NICARAGUA: SUMMARY OF BALANCE OF PAYMENTS
(In Millions of U.S. Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
1. <u>Current Account Balance, Net</u>	<u>-175.7</u>	<u>9.9</u>	<u>36</u>	<u>-289</u>	<u>-136</u>
<u>Trade Balance, Net</u>	<u>-101.8</u>	<u>52.1</u>	<u>109</u>	<u>-236</u>	<u>- 88</u>
Exports (FOB) <u>1/</u>	636.8	646.0	568	524	710
Imports (CIF) <u>2/</u>	-738.6	-592.9	-459	-760	-798
<u>Services Balance, Net</u>	<u>- 84.9</u>	<u>- 52.2</u>	<u>-143</u>	<u>- 73</u>	<u>- 63</u>
<u>Transfers, Net</u>	<u>11.0</u>	<u>10.0</u>	<u>70</u>	<u>20</u>	<u>15</u>
2. <u>Private Capital, Net</u>	<u>- 62.6</u>	<u>-275.1</u>	<u>-698</u>	<u>- 8a/</u>	<u>25</u>
Direct Investments	10.0	7.0	2		
Loan Disbursements	16.0	9.0	-		
Amortization	- 9.0	- 10.0	-323	<u>3/</u>	
Commercial Credits and Other (Capital Flight and Errors and Omissions for 1979-81)	- 79.6	-281.1 ^{4/}	-377 ^{a/}		25
3. <u>Official Capital, Net</u>	<u>196.4</u>	<u>50.9</u>	<u>-164</u>	<u>- 15</u>	<u>- 34</u>
Loan Disbursements <u>5/</u>	245.3	101.6	115	100	71
Amortization ^{5/}	- 50.2	- 52.2	-281	-117	-107
Other	1.3	1.5	2	2	2
4. <u>Arrears</u>	-	<u>39.4</u>			
5. <u>Errors and Omissions</u>	<u>- 14.7</u>	<u>- 10.3</u>	-	-	-
6. <u>Overall Balance (1 through 5)</u>	<u>- 56.6</u>	<u>-224.3</u>	<u>-826</u>	<u>-312</u>	<u>-145</u>

(Financing of deficit on following page)

a/ Projected as a residual by the Central Bank

Table 1 (Continued)

	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>Total 1979-81</u>
6. <u>Balance of Payments Deficits</u>	-826	-312	-145	-1283
7. <u>Projected New Financing (Other than New U.S. Assistance)</u>				

	Amount Authorized	Disbursement Projections			
		1979	1980	1981	Total
IDB	\$127 ^{7/}	15	25	40	80
IBRD	85		40	20	60
IMF	138 ^{8/}	22	40	40	102
Venezuela Investment Fund	20	20	-	-	20
Other Donors (Bilateral)	30	10	10	10	30
AID Emergency	10	10	0	0	10
Insurance Payments	20	10	10	0	20
Refinancing of Private Sector Debt	203 ^{9/}	203	-	-	203
Refinancing of Public Sector Debts to Commercial Banking System	401 ^{10/}	232	92	77	401
Refinancing of Concessionary Debt from Donor Countries	40	10	15	15	40
Total	\$1074	532	232	202	966

8. Uncovered gap (-) over 1979-81

\$1283 - 966 = 317	-294	-80	+57	-317
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Footnotes to Table 1

- 1/ For breakdown, see Table 5
- 2/ Breakdown in Table 6
- 3/ Breakdown in Table 7
- 4/ Central Bank projection. The item consists mostly of capital flight.
- 5/ Central Bank projection on the basis of existing active loans only. Any disbursements and amortization payments of new loans (i.e., not yet signed) are excluded.
- 6/ Includes short-term public sector obligations to foreign banks in 1979.
- 7/ Excludes \$20 million from the Venezuela Investment Fund which is shown separately. Includes new IDB loans only.
- 8/ SDR 90 million (EFF) + SDR 17 million (unconditional advance) = SDR 107 million = U.S. \$138 million. It is assumed that the SDR 17 million advance (US \$22 million) will be spent in 1979, and that the EFF will be disbursed in tranches of \$40 million annually beginning in 1980.
- 9/ See Table 7 for breakdown.
- 10/ Projected by the Central Bank on the assumption that all external public debt to the banking system outstanding on December 31, 1978 will be renegotiated. The amount is so large in 1979 owing to the considerable amount of short-term debt of autonomous public institutions that falls due in that year.

