

**COUNTRY DEVELOPMENT
STRATEGY STATEMENT**

**USAID/NICARAGUA
1991 - 1996**



June 14, 1991

USAID/Nicaragua CDSS
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I. EXECUTIVE SUMMARY

The development needs of Nicaragua over the period 1991-1996 are enormous. During the ten year period of Sandinista rule prior to the elections of 1990, economic mismanagement, war, an economic embargo, and political polarization seriously eroded the basic institutions, infrastructure, values, and policy framework necessary for economic and political development. The new government has been able to make only limited, but important, progress in addressing the huge economic, political, and social needs facing the nation.

Nicaragua faces unique development problems both because of the degree and scope of deterioration in all sectors and because it faces the added difficulties of moving from a socialist to democratic/free market orientation in the aftermath of a civil war which caused broad social disruption and politicization. For development to occur which will bring improved economic and social well-being for Nicaraguan men, women, and children there must be:

Broad-based, sustainable, economic growth - Nicaraguans must have greater potential for earning increased income on a sustainable basis and the country as a whole must be able to address its staggering debt and improve its position in the international market;

A functioning, stable democracy - Nicaraguan citizens must agree on new rules of society based on democratic values and improve the institutions which can help make democracy work;

A healthy and literate population - Nicaraguans must have access to adequate food, potable water, quality health care, basic education, and an environment conducive to physical and mental health.

DEVELOPMENT NEEDS: The above conditions do not exist in Nicaragua for a variety of reasons. The Mission's analysis points to a series of economic, political and social needs that must be addressed for development to occur along these lines in the future.

Economic Needs - The Nicaraguan economy has suffered from rampant hyper-inflation and seven years of negative growth have left many in poverty. To restore growth, Nicaragua needs:

Increased Investment - Nicaragua needs a revitalized private sector to promote economic recovery and growth through increased investment. For increased investment to occur there will need to be price and exchange rate stabilization, a supportive free-market policy framework, resolution of property rights disputes, demonstrated government effectiveness in key areas, a functioning financial system, and active investment promotion.

Improved Productivity - Technological and capital improvements necessary for improving productivity have not kept pace in Nicaragua due to heavy state intervention in the economy and a bias against the private sector. Productivity can be spurred through increased economic competition, especially through privatizing public sector entities; improved access to technology, production inputs, and credit; and improved basic infrastructure.

Diversification and Export Sales - Sustainable growth will require revitalization of traditional agricultural export commodities and expansion to new productive opportunities in both agriculture and industry which can lend greater stability to the economy and stimulate growth.

Expanded Participation - If economic growth is to address conditions of poverty in Nicaragua and support the development of democracy, it must encompass greater numbers of Nicaraguan men and women through creation of jobs, expanded ownership, and improved access to credit, training, and employment opportunities.

Sustainable Resource Use - The natural resource base has not been managed in a sustainable fashion due to political turmoil, lack of budgetary resources, and inappropriate policies. Deforestation is taking place at extremely high levels, water quality suffers from both agricultural and industrial pollution, and important ecological areas are threatened.

Political Needs - Consolidation of a democratic system of government will accommodate change through peaceful means, allow citizens to participate in the decisions that affect their lives, and protect basic rights and freedoms associated with economic progress. Nicaragua lacks consensus regarding democratic values critical to widespread acceptance of decision-making processes, representative institutions, access to information, government accountability, and basic civil and property rights. Such a consensus will be an important foundation for:

Improved Representation - Nicaragua must develop and strengthen the institutions and processes that translate the will of the people into policies and programs that meet their needs. These include the electoral process, legislature, interest groups, parties, and press.

Justice - Politicization of the judiciary, army, police, and regulatory bodies has corrupted justice in Nicaragua and led to human rights violations. These institutions must be depoliticized and re-oriented toward protection of human rights and just application of the law.

Government Effectiveness - The Nicaraguan government has limited capability to undertake even minimal government functions and will need to scale back the scope of government and decentralize in order to concentrate its expertise and resources. To demonstrate the efficacy of democratic government it must improve efficiency, institute financial controls and accounting systems, and establish an apolitical civil service with appropriate incentives.

Social Needs - Key social areas are strongly linked to growth and democracy goals but also represent significant direct impact on economic and social well-being.

Education - The most critical need in Nicaragua is for improved basic education. Literacy rates have fallen off dramatically in recent years and primary school efficiency is very low. Vocational training will be important when employment levels improve; universities are highly politicized and unable to offer a quality education.

Population Growth - Nicaragua's population growth rate of 3.4% is the highest in the hemisphere; contraceptive prevalence is far below the Latin American average. Population growth dilutes the impact of economic growth and puts heavy pressure on natural resources.

Health - Diarrheal disease and respiratory illness/pneumonia, the leading causes of death and illness, are largely the result of poor water or lack of environmental sanitation. The health system, while oriented toward primary care, lacks resources and supplies.

STRATEGY: The USAID/Nicaragua Strategy to address these needs is encompassed in a series of strategic objectives which orient project and program initiatives:

Increased foreign and domestic investment - USAID/Nicaragua will address this overriding priority through balance of payments assistance with associated conditionality to support stabilization efforts and provide a policy framework to attract investment. The Mission will also support financial system reform and establishment of private financial institutions. Institutions promoting investment and exports and serving as a policy voice for the private sector will receive assistance.

Increased competitiveness in the economy - Policy dialogue associated with cash transfers and food assistance will address elimination of barriers to competition and preferential treatment of public sector entities and promote private sector involvement in areas previously under monopoly or state control; privatization efforts will be supported. Local currency generations will be used to provide medium-term credit. Technology transfer activities will help renew Nicaragua's technological base and will improve competitiveness of non-traditional export products. Assistance in establishing producer/market linkages and gaining market access will be provided and policy dialogue will address legal constraints to a broader array of business enterprise. Later in the CDSS period, USAID may consider activities which would facilitate infrastructure improvements through significant private sector involvement. Participant training focused on the private sector will help improve management and technical skills in key areas.

Increased participation in the economy - Short-term employment generation activities will continue over the early part of the CDSS period. Policy dialogue and privatization assistance will focus on eliminating barriers to participation, and the need for broad ownership, maximizing employment, and broad access to credit based on performance; micro-enterprise programs and assistance to credit unions will complement this focus.

Improved productive/extractive practices - To promote sustainable resource use USAID/Nicaragua will address critical natural resource/environmental policy questions through policy dialogue and will strengthen the capacity of the primary Nicaraguan natural resource management/environmental protection agency. Activities to address deforestation, agricultural practices, and watershed management problems will be undertaken; support for management of selected protected areas will be provided.

Greater consensus on democratic values - USAID/Nicaragua will support civic education efforts undertaken by organizations, interest groups, and schools to promote critical value orientations supportive of democracy. Activities to improve objectivity and outreach of the media will be supported as will human rights organizations and key democratic organizations. Activities that promote the effectiveness of democratic government will include assistance in reducing the size and scope of government through programs such as employment conversion, and decentralization of appropriate functions. Government institutions that carry out important representation, judicial, electoral, and accountability functions in a democratic society will be supported. The participant training program, which includes a CLASP component, will complement these activities.

Improved quality and efficiency of basic education - Curriculum development, in-service teacher training, and improvement of administrative efficiency in the Ministry of Education will be financed to address the most serious needs in primary education.

Improved maternal and child health - Preventive primary health care interventions will be financed in priority geographic regions including maternal/child health activities at the regional/municipal level. Health financing reform to improve budgetary allocations to preventive measures may be addressed through non-project assistance which might help create a fund for the purchase of medicines and medical supplies. USAID will also promote increased contraceptive prevalence through support for expansion of family planning services provided by private family planning organizations including the provision of low-cost contraceptives.

These objectives receive special elaboration for the Atlantic Coast region which has been especially affected by war and natural disaster and for the needs of ex-Resistance members currently being re-integrated into Nicaragua society.

A participant training program targets both the private sector and selected public sector entities in support of all strategic objectives; a CLASP component helps support democratic initiatives.

Direct financing of major infrastructure and housing construction are clearly outside the strategy as are support for education beyond the basic level, centralized Ministry of Health programs, and rehabilitation.

RESOURCES: The strategy articulated for Nicaragua over the next five years requires a yearly program budget of at least \$200 million largely composed of Economic Support Funds (ESF) supplemented by Development Assistance (DA) and food assistance. Balance of payments support is expected to stay in the range of \$125 million annually with overall support for economic objectives accounting for approximately 75% of the program budget. Democratization and social programs represent a more or less equal split of remaining resources. After two years of intensive design activity the mission expects to concentrate on implementation at the mid-point of the CDSS period. As the second generation of design gets underway, the mission will be looking increasingly toward non-project modes of assistance.

CONCLUSION: Implementation of this strategy, combined with assistance from other donors should contribute to a major transformation of Nicaraguan society. By 1996, Nicaragua should be well on the road to economic recovery building on progress in moderating inflation and re-establishing a financial system. The private sector will regain its leadership role, traditional exports will rebound, non-traditional exports will be established, enclave manufacturing in a variety of areas will be established, and the economy will achieve significant growth in per capita GDP. The United States will be Nicaragua's principal trading partner. By the time elections are held in 1996, the central values of democratic society will have been transmitted throughout the country contributing to acceptance of democratic government and respect for human rights. Finally, essential social services will be transformed. The primary education system will be strengthened and depoliticized and the basic health system will be revitalized and put on a more sustainable footing. Activities undertaken under this strategy lay the foundation for a free, prosperous and democratic Nicaragua which can realize its full potential over the next decade.

II. ANALYSIS OF NICARAGUAN DEVELOPMENT NEEDS

The development needs of Nicaragua over the period 1991-1996 are enormous. During the 10 year period of Sandinista rule prior to the elections of 1990, economic mismanagement, war, an economic embargo, and political polarization seriously eroded the basic institutions, infrastructure, values, and policy framework necessary for economic and political development. The new government which took power in April 1990 has been able to make limited progress in addressing the huge economic, political, and social needs facing the nation. Its accomplishments as of the beginning of the CDSS period, however, especially in terms of ending the war and demobilizing armed forces on both sides, are important and lay the groundwork for future progress. But the development needs of Nicaragua are so broad and deep, and so complex and interconnected, that they will tax the abilities of both government and donors to respond.

Because of the depths to which Nicaragua has fallen over the period of the 1980's, the development needs are obvious and everywhere. USAID/Nicaragua has attempted to highlight the most critical needs and outline what will be necessary to address them. The analysis starts from the premise that development in Nicaragua essentially means bringing about improved economic and social well-being for Nicaraguan citizens. If the economic and social well-being of Nicaraguans is to improve in the current context there must be:

- **Broad-based, sustainable, economic growth** - All Nicaraguans, men and women, must have greater potential for earning increased income on a sustainable basis and the country as a whole must be able to address its staggering debt and improve its position in the international market; the economy and society must be "open to talent" from all levels of society;
- **Functioning, stable democracy** - Nicaraguan citizens must agree on new rules of society based on democratic values and improve the institutions which can help make democracy work;
- **A healthy and literate population** - Nicaraguans must have access to adequate food, potable water, quality health care, basic education, and an environment conducive to physical and mental health.

These conditions do not exist in Nicaragua at the beginning of the CDSS period; the reasons they do not exist are many and varied. The following analysis attempts to explain the current situation in relation to each area, highlight the most important aspects of the past and current situation that have mitigated against development along these lines and outline what needs to take place if they are to occur in the future.