Source: For 1977-78, Banco Central de Nicaragua. For 1979-81, projected by AID Economic adviser in close collaboration with staff of Economic Research Section of the Central Bank.

Table 2

EXPORT PROJECTIONS 1979-81
(In Millions of U.S. Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
<u>Total Deficit, FOB</u>	<u>636.8</u>	<u>646.0</u>	<u>568</u>	<u>524</u>	<u>710</u>
<u>Agricultural and Marine Products</u>	<u>401.8</u>	<u>375.9</u>	<u>331</u>	<u>281</u>	<u>424</u>
Cotton	150.4	140.9	145 ^{1/}	58 ^{1/}	165 ^{1/}
Coffee	198.8	199.6	157 ^{2/}	192 ^{2/}	222 ^{2/}
Seafood	22.3	14.7	12	10	13
Bananas	4.5	4.8	4	6	6
Tobacco	4.2	3.0	3	3	3
Other	21.9	12.9	10	12	15
<u>Manufacture Products</u>	<u>225.3</u>	<u>259.3</u>	<u>227</u>	<u>233</u>	<u>275</u>
<u>Foodstuffs</u>	<u>84.3</u>	<u>110.8</u>	<u>123</u>	<u>117</u>	<u>137</u>
Meat	36.3	67.7	88 ^{3/}	70 ^{3/}	87 ^{3/}
Sugar	27.8	19.6	17	23	25
Other	20.2	23.5	18	24	25
Wood Products	10.8	9.7	6	5	5
Textiles	12.0	11.5	6	6	8
Leather and Leather Goods	4.8	8.3	6	5	7
Chemical Products	51.0	52.2	43	49	55
Cottonseed By-Products	10.9	12.3	10	6	15
Other	51.5	54.5	33	45	48
Minerals	9.7	10.8	10	10	11

1/ Projected by Central Bank. Assumes the following:

- In 1979, export of 2,460,000 quintales at a price of \$59.0 per quintal
- In 1980, export of 913,000 quintales at a price of \$63.0 per quintal
- In 1981, export of 2,579,000 quintales at a price of \$64.0 per quintal

2/ Projected on basis of following assumptions:

- In 1979, export of 1,203,000 quintales at a price of \$130 per quintal
- In 1980, export of 1,200,000 quintales at a price of \$160 per quintal
- In 1981, export of 1,390,000 quintales at a price of \$160 per quintal

3/ Assuming an output of about 70,000,000 pounds annually over 1979-81 with an average price per pound of \$1.25 in 1979, \$1.00 in 1980 and 1.25 in 1981.

Source: For 1977-78, Central Bank of Nicaragua; for 1979-81, AID Economic Advisor in collaboration with Central Bank

IMPORT PROJECTIONS
(In Millions of U.S. Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
Total Imports, CIF	<u>761.9</u>	<u>793.9</u>	<u>459</u>	<u>760</u>	<u>798</u>
<u>Consumer Goods</u>	<u>177.0</u>	<u>147.9</u>	<u>145</u>	<u>157</u>	<u>141</u>
<u>Non-Durables</u>	<u>110.6</u>	<u>98.1</u>	<u>127</u>	<u>130</u>	<u>108</u>
Food	30.7	31.2	44 ^{1/}	52 ^{1/}	33
Pharmaceutical Products	32.3	29.2	47 ^{2/}	40 ^{2/}	35
Other	47.6	37.7	36	38	40
<u>Durables</u>	<u>66.4</u>	<u>49.8</u>	<u>18</u>	<u>27</u>	<u>33</u>
Passengers Cars	43.5	33.6	10 ^{3/}	15 ^{3/}	18 ^{3/}
Other	22.9	16.2	8 ^{3/}	12 ^{3/}	15 ^{3/}
<u>Intermediate Goods</u>	<u>252.5</u>	<u>217.8</u>	<u>148</u>	<u>250</u>	<u>255</u>
Materials for Agriculture	40.2	36.7	20	50 ^{4/}	45 ^{4/}
Materials for Industry	212.3	181.1	128	200 ^{4/}	210 ^{4/}
<u>Petroleum Products</u>	<u>103.0</u>	<u>89.1</u>	<u>88</u>	<u>123</u>	<u>156</u>
Crude and Partially Refined	78.0	57.4	70	85	110
Petroleum Derivatives	25.0	31.3	18	38	46
<u>Capital Goods</u>	<u>225.3</u>	<u>139.0</u>	<u>78</u>	<u>230</u>	<u>246</u>
Agriculture	19.5	12.8	10	20	18
Industry	113.8	75.2	38	125 ^{5/}	135 ^{5/}
Machinery	51.8	51.9	-	-	-
Other	62.0	23.3	-	-	-
Transportation Equipment	60.0	25.4	16	35 ^{6/}	38
Construction Materials	32.0	25.6	14	50 ^{6/}	55 ^{6/}
Other	.2	.2	-	-	-

1/ Inclusive of donated food. Additional food imports are estimated as follows:

For 1979:

Corn: 300,000 quintales x \$9 per quintal = \$2,700,000

Beans: 400,000 quintales x \$15 per quintal = \$6,000,000

Sorghum: 100,000 quintales x \$7 per quintal = \$700,000

Rice: 100,000 quintales x \$15 per quintal = \$3,000,000

\$13,900,000

For 1980:

Corn: 2,000,000 quintales x \$9 per quintal = \$18,000,000

Beans: 200,000 quintales x \$15 per quintal = \$3,000,000

\$21,000,000

Footnotes to Table 3 (cont.)

2/ Imports of pharmaceutical products through May of 1979 totalled \$12 million. It was estimated that \$35 million will be needed during the rest of the year to replace looted and destroyed inventories. Most of this is being brought in as donations. A further \$10 million allowance for inventory replacement was made for 1980.

3/ Assumes strict control over importation of non-essential consumer goods over 1979-81.

4/ Allows for the following rates of inventory replacement in 1980 and 1981:

	1980	1981
Materials for agriculture	\$12 million	\$15 million
Materials for industry	\$55 million	\$35 million

In projecting the import demand for raw materials and intermediate goods account was taken of the fact that the requirements to feed current output will be below normal in 1979 and 1980 owing to damage to plant and equipment.

5/ Allows \$50 million/1980 for the importation of machinery and parts to replace destroyed or damaged equipment. Roughly similar allowance was made for 1981.

6/ Assumes an extra requirement for construction materials of about \$25 million in 1980 and \$30 million in 1981.

Source: For 1977-78, Central Bank of Nicaragua. For 1979-80, AID Economic Advisor in collaboration with Central Bank staff.

Table 4

PRIVATE SECTOR EXTERNAL FINANCIAL OBLIGATIONS
TO BE PAID IN 1979 AND AMOUNT OF REFINANCING REQUIRED
(In Millions of U.S. Dollars)

Private Non-Banking Sector	213.0
Banking Sector, Loans Due	53.2
Debt Subject to Bank Guarantees	
Amount in Arrears	56.0
Additional Guarantees That Will be Maturing	<u>2.5</u>
Total Owed or Falling Due in 1979	324.7
Amount of Foreign Exchange Owed by Central Bank to Private Citizens ^{1/}	<u>50.0</u>
Total of Above	374.7
Amount Included in Public Sector Account ^{2/}	<u>- 51.9</u>
Total Net Private Sector Obligations Falling Due in 1979	322.8
Amount Paid During Jan.-May 1979	<u>-120.0</u>
Net Amount Required Refinancing	202.8

^{1/} People who already paid cordobas for foreign exchange (to pay debts or imports) but have not received the dollar proceeds.

^{2/} Since private banks were taken over by the government, their debts were treated as public sector obligations and entered in the public sector account.