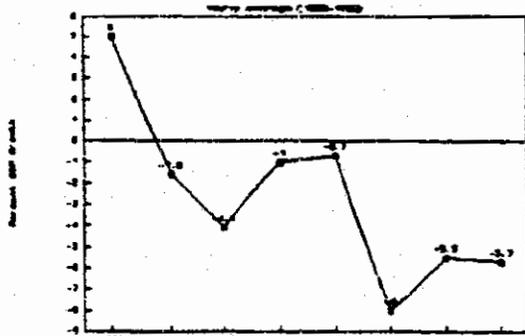
USAID/Nicaragua has also identified two areas which, for a variety of reasons, require specific attention early in the CDSS period. The Atlantic Coast area is an autonomous region in Nicaragua and because it was particularly affected by the war and natural disaster, its specific needs must be considered. In addition, resettlement and repatriation of refugees and members of the ex-resistance have presented special political and economic problems.

A. ECONOMIC NEEDS: SUSTAINABLE GROWTH AND EXPANDED PARTICIPATION

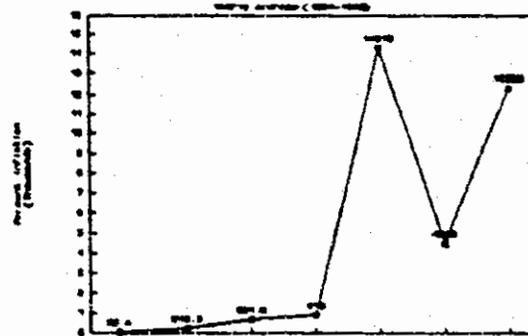
The Chamorro Administration inherited a Nicaraguan economy in shambles following ten years of economic mismanagement and the accumulated effects of war and the U.S. economic embargo. The Nicaraguan GDP declined by 37.8% from 1977 to 1989 and the standard of living for the average Nicaraguan declined by 58.2%. Monetization of central government deficits led to hyper-inflation (reaching a high of 33,000% during 1988); inflationary damage was compounded by efforts to fix exchange rates and control interest rates. Exports deteriorated steadily throughout the 1980's. Nationalization of banks, control of credit, preference to state-owned enterprise, negative interest rates, and arbitrary government forgiveness of outstanding loans devastated commercial banks. State-owned enterprises came to dominate key areas of the economy and were often grossly mismanaged. External debt levels totaled almost \$10 billion; arrears alone totaled \$3.1 billion for an economy with an estimated GDP of slightly over \$1 billion for 1991. High arrears to the IDB and IBRD had closed those sources of development financing.

In its first year the new government concentrated on resolving the political divisions confronting the nation and made little progress in bringing about economic stabilization or growth. The ideological polarization of the country has been clearly demonstrated in matters of economic policy and stabilization. The Sandinista opposition has vociferously opposed, and occasionally sabotaged, measures which would negatively affect its chief constituents, especially in matters of employment. The new government was able to forge a tentative consensus on some key aspects of economic reform through a process of dialogue known as "concertación". While this created space to enact some economic liberalization measures, the overall effect was to delay the stabilization process. Brought to a recognition that stabilization was essential to halt the downward slide of economic activity and that further delay would only compound the problem and reduce the external resource availability to support it, the Nicaraguan government announced a strong stabilization plan in March 1991. As of the drafting of the CDSS, this plan had experienced considerable short-term success in stabilizing prices but its long-term viability remains uncertain.

Real GDP Growth in Nicaragua



Inflation in Nicaragua



The short-term need has been stabilization: hyper-inflation persisted for a world-record 36 months in Nicaragua and high levels of inflation continue to erode the buying power of citizens and sap the confidence of investors. Inflation in 1990 was over 12,000% and declined only marginally as of the beginning of 1991. While important measures to address inflation and real exchange rate instability have been taken with early success in bringing inflation down (monthly inflation improved to approximately 5% in April 1991 according to unofficial indices), it is likely that stabilization will remain a continuing economic need during the next few years.

The longer term need is for growth. In 1990, Nicaraguan GDP fell by 5.7% continuing a seven year negative slide. With estimated per capita income below \$300, Nicaragua is now grouped with Haiti and Guyana as one of the poorest nations in the hemisphere. Family income for the majority of Nicaraguans is insufficient to meet family needs for food, clothing, and shelter.

While rapid economic growth is the most critical need, *how* that growth occurs is equally important. To meet the needs of the Nicaraguan majority and support the development of a functioning and stable democracy such growth must be broadly based encompassing major gains in employment and expanded ownership of productive enterprise. It should provide the basis for all segments of society, including women, marginalized ethnic groups, demobilized military and resistance fighters, and disabled veterans, to find jobs, start businesses, and improve their quality of life.

Moreover, such growth must be sustainable. To recover from the economic losses of the past decade, meet the economic needs of its citizens, and catch up with its neighbors, Nicaragua must maintain high levels of growth for an extended period. The resource base which must support such growth has suffered from past mismanagement. It cannot be further squandered in a quest for short-term growth objectives, and must be renewed, where possible, to form the foundation for future growth.

To achieve broad-based sustainable growth, Nicaragua must see a revitalized private sector and improvement in investment, productivity, entrepreneurship, participation, exports, diversification, and resource use.

1. Investment

The most critical requirement for economic growth in Nicaragua is productive foreign and domestic investment. A re-invigorated private sector is essential to economic improvement in Nicaragua; rebuilding the economy will require resources far beyond those that can be provided through aid channels and the flexibility and dynamism of the private sector will be important to achieve rapid growth. The private sector, however, deteriorated markedly over the period of the 1980's due to a clear government bias toward the public sector, confiscation of property, and an unfavorable policy environment. Private investment declined dramatically over the course of the last ten years. If investment is to increase to levels sufficient to produce rapid and sustained economic growth, the investment climate must improve dramatically through improvements in the following areas:

Economic Stabilization - The first and most important step in creating conditions for increased foreign and domestic investment is to stabilize prices and the real exchange rate in the short term. This will largely require fiscal and monetary control and improved exchange rate policy. The government has taken difficult and painful measures to stabilize the economy in early 1991 but substantial balance of payments assistance from international donors over the next few years will be necessary to consolidate stabilization efforts. The primary macro-economic measures which need to be taken over the CDSS period to bring price stabilization include:

Reduction of the Budget Deficit - Budget reduction will require reducing the size of the public sector payroll which the government has begun to address through its employment conversion program and privatization. Revenues will need to increase in order to prevent further cuts in important government activities.

Monetary Targets - Elimination of domestic monetary emissions and levels of monetary expansion congruent with external financing.

Exchange Rate Policy and Exchange Management - Exchange rate policy which will keep exchange rates competitive and in line with market forces.

Resolution of Property Rights Disputes - Issues related to the return of properties confiscated by the Sandinistas and ensuring security of tenure, particularly in rural areas, have been extremely contentious in Nicaragua and the perceived insecurity of property rights continues to be a major obstacle to new investment. The Nicaraguan government is moving forward to return many business properties, although securing possession against the opposition of Sandinista unions remains a problem. The return of houses confiscated and "sold" by the lame duck Sandinista government in its last days and legalized by decree remains a highly contentious issue. Finally, the problem of securing rural properties from invasions by unions, ex-military, and ex-Resistance, remains unresolved. Though a National Review Commission on Confiscations to review claims for confiscated property has been created, the return of business properties has been proceeding slowly. Lack of a government action regarding return of confiscated homes or in countering continuing land invasions is also seen by many as evidence that the Government cannot, or will not, assure security of property in Nicaragua. The property rights situation is among the most frequently cited reasons for the lack of additional investment from Nicaraguans living outside the country. Resolution of property rights issues will be an important indicator of both government commitment to creating a favorable investment climate and its ability to implement policy in the face of political opposition.

Political Stabilization and Government Effectiveness - Stabilization efforts and economic measures to improve the investment climate are politically divisive in Nicaragua. Investors will be looking for clear indications that political turmoil will be contained and for evidence of progress toward the establishment of a free-market economy. Though the property right issue is currently the most critical to address, the government will need to demonstrate that it has developed a working legal and regulatory structure such that it can guarantee contracts, establish property rights, resolve disputes, and enforce laws which govern business and investment. It must also be able to demonstrate that law enforcement entities have the capability to maintain order in accordance with government directives and policy.

Functioning Financial System - To provide necessary services for potential investors and mobilize domestic savings, Nicaragua must establish a functioning financial system. Currently the financial system consists of the Central Bank and two state banks. The state banks have, in the past, largely supplied credit based on political criteria and offer only limited other financial services. Services such as currency exchange and letters of credit are currently only available through the Central Bank. Because of inflation, exchange rate instability, and lack of real positive interest rates, the total deposit base as of late 1990 had been reduced to only \$46 million. Creation of a Superintendency of Banks to regulate financial institutions and establishment of private profit-seeking financial institutions will be important to the provision of improved financial services and mobilization of savings.

Policy Framework for Investment - Key policy measures have been enacted which have eliminated state trading monopolies, established a framework for privatization of public sector entities, and legalized private financial institutions but there is much more that must be done to create a favorable investment framework. The Investment Law will be an important element in establishing regulations and processes related to investment, especially rules related to repatriation of capital and income, dispute resolution, etc. Other policy measures can address areas which have a more indirect impact on investment decisions but are an important part of an overall investment climate attractive to potential investors. In working to establish and maintain a favorable policy environment the ability of the private sector to organize itself; propose, analyze, and advocate policies supportive of investment; and effectively represent the broad range of private sector entities will be an important factor.

Investment Promotion and Support - Potential investors need information and contacts to develop ideas and establish the linkages necessary to create business opportunities. Nicaragua currently lacks institutions or organizations that can provide information and services to potential investors. In addition, support services such as investment risk insurance are largely unavailable in Nicaragua.

2. Productivity

The drop in investment has had adverse implications for productivity in nearly every sector given that investment is largely the means of embodying improved technologies. In addition, inappropriate policies and institutional deterioration have reduced the output of the economy below its potential. Important sectors were essentially de-capitalized and new technological improvements were deferred during the last ten years. In the agriculture sector, for example, productivity has dropped to approximately half its level of 1979. Market mechanisms which foster economic efficiency and encourage maximum productivity have been impeded by heavy state intervention and a bias against the private sector as well as distorted prices. Besides increased investment, the critical needs for improved productivity are:

Increased economic competition - Monopoly production and marketing arrangements in major commodities and industries, combined with import controls, have produced artificially high prices and removed a major stimulus for improved productivity. Liberalized markets for coffee, rice, and cotton are particularly important to improve Nicaragua's international competitiveness and spark greater overall productivity in the economy. Policy measures to

eliminate a bias toward public sector enterprise and force them to operate in a free market without subsidies are among the most critical steps in improving competition, along with reduction in levels of trade protection. Currently, estimates of public sector participation in the economy range from 40% to 55%; privatization of public sector firms will assure increased competition and send an important signal concerning the government's commitment to a free market economy.

Technology Transfer - In many sectors Nicaragua has had no technological improvement over the last ten years and is operating with a technology base of the late 1970's. In some cases inappropriate Eastern Bloc technology has been incorporated, leaving Nicaragua behind its neighbors and out of step with current needs and tastes. Government supported research and extension services have lagged; Nicaragua's technological level in most areas is far behind neighboring countries which trade in many of the same commodities. Business leaders and entrepreneurs need exposure and access to the latest in technology in all fields in order to improve productivity and increase their overall competitiveness in the world market.