Source: Banco Central de Nicaragua, Centro Bancario

NICARAGUA: REVENUES AND EXPENDITURES OF THE CENTRAL GOVERNMENT
(In Millions of Cordobas)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>
1. <u>Current Revenues</u>	<u>1796</u>	<u>1621</u>	<u>1155</u>	<u>1763</u>
<u>Tax Revenues</u>	<u>1638</u>	<u>1448</u>	<u>907</u>	<u>1575</u>
Direct Taxes	<u>392</u>	<u>363</u>	<u>228</u>	<u>394</u>
Income Taxes	274	270	173	294
Property	62	93	55	102
Other Direct	56)			
Indirect (on Consumption)	711	626	383	679
Foreign Commerce	<u>494</u>	<u>384</u>	<u>215</u>	<u>417</u>
Import Taxes	453	377	207	408
Export Taxes	41	7	8	9
Transactions & Legal Documents	41	75	81	83
Non-Tax Revenues	<u>158</u>	<u>173</u>	<u>248</u>	<u>182</u>
2. <u>Current Expenditures</u>	<u>1462</u>	<u>1979</u>	<u>2056</u>	<u>2208</u>
Wages and Salaries	569	702	911	1002
Purchase of Goods & Services	385	615	409	449
Current Transfers	323	362	257	283
Interest on Public Debt	<u>185</u>	<u>300</u>	<u>479</u>	<u>474</u>
Internal	14	53	35	130
External	171	247	444	344
3. Savings on Current Operations	<u>334</u>	<u>- 358</u>	<u>- 901</u>	<u>- 485</u>

Table 5
(Continued)

	<u>1977</u>	<u>1978</u>	<u>1979</u>		<u>1980</u>
			<u>CEPAL</u>	<u>CENTRAL BANK</u>	
4. <u>Capital Expenditures</u>	<u>1229</u>	<u>1203</u>	<u>899</u>	<u>216</u>	<u>931</u>
Direct Investment, "Real" <u>1/</u>	585	402	61	61	402
Financial Investment <u>2/</u>	212	234	14	14	234
Indirect Investment <u>3/</u>	206	185	45	44	185
Debt Amortization	<u>226</u>	<u>382</u>	<u>779</u>	<u>96</u>	<u>110</u>
Internal	58	69	19	19	-
External	168	313	760	77	110
5. Total Expenditures	<u>2691</u>	<u>3182</u>	<u>2955</u>	<u>2272</u>	<u>3139</u>
6. Overall Surplus or Deficit	<u>- 895</u>	<u>-1561</u>	<u>-1800</u>	<u>-1117</u>	<u>-1381</u>

1/ "Real Direct Investment" refers to investment directly undertaken by the Central Government, such as road or school construction.

2/ "Financial Investment" refers to Central Government investment undertaken through an autonomous institution which channels funds to the private sector, such as a housing bank or an agricultural credit bank.

3/ "Indirect Investments" are mainly transfers or subsidies to public institutions such as the University.

Source: CEPAL Report (Op. Cit) and Central Bank

Table 6

NICARAGUA: PLANNED BANK CREDIT EXPANSION, 1979-80
(In Millions of Cordobas)

	<u>1976/77</u>	<u>1977/78</u>	<u>1978/79</u>	<u>1979/80</u>
<u>Total Domestic Bank Credit Expansion</u>	<u>645</u>	<u>1318</u>	<u>877</u>	<u>1303</u>
TO:				
Central Government	69	579	715	800
Autonomous Institutions	8	-22	0	0
Private Sector	568	338	62	604

Source: Central Bank of Nicaragua

ANNEX II
LEGAL REQUIREMENTS

3A(1) - COUNTRY CHECKLIST

A. GENERAL CRITERIA FOR COUNTRY

1. FAA Sec. 481. Has it been determined that the government of recipient country has failed to take adequate steps to prevent narcotics drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully? The Government of Nicaragua supports the provisions of the Drug Abuse Prevention and Control Act of 1970.
2. FAA Sec. 620(b). If assistance is to a government, has the Secretary of State determined that it is not controlled by the international Communist movement? Yes.
3. FAA Sec. 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) debt is not denied or contested by such government? No
4. FAA Sec. 620(e)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities? No
5. FAA Sec. 620(f); App. Sec. 103. Is recipient country a Communist country? Will assistance be provided to the Democratic Republic of Vietnam (North Vietnam), South Vietnam, Cambodia, or Laos? No

A.

6. FAA Sec. 620(i). Is recipient country in any way involved in (a) subversion of, or military aggression against, the United States or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression? No
7. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction, by mob action, of U.S. property? No
8. FAA Sec. 620(l). If the country has failed to institute the investment guaranty program for the specific risks of expropriation, inconvertibility or confiscation, has the AID Administrator within the past year considered denying assistance to such government for this reason? Nicaragua has instituted an Investment Guarantee Program.
9. FAA Sec. 620(o); Fishermen's Protective Act, Sec. 5. If country has seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters, Nicaragua has not seized, or imposed any penalty or sanctions against, any U.S. fishing activities in international waters.
- a. has any deduction required by Fishermen's Protective Act been made?
- b. has complete denial of assistance been considered by AID Administrator?
10. FAA Sec. 620(q); App. Sec. 504. (a) Is the recipient country in default on interest or principal of any AID loan to that country? (b) Is country more than one year in default on interest or principal on U.S. loan made pursuant to program for which funds appropriated under Approp. Act, unless debt was earlier disputed, or appropriate steps taken to cure default? The GKN is not in default on interest or principal of any AID loan. Since the new government is bankrupt, some of its loans will have to be rescheduled.
11. FAA Sec. 620(s). What percentage of country budget is for military expenditures? How much of foreign exchange resources spent on military equipment? How much spent for the purchase of sophisticated weapons systems? (Consideration of these points is to be coordinated with the Bureau for Program and Policy Coordination, Regional Coordinators and Military Assistance Staff (PPC/RC).) Since the government is new, this information is not available. Under the Somoza regime, the expenditures were close to 9.1% of the country's budget.

A.

- 12. FAA Sec. 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption? No

- 13. FAA Sec. 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the AID Administrator in determining the current AID Operational Year Budget? The country is current on its obligations to the U.N.

- 14. FAA Sec. 620A. Has the country granted sanctuary from prosecution to any individual or group which has committed an act of international terrorism? No

- 15. FAA Sec. 659. If (a) military base is located in recipient country, and was constructed or is being maintained or operated with funds furnished by the United States, and (b) U.S. personnel carry out military operations from such base, has the President determined that the government of recipient country has authorized regular access to U.S. correspondents to such base? Nicaragua does not have any U.S. military bases.

- 16. FAA Sec. 666. Does the country object, on basis of race, religion, national origin or sex, to the presence of any officer or employee of the U.S. there to carry out economic development program under FAA? No

- 17. FAA Sec. 669. Has the country delivered or received nuclear reprocessing or enrichment equipment, materials or technology, without specified arrangements on safeguards, etc.? No

- 18. FAA Sec. 670. Has the country delivered or received nuclear reprocessing, equipment, material or technology? Is the country not a "nuclear-weapon state" as defined in Article IX(3) of the Nuclear Non-Proliferation Treaty and on which detonates a nuclear explosive device? The country does not have any known nuclear reprocessing equipment, material or technology.

- 19. FAA Sec. 901. Has the country denied its citizens the right or opportunity to emigrate? No

B. FUNDING CRITERIA FOR COUNTRY

1. Security Supporting Assistance Country Criteria

- a. FAA Sec. 502B. Has the Department of State made findings which indicate that the country has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, is program in accordance with policy of this Section? No

b. FAA Sec. 531. Is the Assistance to be furnished to a friendly country, organization, or body eligible to receive assistance?

Yes

c. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

The GRN will receive an emergency cash grant in lieu of commodities.

2. Development Assistance Country Criteria

a. FAA Sec. 102(c), (d). Have criteria been established, and taken into account, to assess commitment and progress of country in effectively involving the poor in development, on such indexes as: (1) small-farm labor intensive agriculture, (2) reduced infant mortality, (3) population growth, (4) equality of income distribution, and (5) unemployment.