Credit - If Nicaraguan entrepreneurs and business enterprises are to restore and improve their productive capacity they must have the means to obtain new technology, and incorporate new inputs and techniques. Improved access to credit, irrespective of sex, class, or political affiliation, is critical to the process of technological renewal and capitalization/recapitalization of agriculture and industry. Lack of credit has been identified as a crucial constraint by producers in various sectors and must be remedied to improve productivity. Perhaps more critical is to restore the link between credit and productive investment in capital improvement. Credit policies under the previous government, which allocated credit on a political basis and often forgave massive amounts of accumulated debt, undermined the potential of credit to stimulate productivity and bankrupted the financial system. The provision of credit based on merit and the principle of repayment based on increased production engendered by investment of credit resources must be instilled among borrowers.

While the opening of private financial institutions will be an important step in improving the credit situation in Nicaragua, new banks are likely to be conservative lenders initially and focus on short-term credit for known clients. There will be a continuing need for credit access by those with some degree of credit risk, especially in the agriculture sector. The challenge will be to find a way to provide credit to small clients through alternatives to the state banks.

Access to Production Inputs - Availability of agricultural and industrial inputs is limited and costs are much higher than in other Central American countries. This has been due, in part, to importer/wholesaler/retailer hedging due to the risks of inflation; higher financial transaction costs for imports because of the lack of commercial credit and private banks; and heavy, inefficient government intervention or monopolies in input importation. It is also due to the inability of the country to earn sufficient foreign exchange to purchase production inputs, most of which must be imported.

Infrastructure - Productivity also depends on the level and condition of basic infrastructure in the country: accessibility and dependability of electricity, transport, water and sanitation facilities, telecommunications, etc., that support productive enterprise and lay the foundation for

economic improvement. Nicaraguan infrastructure improvement has not kept pace with its neighbors and in some areas has deteriorated markedly. While primary roads were well-built originally and have stood up well to years of minimal maintenance, there is a need for improvement in secondary roads and transport to large areas of the country, and for greater and more efficient production and use of electrical power, better quality telecommunications which incorporate new computer technologies and communication advances, and improved means of handling the commodities involved in international trade. Infrastructure improvement in these areas will form an important basis for increased productivity.

Human Capital - Nicaragua lost large numbers of its best trained and most entrepreneurial citizens during the tenure of the previous government due to a policy environment unfavorable to private enterprise, repression, war, and economic deterioration. As a result, entrepreneurial, technical, and management skill is largely lacking in society - though it may be accessible through ties to the Nicaraguan community in Miami and other U.S. cities. Of equal concern is the general level of education for the bulk of the workforce. As outlined below [see Section II.C.1], levels of education are extremely low in Nicaragua and the educational system must be vastly improved to affect the level of human capital such that it can form the basis for improved productivity.

The greatest potential for productivity increases during the first portion of the CDSS period is in the agricultural and agribusiness sector. Agriculture still serves as the foundation of the Nicaraguan economy and is the primary source of exports to meet foreign exchange needs. While agriculture has been heavily de-capitalized, new capacity can be put in place relatively quickly for many commodities given access to critical inputs, a favorable policy framework, and renewed access to markets in the U.S. The agriculture sector also may be able to respond quickly to markets for non-traditional exports.

3. Diversification and Export Sales

Sustainable economic growth will not depend only on revitalization of the traditional bases of the Nicaraguan economy - agricultural export commodities such as coffee, cotton, bananas, sugar, and beef. While these will remain important foundations of the Nicaraguan economy and will be critical to growth, they are also vulnerable to changes in world prices and cycles of boom and bust. To the extent that Nicaragua is able to diversify its structure of production, it can stabilize its economy and lay a stronger basis for sustainable growth over the long term.

Nicaragua must improve its export performance to earn the foreign exchange necessary to meet import needs. Improved performance in traditional export crops will undoubtedly play the key role in increasing export earnings but non-traditional agricultural exports and increased levels of manufactured goods can provide an important complement to expand markets and sales.

The key element in promoting diversification will be to improve producer-market linkages. The events of the last decade have disrupted producers' access to their traditional markets. The U.S. market was closed to Nicaraguan exports during a period in which neighboring countries were able to develop significant levels of non-traditional exports through producer-market

linkages encouraged under the Caribbean Basin Initiative. All Nicaraguan exports passed through Sandinista-controlled trade monopolies at artificial prices and Sandinista policies distorted the prices and trade patterns of domestically-consumed commodities as well. As part of its efforts to permit the market determination of prices and free trade, the new government has licensed private operators in foreign trade activities. However, inadequate producer-market linkages continue to constrain economic growth and limit diversification.

Diversification also offers expanded opportunities for new entrepreneurs and, in many cases, for small producers and businesses. Currently, the best opportunities for non-traditional exports and domestic market potential include fruits and vegetables for winter U.S. markets (melons, limes, mangos, etc.) and maquiladoras producing a variety of products associated with light industry. Textile production may have some attraction for investors due to the absence of quotas for the U.S. market. Reactivation of free trade zones will help stimulate light industry and manufacturing.

4. Participation

Increased participation in the economy is critical if growth is to serve as the means for alleviating poverty in Nicaragua. The critical need is for jobs which will allow the poor majority in Nicaragua to earn sufficient income to meet the needs of their families and improve their standard of living.

Moreover, the degree of participation in economic growth has important political implications for Nicaragua. Broad-based growth improves the conditions for democracy and helps create greater support for free market economic policies. To the extent that growth is restricted to a few, whether a particular social class, sex, or political party, opposition to private sector development and free market enterprise is strengthened.

For most of Nicaragua's past, meaningful participation in the economy has tended to be restricted. During most of this century, the economy functioned to provide vast wealth to a few families while leaving the majority in relative poverty - conditions which fueled the revolution of 1979. Under the Sandinistas, economic opportunities for advancement were generally under the control of the state with special access on the basis of political affiliation. If economic growth is to have an impact in reducing poverty in Nicaragua and serve to support a democratic system of government it must create greatly expanded opportunities for men and women to participate in the economy on the basis of merit - skills, experience, determination, training, well-researched proposals, etc. The primary means of expanding participation in the economy will be:

Increased Employment Opportunities - The overwhelming need in Nicaragua is for productive jobs for both men and women; the manner in which the vast majority of Nicaraguans will participate in the economy and experience the results of economic growth will be through wage labor employment. Current estimates of unemployment/underemployment range from 25% to 50%; the challenge is to structure growth to maximize employment potential.

Broader Ownership of Productive Enterprise - One of the opportunities presented by the Sandinista revolution is the break-up of oligarchical control of the economy. To the extent government policies and actions can eliminate the present concentration of production in state enterprise, prevent concentration of private sector ownership, and promote broad-based ownership of productive enterprise, both economic and political goals are served. Ultimately, Nicaragua's political stability and progress in democratization will rest on the development of a middle class and will be largely determined by the structure of ownership established during the CDSS period. Competitiveness in the economy is also enhanced by broad ownership; early indications of the pattern of new investment in Nicaragua raise concerns about the concentration of economic power. The manner in which privatization of public sector entities is undertaken and the degree of support and encouragement for new investors in the Nicaraguan economy and for small and micro entrepreneurs, will be important to achievement of broader ownership.

Improved Access to Credit, Employment, Training Opportunities - Expanded participation will require that those with determination and ability have opportunities to contribute their talents in productive ways. New and broader opportunities must be created and access to them must be established on the basis of merit with special efforts to include disadvantaged groups, women, and disabled persons. While existing programs must, in many cases, be re-oriented to improve access, support for institutions with a generally participatory orientation can contribute to improved opportunities for credit, training, etc. Credit unions, for example, offer an alternative to both private and state banks in supplying credit that is more likely to address the needs of small producers and entrepreneurs. Above all, social and economic activity at all levels must be "open to talent" if the country is to achieve its full potential.

Broader Participation in Economic Policy Formulation and Decision-Making - An important element of increasing participation in the economy will be broad representation of private sector economic interests in policy discussions. Improved representative functions through the political system will be important (see Section II.B.1) and will be complemented by improved outreach and representation of the broad range of private sector interests through private sector associations.

5. Resource Use and Environment

The natural resource base which serves as the basis for the Nicaraguan economy has suffered from years of political upheaval and economic deterioration in Nicaragua. The previous regime promoted mining of soil and water resources and significantly depleted the human and technical capacity required for proper natural resource stewardship. Relocation programs, nationalization of forests and fisheries, and land redistribution further eroded incentive systems supporting sustainable land-use practices. High levels of population growth will continue to put heavy pressure on Nicaraguan resources in almost every major problem area:

Deforestation - The vast majority of homes even in urban areas still use firewood for cooking which contributes to deforestation already taking place at high rates due to lumber operations. Between 1960 and 1980 Nicaragua experienced the highest rate of deforestation in Central America: forest cover was reduced by nearly two million hectares (one third of the total forest

area) to either marginally productive pasture or wasteland. Trend analysis indicates that at present deforestation rates Nicaragua will be completely denuded before 2020. Current forest management efforts are limited and lack resources.

Agriculture-Related Resource Loss - Current farming practices, hillside agriculture, and agriculture expansion to marginal areas have contributed to high rates of soil erosion. Chemical and fertilizer run-off, aggravated by heavy subsidies on agricultural chemicals which have encouraged their use, has had a serious negative impact on water quality. Encroachment on forest lands with marginal agriculture potential has contributed to deforestation.

Water Quality - Among the more significant environmental problems in Nicaragua is the worsening condition of major watersheds surrounding Lakes Managua and Nicaragua and others emptying directly into marine areas along the Pacific coast. Siltation, born through soil erosion and introduction of agrochemicals and industrial contaminants, has led to the biological death of Lake Managua. Similar trends are underway in the much larger Lake Nicaragua. Siltation is increasingly identified as the most significant threat to Nicaragua's hydroelectric infrastructure, which accounts for an estimated 50 percent of generating capacity.

Protection of Bio-diversity and Ecologically Fragile Areas - The Sandinista government promoted some activities that incidentally spared wildlife populations (restrictions on arms use) and reduced pressure on some protected areas and forests (resettlement schemes). In addition, net migration due to the political turmoil of the late 1970's and 1980's relieved much of the pressure on the environment and actually reversed the habitation patterns of the Atlantic region that had predominated since the 1950's. However, the quarter million refugees who migrated to Costa Rica and Honduras are now returning and resettlement programs are stretched beyond capacity. Existing programs are under great pressure to stabilize these populations and are increasingly turning to forested areas, incapable of supporting traditional agriculture for more than a few years, for repatriation purposes. Although the forest lands of the Atlantic Coast region remain somewhat intact (due to the social and economic turmoil of the 1980's), increasing pressure and disintegrated regulatory capacity pose immediate threats to forests and attendant biological diversity. The lack of a policy framework or an operational institution to assist in rational land-use allocation is a paramount problem which needs urgent attention.