New criteria are being developed to cover these sections.

b. FAA Sec. 115. Will country be furnished, in same fiscal year, either security supporting assistance, or Middle East peace funds? If so, has the Congress specifically authorized such funds, or is assistance for population programs, humanitarian aid through international organizations, or regional programs?

Yes

c. FAA Sec. 116. Can it be demonstrated that contemplated assistance will directly benefit the needy? If not, has the Department of State made findings which indicate that this government has engaged in a consistent pattern of gross violations of internationally recognized human rights?

Yes

3A(2) - NONPROJECT ASSISTANCE CHECKLIST

A. GENERAL CRITERIA FOR NONPROJECT ASSISTANCE

1. App. Unnumbered; FAA Sec 653(b)

(a) Describe how Committees on Appropriations of Senate and House have been or will be notified concerning the nonproject assistance;

Hearings have been held before the Subcommittee on Foreign Operations, House Appropriations Committee.

(b) Is assistance within (Operational Year Budget) country or international organization allocation reported to the Congress (or no more than \$1 million over that figure - 100%)?

No, the assistance is incremental to the level that was reported to Congress. The Advice of Program Change and 653(b) notifications have been sent to Congress and the waiting periods have expired.

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2. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

No further legislation is required.
 3. FAA Sec. 209, 619. Is assistance more efficiently and effectively given through regional or multilateral organizations? If so why is assistance not so given? Information and conclusion whether assistance will encourage regional development programs. If assistance is for newly independent country, is it furnished through multilateral organizations or in accordance with multilateral plans to the maximum extent appropriate?

The project is designed to provide immediate budget support to the GRN. It is doubtful that more effective or efficient assistance could be provided through regional or multilateral organizations.
 4. FAA Sec. 601(a); (and Sec. 201(f) for development loans). Information and conclusions whether assistance will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.

The project may enable INCEI to market agricultural products more efficiently and improve their technical ability to manage the grain stabilization program.
 5. FAA Sec. 601(b). Information and conclusion on how assistance will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

The project is not designed to support these objectives. The FY 81 program may include assistance programs to encourage U.S. private trade and investment programs.
 6. FAA Sec. 612(b); Sec 636(h). Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the United States are utilized to meet the cost of contractual and other services.

The emergency cash grant is designed to enable the GRN to meet local currency requirements related to the rehabilitation program.
 7. FAA Sec. 612(4). Does the United States own excess foreign currency and, if so, what arrangements have been made for its release?

The U.S. does not own excess foreign currency.

B. FUNDING CRITERIA FOR NONPROJECT ASSISTANCE

1. Nonproject Criteria for Security Support Assistance

a. FAA Sec. 531. How will this assistance support promote economic or political stability?

The assistance will permit budget support to ameliorate pressing balance of payment problems.

2. Nonproject Criteria for Development Assistance

a. FAA Sec. 102(c); Sec. 111; Sec. 281a. Extent to which activity will (1) effectively involve the poor in development, by extending access to economy at local level, increasing labor-intensive production, spreading investment out from cities to small towns and rural areas; and (2) help develop cooperatives, assist rural and urban poor to help themselves toward better life, and otherwise encourage democratic private and local government institutions?

The project will assure a market for basic crops to the vast majority of Nicaragua's rural farmers, and will provide housing for about 1,500 rural and urban poor families.

b. FAA Sec. 103, 103A, 104, 105, 106, 107. Is assistance being made available: [include only applicable paragraph -- e.g., a, b, etc. -- which corresponds to sources of funds used. If more than one fund source is used for assistance, include relevant paragraph for each fund source.]

B2b

(1) [103] for agriculture, rural development or nutrition; if so, extent to which activity is specifically designed to increase productivity and income of rural poor; [103A] if for agricultural research, is full account taken of needs of small farmers;

Assistance is being provided to encourage small farmers to grow more basic crops.

(2) [104] for population planning or health; if so, extent to which activity extends low-cost, integrated delivery systems to provide health and family planning services, especially to rural areas and poor; extent to which assistance gives attention to interrelationship between (A) population growth and (B) development and overall improvement in living standards in developing countries. Is activity designed to build motivation for small families in programs such as education in and out of school, maternal and child health services, agriculture production, rural development, and assistance to urban poor?