Past neglect of the environment has also led to the loss of personnel and capacity to monitor the environment's deteriorating health. The Nicaraguan Institute for Natural Resources and Environment (IRENA), the primary agency for scientific investigation, policy formulation and regulatory oversight, was essentially dismantled. The flow of accurate information on water, soils, forest, wildlife, and parks ceased in early 1982. Present estimates of the environment's "pulse" are subjective and understate the magnitude of the problems faced. Likewise, management of the policy, legal, and regulatory framework critical for successful natural resource management was never undertaken which resulted in economic policies, economic incentives, environmental protection measures, regulation, enforcement, and land use going at cross purposes. The new government, however, has expressed a commitment to improved management of natural resources and has begun to build the institutional basis necessary to do so.

B. POLITICAL NEEDS: TRANSITION TO DEMOCRACY

Democracy, as a system of government in which ultimate power resides in the people, provides mechanisms and processes for individuals to participate in the economic and political decisions which affect their lives. The ability of individuals to participate in decision-making and the freedoms inherent in a democratic system are significant elements of economic and social well-being. For these reasons, movement toward democracy is an integral part of the process of overall development in Nicaragua.

A number of scholars have also asserted a relationship between economic development and democracy and suggest that political freedom is an important complement to the operation of a free market economy. In the Nicaraguan context, democratic transition and improved functioning of key institutions will clearly play a role in improving investor confidence and providing the foundation for economic stabilization and growth. At the same time, broad-based growth will ameliorate the sources of discontent which tend to undermine democratic institutions.

1. Representation

The cornerstone of democracy is the principle that ultimate political power resides in the people. It is the ability of citizens to play a role in decision making that makes democracy desirable, and, despite its inefficiencies, the most sustainable and effective system of government. If democratic systems are to work, the will of the people must be conveyed accurately by their representatives and reflected in decision making. Democratic systems incorporate various processes, mechanisms, and institutions to assure proper representation. In Nicaragua, these processes, mechanisms, and institutions are weak and extremely fragile. The elections of 1990, in serving as a process to determine fairly and accurately, the will of the Nicaraguan people, represent a significant departure from tradition and present an important starting point for the consolidation of democratic forms of decision making.

Consolidation of democracy in Nicaragua will require the establishment and strengthening of:

Consensus on Democratic Values - Though democratic rhetoric has been used to justify recent forms of authoritarian rule and democratic forms and structures such as the legislature, courts, political parties, etc. have been established, Nicaragua's cultural legacy is primarily authoritarian and centralist - dating from the days of Spanish colonialism and oligarchic rule. Nicaragua's past, including the recent periods of Somoza and Sandinista rule, has not served to develop the values and attitudes which nurture and support democratic systems of government. Moreover, the previous Sandinista government used sophisticated methods of indoctrination and propaganda to inculcate its Marxist orientation throughout society. Though the election in February, 1990 clearly demonstrated a desire for change in the direction of democratic rule, personal freedom, and economic liberalization, the political disruption of strikes and street demonstrations, splits in the UNO coalition, and ideological polarization of political and economic discourse are indications of a lack of consensus related to democratic values and attitudes. The legitimacy of representative processes and institutions and their acceptance and

support in society depend almost entirely upon the degree to which they conform with popularly held values, attitudes, and expectations - the political culture of the nation. Given the current disarray and polarization of contemporary Nicaraguan political culture, there is a profound need to articulate and promote democratic values and reach a consensus on the rules that govern political and economic life in Nicaragua. A shared consensus on democratic values is also important to assure proper conduct by elected representatives, leaders, and government officials and effective operation of democratic institutions and processes.

The following values are especially critical to improved representation within the Nicaraguan democratic transition and need to become more firmly rooted in Nicaraguan society:

Majority Rule and Institutional Means of Resolving Conflict - Resolution of differences regarding government policy should take place through the legislative and electoral system. Groups desiring change should work to persuade a majority and operate within the democratic system rather than create civil disturbance or sabotage measures taken by those with majority support.

Accountability and Checks on Power - Concentration of power should be avoided through a system of checks and balances to assure fairness and effective representation. Public officials should act to promote the public welfare and should be removed and/or punished if they act for personal gain.

Access to Information - The press should be free from government control and should report the facts objectively, fairly, and completely. Activities of elected representatives and elected officials should be open to the public and press.

Electoral Processes - As the operational expression of majority rule, elections are the primary means by which the people express their will and act to remove representatives who are not faithfully representing their views. The elections of 1990 represent an aberration in Nicaraguan political life - past elections have been sporadic and generally non-competitive and/or rigged. Nicaragua must build on the 1990 experience to establish a tradition of competitive elections and strengthen the organizations which oversee, monitor, and implement elections to assure their accuracy and fairness. The next major election is scheduled for the 1996, the end of the CDSS period. Nicaragua must begin to lay the groundwork for these elections which will be an important milestone in the consolidation of democracy.

Formal Representative Institutions - In democratic systems of government, elections determine who will fill important decision-making positions in the government. These officials then have the responsibility to act in the interest of their constituents, according to the law, and in an ethical manner. To the extent that the Nicaraguan government institutions can demonstrate responsiveness in dealing with the problems facing the country and successfully resolve differences of opinion over policy, they will engender increased acceptance and confidence in the representative functions of democracy.

National Assembly - The legislature is the primary representative body of the Nicaraguan people and must play an important role in checking the substantial power granted the

President in the Nicaraguan constitution - it will also play a central role in any constitutional reform efforts. However, Nicaragua is bereft of legislative experience; though legislatures have been formed under the numerous constitutions since independence in 1821, all of them, including the one created by the Sandinistas, have been rubber stamps. Though the 1987 constitution gives inordinate power to the executive branch, the legislature has a very low veto override threshold and the constitutional authority to interpret the constitution which could be used to increase its institutional power. The 1990 election has produced a group of legislators who substantially reflect popular opinion, but there is little understanding of the role of legislatures within the populace, no real prior experience among the legislators themselves, no established procedures, and no experienced staff. In sum, the legislature can be considered an institution in formation. It also suffers from an acute shortage of budgetary resources which constrains its ability to acquire necessary equipment and attract and train professional staff.

Presidency and Executive Branch - Because of the Latin American tradition of strong presidential power and the level of constitutional power granted the Nicaraguan president, the actions of the Executive Branch will play a large role in shaping the course of democratic transition. Presidential leadership can shape public opinion and choices regarding policy direction, and tactics and strategy for resolving major domestic and foreign policy issues and implementation of policy will establish the context for movement toward democratization. Because it is the first democratically elected government in Nicaragua in this century, the Chamorro Administration will establish standards by which other administrations will be measured - a unique opportunity and a heavy responsibility. The Administration suffers, however, from a lack of well-trained advisors and managers at all levels, inadequate budgetary resources, a civil service that largely reflects Sandinista patronage, and Sandinista control of military and police. [See Section II.B.3 - Government Effectiveness].

Municipal Level Government Institutions - Local government has traditionally been neglected in Nicaragua, as in most Latin American countries. The municipalities are woefully under funded, the chronic meagerness of their revenue base aggravated by the depression Nicaragua has experienced in the last decade. The existing municipal law is a further obstacle to the loosening of the municipalities' fiscal bind: the central government must approve any new taxes or increased rates. With the central government itself facing a continuous fiscal crisis, the municipalities are at a clear disadvantage in the competition for scarce resources. Finally, a number of mayors have disagreed publicly with the central government's policy of accommodation with the FSLN, further prejudicing their ability to obtain help from the central government. For the foreseeable future, the principal problem of the municipalities will be financial and technical obstacles to the efficient provision of normal services, including trash collection, operation of city water and sewage systems, maintenance and operation of property registries, and tax collection. All the municipalities are weak in city planning, including zoning.

Checks and Balances - The political tradition in Nicaragua is to rule autocratically once gaining power. A principal mechanism used to prevent abuse of power in democratic societies and assure appropriate representation is a system of checks and balances among branches of

government and among key political and governmental institutions. As noted above, a potential problem area for the consolidation of democracy is the inordinate power of the presidency in relation to other branches of government. During the 1990 electoral campaign, the Chamorro campaign raised the issue of constitutional reform to address this issue; the Sandinistas, now out of power, also recognize strong presidential power as a liability. Though a strong movement for constitutional reform to address this and other issues of relative power and state responsibility has not yet emerged, such reform will be an important element assuring the long-term establishment of democracy.

Loyal Opposition - As of the drafting of the CDSS, the Sandinistas could not be considered a "loyal opposition" - meaning that they accept a democratic system and its processes and mechanisms as the means for making decisions. Over the first year of the Chamorro Administration, Sandinista strikes and civic disruption were designed to sabotage government policy and initiative. Consolidation of democracy will require that the primary political factions in the nation accept the system and resolve policy differences through representative legislative and electoral processes. To the degree that objective decision-making processes can be designed to resolve major issues and the Sandinistas see that a democratic system of government offers them future opportunity to hold power and influence decision-making, they will be more likely to take on the role of loyal rather than disloyal opposition and represent their constituencies through established channels.

Access to Information - A pluralistic society requires free flow of information, which is largely the function of the press but also involves interest groups and openness from government and political organizations. Citizens must know what is happening in society, government, and political life; how their elected representatives are representing them; and the range of policy options along with their potential implications. Though now free of censorship, the press in Nicaragua is highly politicized and generally reports news from an advocacy position. Despite a fairly broad range of media outlets, Sandinista affiliates dominate the airwaves and periodicals. To the extent that objective reporting takes place in the press and responsible and investigative journalism is practiced, representational functions are improved. There is also a need to improve the outreach of various media throughout the country and improve the basic infrastructure of both print and broadcast media.

Interest groups - An important representative function is filled by interest groups that represent various elements of society - business, labor, consumers, students, the church, etc. Women's groups and women leaders are a critical resource for the process of broader political representation as well. Such groups play an important role in articulating the interests of their members and lobbying for policies and government action that address their needs. Most of these groups have suffered financially due to overall economic downturn and many require new and dynamic leadership to confront changed circumstances and to move beyond ideological positions. To the extent that these groups can be strengthened to accurately represent their constituencies and insert themselves into the democratic process, representation of societal interests is improved.

Political parties are a distinct type of interest group with special importance for the development of democratic societies because of their role in presenting candidates for office and developing

specific and broad policy alternatives. Nicaragua's authoritarian history and persistent factionalism have undermined the development of viable political parties. The Sandinista party remains the best organized and strongest single party though it is undergoing significant internal dissension in the aftermath of the 1990 election defeat. The UNO coalition is fragmented and many of its member parties are quite weak, inexperienced in the basic functions of presenting a coherent, constructive message, and of mobilizing activists and members. The 1990 campaign, however, served as an important learning experience regarding the value of political organization, coalition-building, and competitive elections which can serve as a foundation for building improved party structures which represent their members' interests.

2. Justice

Democratic societies also rest on a foundation of basic political and economic rights and the rule of law. These form an absolute standard by which all members of society are guaranteed just treatment and equal opportunity. A working system of justice requires institutions and processes that enact just laws and effectively enforce and implement them, protect and defend basic political and economic rights, and assure equality of opportunity. Central to the operation and effectiveness of these institutions and processes, however, are the underlying values of society as reflected by those who embody these judicial institutions and oversee judicial process, and by those who monitor the workings of the system and work to assure its fairness and effectiveness.

The concept of justice in Nicaragua has been perverted by the excesses of previous governments. Family connections, association with those in power, political affiliation, or wealth have often been the means of subverting justice. To move toward the democratic ideal of a just society, whole institutions will need to be revamped and a fundamental reshaping of societal expectations and values will need to begin:

Enactment of Laws that Reflect Democratic Values - The rule of law requires a set of laws that reflects idealized societal values and establishes processes to change, modify, and improve that body of law - generally through a constitutional framework. The above analysis outlines changes, including revision of the Nicaraguan constitution, that will help assure that the system of representation works to enact just laws.

Law Enforcement - A central tenet of concepts of justice is that those who break the law should be punished. But law enforcement also encompasses aspects of civil law that are critical to the conduct of economic transactions and maintaining a framework of order in society. Law enforcement has been problematic in Nicaragua for a variety of reasons including problems generic to government in recent times - lack of budgetary resources and well-trained personnel. If law enforcement in Nicaragua is to improve, however, more serious problems must be addressed through:

Civilian Control and Depoliticization of the Military and Police - The military and police currently are dominated by Sandinista supporters. Loyalty of these institutions and its members to the current government is questionable and their actions in response to public

disturbances over the last year have raised doubts about whether they respond to the dictates of the party or the mandate of the government. These institutions must be "professionalized" so they can perform their proper functions in society as guarantors of security and justice. The role of the armed forces should be focused primarily on confronting external threats to security.

Improved Functioning of Regulatory Agencies - Many elements of law which help to establish a just society are not in the province of police or military but depend upon the proper operation of regulatory agencies. Agencies such as the Comptroller General and the environmental regulatory agency, IRENA, have been negatively affected by ideological preference and patronage and lack of budgetary and personnel resources. The newly created Superintendency of Banks will also play a critical regulatory role. [See Section II.B.C - Government Effectiveness]

Improved Operation of Civil Law - Aspects of civil law such as enforcement of contracts and property rights are critical to creating a framework for a healthy economy and political system.

Judicial System - The system of justice created by the Nicaraguan constitution is workable in theory but in practice has created a caricature of justice. Judges have been motivated by ideology rather than by the explicit terms of the law; corruption has come to be an accepted part of the judicial process. Institutions both within and outside the formal system must be strengthened to assure its proper operation. The Bar Associations, for example, are weak, disorganized, and unable to play the professional review and regulatory role found in other countries. Some organization must be formed to strengthen the legal profession through licensing and self-regulation and to serve as a mechanism for upgrading the standards of lawyers in an advocacy system and as a training ground for judges. There is a need for critical review of judicial appointments as part of a process of improved selection and performance of judges in addition to the establishment of judicial mechanisms which assure impartiality, just rulings, and objective interpretation of the law.

Protection of Human Rights - Protection of human rights and widespread respect for such rights are the foundation of democracy. Civil and property rights assure equal treatment under the law and protection of minorities and form the basis for equal opportunity in society. While the principal responsibility for protection of human rights rests with the government, private groups play a crucial role in assuring that government seriously undertakes its responsibilities and help move the weight of public opinion toward respect and support for human rights. The human rights situation in Nicaragua has improved since the Chamorro government took power in April 1990. Freedom of expression, arbitrarily restricted under the Sandinista regime, is exercised openly and vigorously across the political spectrum. Criticism of the government is prominent in newspapers, television, and radio, which operate without government censorship. Freedom of association is exercised by diverse political groups without the systematic repression that was evident under the Sandinistas. The right of organization and collective bargaining by workers is respected; independent unions, as well as the powerful workers' front which answers to the opposition Sandinistas, operate unrestrained.

However, human rights violations have persisted. Local independent monitors report politically motivated abuses by the National Police and the Sandinista People's Army, particularly in rural regions. Cases of arbitrary detention, police complicity in mob violence, attacks against demobilized members of the Nicaraguan Resistance, and threats against human rights activists have been documented. Nicaragua's judicial system – politicized and dysfunctional – has failed to respond to a series of violations of human rights or to uphold basic tenets of justice.

Two independent Nicaraguan human rights groups, the *Comisión Permanente de Derechos Humanos* (CPDH) and *Asociación Nicaragüense Pro Derechos Humanos* (ANPDH) are playing critical roles in investigating and publicizing violations of human rights. By drawing public attention and gathering evidence in such cases, these groups have pressed the government to respond to allegations. The Catholic Church has been an important voice in Nicaragua calling for respect for human rights and pressuring for an end to human rights abuses. For over a year, the *Comisión Internacional de Apoyo y Verificación* (CIAV) also has played a vital protection role for demobilized Resistance members, who have often been the target of recent abuses. When CIAV completes its work it will leave a void in this protection function. The press also plays an important role in providing information on human rights violations and keeping such issues in the public spotlight.

Agreement/Consensus on Basic Rights and Privileges - Justice will be improved in Nicaragua to the extent key values are internalized among the population at large and those who play a direct role in the operation of the justice system. These values include:

Equal Opportunity and Merit - Everyone should have equal access to jobs, credit, educational opportunities, etc. on the basis of merit - skills, training, experience, performance, well-formulated ideas and plans, and hard work. Opportunities should be open to all regardless of political affiliation, family connection, or gender.

Protection and Respect for Political and Economic Rights - Nicaraguan citizens should have basic political and economic rights protected and respected: the right to own and use private property for personal gain, freedom of speech and religion, judicial rights, etc. All should be treated equally under the law.

Respect for Private Property; Free and Competitive Enterprise - The right to own and use private property for personal gain is a critical element of a free market society and provides the basic incentives necessary for economic growth. Markets operate effectively only under conditions of free and competitive enterprise; regulation and intervention should be minimized.

3. Effectiveness

A cross-cutting need in all areas of Nicaraguan development that may be most closely identified with the process of democratization is government effectiveness. If democracy is to flourish in Nicaragua, and if democratic institutions are to gain strength and legitimacy, democratically elected governments will have to show themselves to be responsive to the needs of the people and effective in meeting their needs and desires. Government effectiveness is equally important in addressing the key economic questions facing Nicaraguan society. The ability of key ministries and agencies to enact and enforce effective economic policy measures and create a climate for private sector expansion is critical to economic growth objectives. Government effectiveness is also a crucial factor in determining the degree to which social goals such as preventive health and education are met.

Because of Nicaragua's limited experience with democracy, citizens will largely derive their opinions and attitudes from perceptions of the efficacy of democratic rule over the next two to three years. Thus, the degree to which democratic principles are applied within all government institutions will be a major determinant of democratization in Nicaragua.

Nicaraguan government ministries and agencies lack the basic requirements of skilled, trained, and experienced staff, adequate equipment, effective management systems and procedures, and sufficient budgetary resources, to be effective in carrying out their mission and functions. These constraints limit the effectiveness and efficiency of government in developing appropriate and workable policies and implementing them, delivering services, and providing regulatory functions to assure access and competition and protect resources and minority groups.

Over the course of the CDSS period, the Nicaraguan government has critical needs to develop effective management and financial systems and attract, train, and keep competent managers and technicians. Improved government effectiveness requires:

Scaling Back the Scope of Government - Under the previous government, the public sector was increased dramatically to encompass production, distribution, and market functions in large sectors of the economy. Mismanagement and lack of competition have meant that most of these endeavors represent a major drain on public sector resources. The capacity of the Nicaraguan public sector is so limited that it must carve out only the essential government functions of regulation and provision of essential social services and allow the private sector to undertake as many societal functions as feasible.

Increased Efficiency - The most serious problem is one of overall budget levels. Overall economic decline and the economic stabilization requirements of budget cuts has meant that operational budgets are squeezed beyond the limits for effective programs and services. Since new and expanded sources of revenue are unlikely in the near term, government entities will have to find ways to improve their efficiency to get more out of the limited budget resources available. Over the longer term, economic growth should provide a larger revenue base.

Institution of Improved Accounting Systems and Financial Controls - Initial USAID experience with a number of counterpart agencies indicates that there is a serious need for

accounting and management systems and improved financial controls. Allegations of corruption at various levels have surfaced regularly over the past few decades. To improve the allocation and tracking of resources and remove the potential for abuse which would taint the democratic transition, government agencies across the board must improve their accounting and contracting systems. The Office of the Comptroller General will also play an important role in overseeing improved accountability functions.

Apolitical Civil Service - The civil service in Nicaragua was used heavily for patronage purposes by the previous government and recent strikes have demonstrated that for high numbers of employees loyalty to party remains paramount. The civil service must come to represent an apolitical body which implements policy in accordance with the direction of government leadership.

Adequate Incentive Systems - The institution of socialism under the previous government removed many important incentive mechanisms for government workers. Incentives need to be made a part of the system in order to attract new talent and keep and improve the skills of those currently performing well.

Decentralization of Appropriate Government Functions - In addition to reducing the scope of government functions, it will be important to reduce the state centralization inherited from previous governments. Many governing functions can be handled most efficiently and effectively at local levels if both authority and revenue collection/retention is delegated to those levels.

Value Orientation Supportive of Democratic Government - Values and attitudes both within the civil service and in society at large are important determinants of government effectiveness in that they frame the standards for service and behavior by government officials and establish the parameters for government functions. Such values include:

Professional Standards and Expectations of a Service Orientation - Government should operate of, for, and by the people; government employees have an obligation to serve the societal good in a professional manner and behave ethically in their positions.

Limited Scope of Government - Free markets should be the primary means of allocating resources and form the basis of the economy; government should play an important regulatory role and address limited social needs such as education and public health. Private enterprise is the most efficient means of mobilizing the factors of production to bring economic growth and provide meaningful employment.

C. SOCIAL NEEDS: IMPROVING HEALTH AND LITERACY AND MEETING NEEDS FOR GROWTH AND DEMOCRACY

1. Education

Education plays a critical role in both economic growth and democratization and contributes directly to personal well-being and potential. It is improved education at various levels that will create the human capital needed to increase productivity and fuel economic growth. An educated citizenry forms the basis of a functioning democracy - it may be an essential element of an operating democratic system of government.

The previous government placed a great deal of emphasis on improved education and literacy campaigns. While these met with some early success, budgetary difficulties brought on by general economic decay, loss of enthusiasm by volunteers, and the dislocation and distraction of war served to decimate education efforts. Currently, though solid statistics are almost impossible to find, the literacy rate is estimated in the range of 60%. The education needs of Nicaragua are vast at all levels:

Basic Education - Basic education is of primary importance in building an educated populace as it represents the foundation for future learning and, for the majority of the population, is the only formal schooling they receive. Despite an initial heavy emphasis on basic education in the previous government's budgets, basic education in Nicaragua today is in serious need of improvement:

Efficiency and Access - Nicaraguan primary schools are producing students with literacy and numeracy skills at an extremely low rate. Only 22% of those entering first grade complete a sixth grade education and 16 student years of effort are needed to produce one sixth grade graduate - levels far below the average in Central America. Though enrollment levels appear to be high for both males and females and urban and rural dwellers, an influx of immigration and rapid population growth are putting heavy pressure on educational infrastructure. Available data indicates no bias against girls in either access or efficiency of the primary education system; enrollment ratios and health statistics show female enrollment to be higher than that of males and female nutritional status is better. Nicaraguan primary schools have repetition rates as high as 50% and high numbers of overage children. Current student teacher ratios are 34:1.

Educational Infrastructure - School buildings and equipment are in extremely poor condition with an estimated 30% of classrooms needing rehabilitation. An estimated 50% of students are without desks, and many schools lack blackboards, or other teaching aids; in some cases classes are held in homes because of the lack of a suitable building. Projected increases in primary school students from 648,277 to over 855,000 by the year 2000 will necessitate more than 6,000 additional classrooms over the next 10 years.