- (3) [105] for education, public administration, or human resources development; if so, extent to which activity strengthens nonformal education, makes formal education more relevant, especially for rural families and urban poor, or strengthens management capability of institutions enabling the poor to participate in development;
- (4) [106] for technical assistance, energy, research, reconstruction, and selected development problems; if so, extent activity is:

(a) to help alleviate energy problem;

(b) reconstruction after natural or manmade disaster;

(c) for special development problem, and to enable proper utilization of earlier U.S. infrastructure, etc., assistance;

(d) for programs of urban development, especially small labor-intensive enterprises, marketing systems, and financial or other institutions to help urban poor participate in economic and social development.

- (5) [107] by grants for coordinated private effort to develop and disseminate intermediate technologies appropriate for developing countries.

Approximately \$2,000,000 is provided to reconstruct homes and build new homes destroyed during recent civil war.

c. FAA Sec. 207; Sec. 113. Extent to which assistance reflects appropriate emphasis on: (1) encouraging development of democratic, economic, political, and social institutions; (2) self-help in meeting the country's food needs; (3) improving availability of trained worker-power in the country; (4) programs designed to meet the country's health needs; (5) other important areas of economic, political, and social development, including industry; free labor unions, cooperatives, and Voluntary Agencies; transportation and communication; planning and public administration; urban development, and modernization of existing laws; or (6) integrating women into the recipient country's national economy.

The project is designed to support agricultural self-sufficiency in rice, sorghum, beans, and corn.

d. FAA Sec. 201(a). Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civic education and training in skills required for effective participation in governmental and political processes essential to self-government.

The project utilizes local manpower both to manage the grain stabilization program and rehabilitate homes destroyed in the civil war.

GRANT AGREEMENT
BETWEEN THE
REPUBLIC OF NICARAGUA
AND THE
UNITED STATES OF AMERICA

By this Agreement made and entered into on the ___ day of September, 1979, the Republic of Nicaragua (hereinafter referred to as the "Grantee"), and the United States of America, acting through the Agency for International Development (hereinafter referred to as "AID"), hereby agree as follows:

Section 1. The Grant. For the purpose of assisting the Grantee to alleviate a severe balance of payments problem and to maintain its economic development following the recent civil war, AID, pursuant to the Foreign Assistance Act of 1961, as amended, hereby grants to the Grantee Eight Million United States Dollars (\$8,000,000).

Section 2. Condition Precedent to Disbursement. Prior to disbursement under this Agreement, or to the issuance by AID of documentation pursuant to which disbursement will be made, the Grantee will, except as AID may otherwise agree in writing, furnish to AID, in form and substance

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satisfactory to AID, a statement of the name or names of the persons holding or acting in the office of the Grantee specified in Section 12, and a specimen signature of each person specified in such statement.

Section 3. Notification of Satisfaction of Condition Precedent. When AID has determined that the condition precedent specified in Section 2 has been met, AID will promptly notify the Grantee.

Section 4. Terminal Date for Condition Precedent. If the condition specified in Section 2 has not been met within ninety (90) days from the date this Agreement is made and entered into, or such later date as AID may agree to in writing, AID, at its option, may terminate this Agreement by written notice to the Grantee.

Section 5. Disbursement. Disbursement of the funds made available under this Agreement will be made in one installment pursuant to a request for disbursement by the Grantee and subsequent to satisfaction of the Condition Precedent to disbursement under Section 2. The request for disbursement will be submitted to the Mission Director, USAID Mission to Nicaragua, on AID Form 1130-2 (Financing Request). In accordance with the request for disbursement, AID will deposit the funds into an account of the

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Grantee at a United States bank designated by the Grantee.

Section 6. Terminal Date for Requesting Disbursement.

The terminal date for requesting disbursement of funds will be six (6) months from the date this Agreement was made and entered into, except as AID may otherwise agree in writing.

Section 7. Special Accounts for Development Programs.

A. For the purpose of financing the local currency cost of development programs, the Grantee will establish two special accounts, and within three months from the date of disbursement of funds under this Agreement, deposit therein currency of the Republic of Nicaragua equivalent in amount to the United States Dollar disbursement made under this Agreement and in accordance with the terms of Subsection B below. The highest rate of exchange which is not unlawful in the Republic of Nicaragua on the date of dollar disbursement shall be used in determining the total amount required to be deposited in the account.