Educational Financing - Expenditure levels for basic education, after reaching a peak in the mid-1980's, had declined below the level of 1970 by 1989 meaning a reduction in teacher's salaries and in all the other expenditures necessary to operate schools and classrooms:

equipment, buildings and maintenance, textbooks, etc. The Ministry of Education's proposed budget for 1991 was cut by 44% due to overall budget measures necessary for economic stabilization and there appears to be little potential for increasing budgetary resources. One of the most serious implications of restricted budgets has been extremely low salaries for teachers. Current salary levels are unlikely to attract and keep teachers once economic improvement creates other employment opportunities.

Educational Administration - Confused and contradictory legal foundations impede reform, regulation, and clear lines of authority for the Nicaraguan Ministry of Education. The Ministry's structure impedes appropriate integration and coordination of activities across functional units and key processes; organizational operations and management tools are out of date and ill-defined. Middle managers lack training, education, and experience to effectively direct structural and operational reform. The Ministry has deconcentrated authority in the areas of staffing, discretionary spending, and materials distribution which can be a basis for decentralization. However, local political organization is not conducive to decentralization at this time.

Teacher Training - Of the 18,000 primary school teachers in Nicaragua about 7,000 are unaccredited. Regional in-service training programs accredit about 1500 new teachers per year and twelve normal (secondary) schools accredit approximately 400 per year. Projected increases in the primary school population mean there is a growing need for accredited teachers that is not likely to be met by the current system. Teachers are trained in traditional, non-student-based methodologies such as rote learning and memorization and their program is subject-matter based in a wide variety of subjects. They receive little training in instruction and materials.

Curriculum and Materials - AID has provided more than 7 million new textbooks to primary and secondary schools in Nicaragua which replaced the heavily politicized textbooks used previously. Most of these texts will need to be replaced beginning in 1992 as they have a short life span. In addition, these texts do not reflect active and holistic learning, cognitive strategies development, or other modern learning theory approaches. The Curriculum Planning Bureau has a number of experienced classroom teachers who have used instructional materials and have some sense of materials design but they lack training in both the systematic development of modern instructional or learning materials and in automated technology. Efforts at curriculum reform are being contemplated but at present do not include textbook development; Nicaragua has the capacity to print new textbooks in country.

Socio-Cultural Effects on Education - Educational potential is limited by the situation of poverty encountered by most families. Nutritional deficiencies affecting 30-35% of school children in marginal and poor areas of the country have educational consequences: poor cognitive abilities, decreased aerobic activities, and significant reduction in alertness. These have an immediate bearing on learning ability, school achievement, grade repetition rates, and school desertion. School feeding programs have not been available for some years. Another area of concern is the growing number (30%) of matrifocal households, given available data on socio-economic problems confronting children from such households.

Adult Education - The low school completion rate found in Nicaragua makes a focus on adult education imperative if a literate populace is to be formed in the near future. During the early years of the Sandinista regime, heavy emphasis was placed on adult education. However, during the last few years the supply of literacy and non-formal education for adult men and women has decreased dramatically, probably due to decreased numbers of persons willing to serve as teachers on a voluntary basis. Since teachers recruit students, this has also meant a fall in enrollment. An inexpensive non-formal literacy program being considered by the Bureau of Adult Education has potential but new complementary textbooks may need to be developed.

Vocational Education - The influx of demobilized soldiers and refugees has exacerbated a situation where the unemployment/underemployment rate may range beyond 40%. Many of these new unemployed have little formal education and few have any actual job experience. Vocational training can play a major role in preparing unskilled workers for entry into positions created by private sector growth.

Vocational/Technical Training Needs - At the present time, firms are able to find skilled workers from the ranks of the unemployed; current demand for vocational training is low. However, private sector employers expect their training needs to expand as the economy improves, especially in such skill areas as electrical mechanics, lathe operators, and industrial equipment and maintenance repair. The construction sector also anticipates a need for additional skilled workers in carpentry, masonry, plumbing, electrical installation and construction equipment repair once investments are made to rebuild Nicaraguan infrastructure and expand the stock of housing. Firms anticipate a greater need for training in management than vocational/technical areas, especially in export marketing, financial administration, computer systems, production systems management, and general administration; middle management needs training in personnel management and human relations. Special efforts should be made to recruit women for programs in areas where they are under-represented.

Nicaraguan firms note that the attitude and work habits of employees deteriorated under the previous government due, in part, to a government controlled economy that emphasized ideology over work performance. Employers indicate a need to improve the attitude and discipline of workers by integrating such training into their own training programs.

Vocational/Technical Training Delivery Systems - Vocational Training is provided through Ministry of Education programs and the National System for Training (SINACAP) as well as smaller programs run by PVO's and NGO's.

Ministry of Education programs suffer from inefficiencies due to excessive training costs and high drop-out rates. Training quality is also low due to inoperable equipment, inappropriate training methods, poor instructors, and inadequate training materials. Significant amounts of technical assistance and substantial reforms will need to be made if these schools are to become an effective provider of skilled workers.

SINACAP is also operating at low levels of efficiency and has many of the same problems. However, it has the potential to be a highly responsive and effective training institution because of provisions of law regarding establishment of a private sector- represented advisory board and executive director who the President could appoint from within the business sector. In addition, SINACAP has the capacity to be self-financing from a 2% payroll tax levied to fund vocational training if it were properly collected and monitored.

PVO and NGO vocational/technical education programs generally offer high quality training and employability preparation in a cost-effective manner due to more consistent financing, superior instruction and training material, well-maintained equipment, and stronger linkages with the business community. They represent an attractive alternative to Ministry schools for marginalized groups for whom other training programs might be ineffective and difficult to access.

University Training - Nicaragua offers free university education in three primary universities to those undertaking advanced study. Since the revolution, the universities have all become centers of radical activity and politics in varying degrees and they have generally had links to scholars from socialist countries and institutions. Politics aside, the constrained budgets of these institutions and the level of education for most entrants has severely eroded the quality of instruction. The universities lack appropriate facilities for advanced study - from equipment to books. Textbooks have been a severe constraint as students are often unable to find assigned books or professors must build courses around the limited texts available. In short, the universities are highly politicized and are unable to offer a quality education.

Offshore training has in the past been largely offered by the socialist bloc. Over 2300 Nicaraguans have received advanced training in the Soviet Union, Cuba, East Germany, Bulgaria, and other formerly communist countries, including 846 high school scholarships to Cuba. During 1991, an estimated 200 university scholarships will be granted by Eastern Bloc countries.

A bright spot on the educational scene for Nicaragua is the presence of the Central American Business Administration Institute (INCAE). This graduate level business school is a source of apolitical upper level management training and a focal point for business and public policy analysis and research.

2. Population Growth

Nicaragua has one of the fastest growing populations in Latin America; its rapid population growth has serious consequences for both maternal and child health, and undermines development efforts by expanding the number of poor, needy and economically dependent individuals faster than services can be expanded. This leads to either a growing erosion in social and economic well being or to a dilution in the expansion of economic and social progress throughout the population. Population growth also represents perhaps the greatest threat to Nicaraguan natural resources.

Population Rates - Nicaragua has an estimated population growth rate of 3.2% to 3.5% per year, the highest rate in the hemisphere (compared to 2.2% for Latin America as a whole and to 2.9% for Central America). The Total Fertility Rate in Nicaragua (i.e. the average number of children borne by a woman during her reproductive life) is 5.5 compared to 3.8 for Latin America and 4.8 for Central America.

Contraceptive Use - The principal proximate means of reducing fertility and population growth rates is contraceptive use. Though estimates of contraceptive use in Nicaragua range from 27% (presumably of women in fertile age) to a confirmed rate of only 9%, the rate is clearly significantly lower than the Latin American average of 40%.

Birth Spacing - Of no less importance is the relationship of birth spacing to infant mortality. Throughout the world it has been proven that babies born to women over the age of thirty-five years or under the age of eighteen years, babies born less than two years after their immediately older sibling, or babies with four or more older siblings are more likely to die during infancy. Since contraception is the only feasible strategy for regulating conception, almost every developing country with a child survival strategy has identified the provision of birth spacing/family planning services as one of its priorities.

Family Planning Programs - In most countries reproductive health needs are met by the complementary efforts of the three main sectors: the public, the private commercial (or non-subsidized), and the private non-profit (or subsidized). In marketing terms, this division of labor responds to the segmentation of demand on the basis of the client's ability to pay for services and contraceptives. During the last decade, the worsening of socio-economic conditions in Nicaragua gradually diminished the availability of family planning services and information for everyone in the country. The importation of contraceptives for the commercial sector was virtually stopped, reproductive health did not fall within the public sector's priorities, and the non-profit sector became seriously affected by the reduction of financial aid flowing into the country from the traditional international family planning donor community. In 1991, the situation not only remains critically linked to the harsh socio-economic conditions which currently prevail in Nicaragua, but it is likely to remain so for the next five years.

Public sector priorities are placed elsewhere and the deterioration that is apparent in all aspects of Ministry of Health infrastructure is also reflected in the deficient availability of family planning services. Nonetheless, the demand for contraceptives has been demonstrated by the emergence of informal market activities and distribution networks. Pharmacies are now making contraceptives available (restrictions on importation have been lifted), but both private physicians' services and the commercially distributed contraceptives are, and will likely remain, out of reach for the vast majority of the population due in large part to limitations in purchasing power and disposable income. Family planning programs will largely be the province of PVO's and NGO's with programs in Nicaragua.

3. Health Care

The health sector, probably more than any other social sector, faces problems of an enormous magnitude — problems of high visibility and immediacy because they affect people in the most fundamental way.

While the immediate and obvious problems are ones of lack of equipment, spare parts, operating expenses for maintenance of equipment, medicines, and trained health care providers, there are also major structural dysfunctions within the overall health care system that must be addressed over the near future if Nicaragua is to move beyond its current predicament. The government's assumption of monopoly status and free medical care simply makes no sense from a financial or efficiency point of view. The government also needs to improve and reinforce preventive approaches to health conditions, e.g. addressing the appalling potable water and environmental sanitation situation in both urban and rural areas which is an underlying cause of infant and child diarrhea and other endemic diseases.

Primary Causes of Morbidity and Mortality - Leading causes of death and illness among both children and adults in Nicaragua are acute diarrheal diseases and respiratory illness/pneumonia which are largely the result of environmental conditions. Only slightly more than 50% of the population has access to piped water - only 14% in rural areas. Water systems often are insufficient and may deliver poor water quality. Only 35% of the urban population is served by sewer systems and rural latrine coverage is estimated at 14%. Exacerbating these and other health problems are significant levels of malnutrition. Malnutrition among school-aged children may range as high as 20-30% and a recent study concluded that the principal factor influencing pediatric mortality was the nutritional state of the child. Breast-feeding levels are relatively low in Nicaragua. Maternal health problems are a major cause of high rates of neo-natal and perinatal deaths. Nicaragua still experiences periodic measles outbreaks and malaria and dengue are prevalent in scattered areas.

Health Care System - The deterioration of Nicaragua's national health system is evident throughout the country. The Sandinista government early on nationalized the health delivery system. Most private hospitals were brought under the control of the state. As Nicaragua's economic and financial systems fell apart in the mid and late 1980's, new investment and access to foreign exchange declined rapidly, thus severely limiting the health sector's ability to import medicines, spare parts, and equipment. Accompanying the flight of trained Nicaraguan doctors to the U.S., Canada, and other countries, the Sandinista government undertook to staff up the state-run hospitals with doctors brought in from Cuba and Eastern Europe. Over the last year Nicaragua's health system faced the following realities:

Basic health care stocks, including both basic medicines and equipment, were critically scarce, with few procurements in the pipelines.

The physical condition of the state-run hospitals and clinics had deteriorated significantly, since investment in health infrastructure and maintenance had dropped to practically zero.

Most of the Cuban and Eastern European doctors who had been working in Nicaragua departed the country.

The very tenuous health system was being subjected to new demands and conditions, as repatriation of the Nicaraguan Resistance began, including large numbers of persons with severe medical problems. An already inefficient and inadequate national health system thus was put under increasing pressure.

Nicaragua, however, has established a health care system which puts the highest priority on preventive and primary health care and addresses the principal causes of infant, child, and maternal mortality. The system has high levels of community participation, extended coverage, and administrative decentralization. Oral rehydration programs are well established and immunization campaigns have generally been well structured and have relatively high rates of coverage. Community participation has centered around the recruitment of "brigadistas" who work as health promoters in local communities. What the system lacks is sufficient budgetary resources to procure adequate supplies of medicines and equipment, maintain clinics and hospitals, and attract, train, and keep qualified staff. Nicaragua has suffered from severe shortages of medicines and medical supplies and high turnover among health personnel. Because hospitals are under Ministry of Health control, salaries for hospital workers consume a major part of the national health budget. Privatization of some aspects of the health care system and institution of cost recovery measures could have a major impact on health financing.

Environmental Health - Nicaragua has been unable to seriously address the environmental conditions - lack of potable water and sanitation systems plus nutritional deficiencies - that must be improved to address the leading causes of mortality and morbidity. Environmental sanitation is extremely lacking in both rural and urban environments; these conditions assume greater importance in considering the current threat of cholera. In addition, Lake Managua is still being used a water source despite the dangers of mercury poisoning from its heavily polluted waters.

While Nicaragua has prioritized its health care emphasis appropriately on primary and preventive care it has debilitating needs for supplies, facilities, and personnel necessary for providing both preventive and curative care at all levels and throughout the country. Financing the health system at all levels is a primary concern in the sector.

4. Housing

Housing is an extremely obvious and visible need in Nicaragua. Large numbers of people are living in shacks constructed with scavenged cardboard, wood, and roofing materials. While the growth of shanty towns in Managua and the low standards of housing in rural areas are very visible, the most critical needs related to housing are not those of shelter, per se, given Nicaragua's tropical climate. Rather, the availability of services such as water and sewage related to environmental sanitation and health are of greater importance. The key to improved

housing will be improvement in income and security of land title. Nicaragua has the capacity in its industrial and construction sectors to produce better housing once family incomes improve to the point that housing improvements and/or new construction becomes affordable.

D. AREAS FOR SPECIAL ATTENTION

1. Atlantic Coast

The Atlantic Coast region, representing about half of Nicaragua's land mass and an estimated 210,000 to 230,000 residents, is an autonomous region primarily inhabited by Indian groups in the north and a mixture of ethnic groups of African, Spanish, and Caribbean descent in the south. It was particularly affected by the war because of resistance camps across the border in Honduras and repressive government policies in the region in response. Fighting, relocations, restrictions on freedom of movement, and forced conscription all had a negative effect on economic activity and created enormous social and political problems for the region. In 1988 Hurricane Juana devastated a large portion of the southern Atlantic Coast region near Bluefields and in early 1991 over 100,000 hectares burned in large forest fires located in the north. Though the process of dialogue and demobilization has brought relative peace to the region, large numbers of demobilized resistance fighters and refugees need to be resettled and integrated into the local economy. An assessment of the current status of the region includes:

Nutrition - Independent assessments indicate that nutritional levels in the Atlantic Coast region are about the same or better than the national average. Though consumption of rice and beans is less than periods prior to the war, other food sources have remained available. Economic reactivation in the region could further improve nutritional levels.

Health Services - The Northern Atlantic Coast Region is the beneficiary of a well-coordinated \$5 million multi-year international package of integrated health development assistance by about a dozen professional agencies who work in close coordination with the Ministry of Health. The Southern Atlantic Coast Region also has a number of health programs but the Ministry of Health does not receive the type of logistics and personnel support for its rural areas which are received in the north. Nonetheless, they appear to be actively addressing health needs in the region within these limitations.

Economic Reactivation - The economy of the Atlantic Coast region remains stagnant; even modest gains achieved in the late 1980's appear to have been destroyed. Rice cultivation, which was the source of much economic activity prior to the disruption of the last decade, has not revived due to lack of seed stemming from losses sustained by heavy 1990 rains and losses to pests. Seeds for watermelon, tomato, cabbage and other vegetables are also lacking and fruit trees have been lost due to lack of attention. A region which was once largely self-sufficient in all major food items has been importing rice, beans, vegetables, and other food products from Managua at high prices accompanied by high transport costs. In the industrial sector, a number

of factories using resources from the region are closed and even most commercial lumbering activities have ceased. Only a sugar mill, a sea-food processing plant, a couple of gold mines, and some shipyards in Bluefields remain active. In short, the modest industrial economy which existed before the war is largely, although not entirely, at a standstill. Unemployment rates in the region are far above the national average.

Infrastructure - The very few roads in the region have deteriorated markedly due to lack of maintenance and require substantial repair and drainage work. Waterways which form the main transportation routes in much of the Coast are increasingly clogged with debris, especially heavy tree trunks, which have not been cleared. Electricity networks are localized around the region's major cities of Bluefields and Puerto Cabezas and have suffered from deterioration over the last ten years.

Forests and Environmental Activity - The forests which had been managed in an environmentally balanced manner are receiving no attention. Although many forests affected by Hurricane Juana in the south are naturally regenerating, the new trees are being smothered and twisted by brush, and without assistance it is said that they will take 75 years to recover. Other areas are not regenerating and require reforestation. In the north, the reforestation plan in which so much was invested in the 1970's and 1980's is not continuing because of lack of funds to thin some 80,000 to 100,000 hectares. Tree nurseries are operating at a fraction of their capacity; as a result reforestation and planting of new fruit trees has been slow to begin.

In summary, agricultural production -- particularly of the key commercial crop, rice, as well as vegetables -- is at a standstill; the industrial sector is largely stagnant; otherwise good roads and waterways are deteriorating for lack of relatively modest maintenance; and the environment is not receiving the attention which would offer some hope for the reasonable future for economic viability through proper management.

2. Former Resistance

Nicaragua faces a unique challenge in dealing with the need to repatriate and resettle thousands of ex-Nicaraguan Resistance (RN) fighters. Much has been accomplished during the period since the peace process began but the situation related to the ex-RN still requires attention.

Demobilization Process - Agreements emanating from a series of meetings of Central American Presidents dealing with the Central American Peace Process and the surprise victory of the UNO coalition in the Nicaraguan elections of February 25 provided a framework for the demobilization of the RN. The demobilization process, ratified by the Agreement of Toncontin (Honduras, April 19, 1990) entailed Resistance members turning over their arms and military uniforms and equipment to the UN Peace Force (ONUCA) and humanitarian assistance through a series of programs designed to sustain, protect, and aid the demobilized RN in the process of reentry into Nicaraguan society. The International Commission for Support and Verification (CIAV), formed by United Nations (ONU) and the Organization of American States (OEA) to

aid in the peace-making and peace-keeping process, has played a central role in this process. AID has provided over \$40 million to support the CIAV/OEA programs which include 1) monitoring the observance of the physical security and legal rights of the demobilized RN, 2) provision of a basic ration for the demobilized and their families, 3) distribution of basic tools as well as roofing material for the self-help construction of housing, 4) medical services, 5) surgical and rehabilitation attention for handicapped RN veterans, 6) coordination with CIAV/ONU for the repatriation of RN members and family outside of Nicaragua, and 7) short range development projects designed to aid in the process of converting the ex-RN into self-sufficient, productive members of a civilian population.

Current Situation - The fact that the demobilized RN population (22,500; 95,000 including family members) is dispersed and often in remote areas has complicated matters for CIAV and is in itself a symptom of the most serious breakdown in the demobilization/reintegration process.

Re-Settlement Problems - The original plan/agreement arrived at by Resistance and Nicaraguan government negotiators, concentrated resettlement of the RN in "development poles", proved to be unacceptable to resistance members and both undesirable and undeliverable from the government's standpoint. Delays in identifying a land bank of abandoned or confiscated or expropriated farms, land in the possession of fictitious cooperatives or under-utilized by them, or other lands under government control led members of the RN to identify land near their homes which met such conditions, occupy it, and seek retroactive recognition. The majority of the farms now in possession of the RN were obtained in this manner but the potential for conflict in this method is high and gets higher as the targets for take-over become fewer or are disputed. There have also been difficulties in establishing legal title for these lands.

Of the total population of 22,500 demobilized RN, perhaps 18,000 are actively seeking to be resettled on farmlands. Of these, approximately 9,000 have been beneficiaries of some 360,000 hectares distributed by the GON (both Nicaraguan Agrarian Reform Institute (INRA) and Agrarian Commission titles) to date. Of the remaining 9,000 about half have found some temporary *modus vivendi*, but the remaining 4,000-5,000 are desperately searching for the land they need for survival. The highest concentration of these are in the North, Regions I and VI. Since there are others in the field competing for available and desirable land, not the least of whom are former, now demobilized, members of the Sandinista Popular Army, the land issue becomes strongly tied to security issues.

Re-Armed Resistance Groups - Some groups of demobilized resistance, frustrated at their inability to obtain land, have re-armed and created disturbances. Their complaints revolve around perceived non-compliance of the Chamorro government with promises made at the time of demobilization. The demobilized are concerned with the threat that a still powerful Sandinista-dominated military presence represents for their safety; the right for various other reasons. Any marriage of these groups seems to be one of convenience for their long-term goals are not the same.

Needs of the Demobilized Resistance - The demobilized resistance has a number of specific needs which include the following:

Security - The greatest need and the overwhelming concern of the demobilized RN is, and has always been, security. Giving up their arms and returning to a country in which the forces opposing them are still armed, and led and manned by the same individuals, was a difficult decision. CIAV (and other human rights organizations) have played an important role in defusing this potentially explosive situation, but the fact of 47 verified homicides and over 500 documented legal and human rights violations perpetrated on the demobilized RN give credence to their concern.

Land - The critical economic need for the ex-RN is land and it is one of the few resources the GON has in abundance. Although there are competing demands from myriad sources, it would seem that resolution of the "land problem" should be feasible and of the highest priority. The potential for social disorder inherent in the failure to promptly and equitably comply with GON commitments in this regard can be countered by the potential for making major gains in social harmony by taking advantage of the fortuitous fact that the RN was a peasant army. Most of their demands revolve about, and can be satisfied by, giving them land. Implied in this priority, however, are also the ancillary benefits of credit, infrastructure, technical assistance and social services which would need to follow.