B. Funds deposited in the special accounts shall be used as follows:

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(i) \$2,000,000 to finance local currency costs of the Ministry of Housing (MDV) related to repair and reconstruction of houses damaged or destroyed during the civil war, such activities to be more specifically described in an activity agreement to be entered into between the MOH and AID; and

(ii) \$6,000,000 to finance local currency costs of the Instituto de Comercio Exterior e Interior (INCEI) related to a grain stabilization program and repairs to silos and other equipment (or replacement thereof) of INCEI damaged during the civil war, such activities to be more specifically described in an activity agreement to be entered into between INCEI and AID.

Upon written approval of AID, funds may be transferred from one special account to the other; provided, that not to exceed \$1.5 million equivalent in the aggregate shall be so transferred

C. Disbursement from the special accounts for development programs meeting the criteria set forth in Section 7.B. shall be made by the Grantee in accordance with such procedures and at such times as determined to be appropriate by the Grantee; provided, that all funds deposited in the

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special account shall be disbursed within eighteen (18) months from the date this Agreement is made and entered into.

D. The Grantee will provide to AID at six month intervals following the date this Agreement is made and entered into until such time as all special account funds have been disbursed, financial reports which show:

(a) cumulative deposits to and disbursements from the special accounts; and

(b) for all activities, the budget amount, disbursements made during the six month period and cumulative disbursements.

These reports, certified as correct by the President of the Central Bank of Nicaragua, subject to audit, will be submitted to AID within sixty (60) days after the close of each six month period.

E. The Grantee will, at mutually agreed upon times, afford representatives of AID the opportunity to observe activities financed under the special accounts.

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Section 8. Taxation. This Agreement and the amount to be granted hereunder shall be free from any taxation or fees imposed under any laws in effect within the Republic of Nicaragua.

Section 9. Use of Funds. The Grantee agrees that the funds provided hereunder shall not be used to finance military requirements of any kind including the procurement of commodities or services for military purposes.

Section 10. Records. The Grantee agrees that financial records relating to the utilization of funds granted by AID under this Agreement and the funds deposited into the special accounts by the Grantee shall be kept in accordance with the Grantee's usual accounting procedures, which shall follow generally accepted accounting procedures. All such financial records shall be maintained for at least three years after the final disbursement of funds from the special accounts, and shall be made available at any reasonable time to authorized representatives of AID for the purpose of examination and inspection.

Section 11. Communications and Language. Any notice, request, document or other communication submitted by either party to the other under this Agreement will be in

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writing or by telegram, cable or radiogram, and will be deemed duly given or sent when delivered to such party at the following addresses:

To the Grantee

Mail Address:

Alternate Address for Cables:

To AID

Mail Address: USAID Mission to Nicaragua
American Embassy
Managua, Nicaragua

Alternate Address for Cables:

All such communications will be in English, unless the parties hereto otherwise agree in writing. Other addresses may be substituted for the above upon the giving of notice. The English language version of this Agreement shall be controlling for purposes of interpretation.

Section 12. Representatives. For all purposes relevant to this Agreement, the Grantee will be represented by the individual holding or acting in the office of the _____, and AID will be represented by the individual holding or acting in the office of the Mission Director, USAID Mission to Nicaragua, each of whom, by written notice, may designate additional representatives for all purposes other than revising project details. The names of the representatives of the Grantee, with specimen signatures, will be provided to AID, which may accept as duly authorized any

instrument signed by such representatives in implementation of this Agreement, until receipt of written notice of revocation of their authority.

IN WITNESS WHEREOF, the Republic of Nicaragua and the United States of America, each acting through its duly authorized representative, have caused this Agreement to be signed in their names and delivered as of the day and year first above written.

Republic of Nicaragua

By: _____

Title: Minister of Finance

By: _____

Title: President, Central Bank
of Nicaragua

United States of America

By: _____

Title: Director, United
States AID Mission to
the Republic of Nicaragua