Credit - Once the land issue is resolved, access to credit assumes a significant role in the process of becoming productive. Money is needed for seed, agricultural supplies, tools, and basic supplies during the process of cultivation. The Nicaraguan Repatriation Institute (INIRE) has implemented an "Emergency Plan for the Planting of Basic Grains" which opens lines of credit backed by INIRE for recipients which would not otherwise be eligible for credit. A positive repayment record should enable the loan recipient to establish a bank credit rating; funds recaptured become part of a revolving credit fund targeted toward the RN. CIAV has also converted some of its donations of seeds, agricultural tools, and livestock to a loan basis, hoping to establish another revolving credit fund.

Infrastructure - Fairly large concentrations of resettled RN are in inaccessible areas. Penetration roads with the requisite bridges and culverts are of high priority to make these areas economically viable.

Housing - Expectations were raised that housing would be provided as part of the deal for demobilization. Beyond issuing roofing material and nails, CIAV has experimented with various degrees of support for the concept of self-help housing through its development program. The goal is to complete 1000 urban and rural units by the end of July. Housing is an important factor in the stabilization of the population.

Other Needs - The needs of the RN beyond those outlined above begin to blend with those of the general population, although they have been given assurances of special treatment in regard to certain government services such as infrastructure, health and education services,

and social welfare programs. Although the RN has dispersed considerably about the country, the majority are located along the agricultural frontier where these government services are minimal. Any extension of government services to these areas for the benefit of the general population will obviously benefit the RN. Provision of government social services, however, has political ramifications, as well, in that government cadres at the level of service delivery are still Sandinista-oriented; this can constitute another dimension to the security problem especially in the area of health service delivery. CIAV will need to continue to monitor the politically-motivated failure to deliver proper attention to the RN on the part of the Government personnel.

The time frame for addressing RN-specific problems should be relatively short if the land issue can be resolved. CIAV feeding programs were extended over a longer period than would have been necessary had the land problem been more effectively addressed. Likewise CIAV's development programs have been constrained by the need to dedicate resources to feeding that might have been used more constructively and by the requirement that beneficiaries of such programs be settled on the land.

III. STRATEGY - Addressing strategic objectives

In the face of the overwhelming development needs of Nicaragua, the challenge in crafting a USAID strategy is to identify the key factors and interventions that will create the largest ripple effect and address the critical path for development progress. While the mission expects that levels of U.S. assistance will remain high in relative terms over the course of the CDSS period, they will not be sufficient to meet Nicaragua's development needs in every sector. Matching budgetary resources to critical needs requires careful choices and a strong focus on key issues. The strategy must serve both as a guide for AID interventions and a justification for turning down myriad requests for assistance across the board.

The foregoing analysis in light of the mission's overall goals points to both constraints and opportunities. In confronting the situation facing Nicaragua, the Mission has struggled to focus its attention in the most critical areas and address those areas where AID has a comparative advantage. The mission has identified seven strategic objectives which address the decisive issues and problems facing Nicaragua, and focus limited AID resources on the key development constraints and opportunities in Nicaragua. They are:

<i>Increased foreign & domestic investment</i>	<i>Increased competitiveness and diversification in the economy</i>
<i>Increased participation in the economy</i>	<i>Improved productive/extractive practices</i>
<i>Greater consensus on democratic values</i>	<i>Improved quality and efficiency of basic education</i>
<i>Improved maternal and child health</i>	

Each of these is further elaborated, defined, and circumscribed below; as a whole, they represent the mission's program for the next 5 years. The Mission accepts responsibility for undertaking activities which will bring about change in the direction outlined by each objective. The mission also recognizes that the number and scope of these objectives is beyond that attempted by many other programs and is likely to tax the abilities and resources of this mission as well. The Mission believes, however, that the chosen objectives can be realistically addressed over the course of the CDSS period. Many of these objectives represent one of a number inputs to other larger goals and others have been carefully defined within realistic limits through identification of the indicators and benchmarks. In formulating these objectives the mission is operating under the following assumptions:

U.S. economic assistance levels to Nicaragua will remain relatively high.

Recognizing that U.S. budget constraints and general lack of support for foreign aid may mean a gradual general decline in AID resources, the mission nonetheless assumes that development progress in Nicaragua will remain a high political objective and that resources in the order of \$200 million or more per year will be available for programming in Nicaragua.

Other major donors will require a lengthy start-up time.

As of the beginning of the CDSS period, Nicaragua had only just obtained sufficient financial support from bilateral donors to clear arrears with the Inter-American Development Bank and World Bank. These institutions may be able to provide short-term balance of payments assistance critical to economic stabilization efforts, but development of programs and projects to address other development needs will take time. While there are some sectors and activities which are most clearly in the province of the major international financial institutions, as the only major donor with an established presence USAID will necessarily have to shoulder a broader range of activities. Once these institutions have resumed activity and donor responsibilities have sorted themselves out, AID may be able to focus its strategy more tightly.

The inter-relationships between goals and objectives require concerted effort on a number of fronts simultaneously.

Discussions of mission strategy have repeatedly highlighted the strong linkages between economic, political and social development in Nicaragua. Many of these linkages are outlined in the analysis section above. Early in the CDSS period, USAID is unable and unwilling to leave critical activities unaddressed which may have important linkages to other key areas of the strategy. For example, progress in democratic values is clearly linked to basic education.

Based on these assumptions, the USAID/Nicaragua mission proposes the following strategy to address Nicaraguan development needs and move toward the overall goals of broad-based, sustainable economic growth, a stable, functioning democracy, and a healthy and literate population. It is formulated around the seven strategic objectives outlined above with special elaboration for the Atlantic Coast and members of the ex-Resistance. Where possible, objective and measurable indicators for each strategic objective are outlined and initial benchmarks for the CDSS period are proposed. Data sources in Nicaragua at the beginning of the CDSS period, however, make any attempt to propose realistic goals for a five year period largely a process of guesswork and numbers used in delineating benchmarks should be viewed primarily as illustrative with some attempt to show levels of magnitude. The mission will attempt to refine its estimates in its Action Plan submissions.

A. ECONOMIC RECOVERY & BROAD-BASED SUSTAINABLE GROWTH

The clear priority in USAID Nicaragua's strategy is to stabilize and revitalize the Nicaraguan economy. Without growth, Nicaragua will not have the resources to address social needs and democracy will founder. Four strategic objectives have been identified which the Mission believes will create the conditions for positive GDP growth which is both broad-based and sustainable over the long-term. The bulk of AID resources over the course of the CDSS period will be addressed to these needs.

Because the agriculture sector is the foundation of the Nicaraguan economy, has substantial export potential, and appears to have the greatest potential to quickly respond to a changed policy environment it will be the early sector focus for USAID economic reactivation efforts. Early in the CDSS period a detailed assessment of industry and manufacturing in Nicaragua and its potential will be carried out which will form the basis for consideration of a broader sector focus.

1. Increased foreign and domestic investment

The number one priority for the USAID/Nicaragua program is to help generate increased investment. Nicaragua must have greater financial resources to serve as the basis for development than can be provided by donors and the private sector must become the engine of growth. Increased investment in Nicaragua will require progress in a number of sub-objectives which form the basis for USAID/Nicaragua's assistance. These include economic stabilization, a functioning financial system, improved policy framework for investment, and investment promotion activities:

Investment Indicators & Benchmarks

- Private investment levels equal to 1977 levels by 1996
 - Increased number of licensed businesses
 - Increased number of approved foreign investment applications
 - Increased foreign direct investment levels in Balance of Payments
 - Appearance of U.S. fast food chain outlets in Managua
-

Economic Stabilization - Policy dialogue associated with cash transfers will be the primary means of addressing price instability. The mission will provide balance of payments assistance in support of economic stabilization measures at levels ranging up to \$125 million per year through cash transfers and private sector mechanisms.

Stabilization Benchmarks/Indicators

- Inflation reduced to less than 5% per year beginning in 1993 and sustained at or below that level through 1996.
 - Exchange rate stabilized at competitive rates by 1993.
-

Conditionality in cash transfers will be focused on the following policy areas:

Fiscal targets - especially in relation to reducing government expenditure so that external financing can be available to expand the resource base of the financial system rather than funding government expenditures.

Monetary targets - continued elimination of emissions.

Exchange rate targets - set at a level which provides current access to foreign exchange for both current transactions and normal capital transactions without exchange controls.

Financial System Reform - A functioning financial system is crucial for mobilizing domestic savings for investment purposes and providing services to foreign investors. To improve the functioning of the financial system, USAID will undertake the following measures:

Support for policy reform through conditionality in cash transfer agreements or non-project assistance. Policy measures

currently anticipated include further steps in creating and establishing a Superintendency of Banks, continued progress in licensing private financial institutions, movement toward real positive interest rates, and allocation of Central Bank financing to private institutions.

Expanding the resource base of private financial institutions through a stable source of medium term financing. While mobilization of short-term resources will begin fairly quickly, the confidence in longer term economic and political stability will take much longer. During this period, it will be necessary for donor resources to augment the deposit base of the financial system. USAID will consider some formulation of a Private Sector Commodity Import Program (CIP) run through private financial institutions as a means of providing financial resources through private institutions. A privately controlled medium-term credit fund will be supported through local currency generations from the private sector CIP.

Technical Support for Private Financial Institutions and the Superintendency of Banks will be offered through project mechanisms.

Policy Framework Supportive of Investment - Cash transfer conditionality will support implementation of the new Investment Law and streamlining of the bureaucratic requirements necessary to undertake productive investment in Nicaragua. Property rights questions will be addressed in the context of USAID's policy dialogue as appropriate given the political sensitivities surrounding the issues and they will be the focus of further study by the mission.

Other policy initiatives to improve investment potential in Nicaragua will be supported based on USAID analysis of needs and alternative proposals. AID also will assist the Nicaraguan private sector in developing the capacity to undertake its own policy analysis and advocate policies conducive to private sector development.

Financial System Indicators/Benchmarks

Functioning Superintendency of Banks by 1992

10 private financial institutions operating by 1996

Deposit base of financial institutions increased to 30% of GDP by 1996

Positive real interest rates established.

Policy Indicators/Benchmarks

Investment applications efficiently processed and routinely approved

One-stop investment processing office in operation

Effective system in place for resolving property disputes

Private sector organizations effectively analyzing and voicing policy concerns

Investment Promotion and Support - AID will provide technical and operational assistance to government and private institutions working to stimulate private sector response to an improved policy environment by promoting investment in Nicaragua. Services supported would include information campaigns, trade fairs, support for feasibility studies, investment orientation trips, etc.

Promotion Indicators/Benchmarks

Information campaign underway by mid-1992

Investment promotion office providing assistance to all firms investigating investment opportunities

2. Increased competitiveness and diversification in the economy

USAID/Nicaragua believes the most important element of improving productivity is to open the economy to increased competition both domestically and internationally. Open and competitive markets will allow producers to find arrangements for inputs and sales that maximize their returns and provide incentives for new productivity-enhancing investments. Parallel to policy improvements, AID will support efforts to promote a vigorous private sector response to these policy initiatives including an emphasis on improved export performance. AID will, therefore, promote greater competitiveness and diversification in the Nicaraguan economy through the following activities:

Policy Dialogue to Remove Barriers to Competition

A strong emphasis in USAID policy discussions with the Nicaraguan government will be removal of barriers to competition in the economy. This policy dialogue, associated with cash transfer programs and Food for Progress, will focus on:

Elimination of preferential treatment for public sector enterprise - Implicit or explicit subsidies, mandated credit, targeted contracts, and mandated marketing or input arrangements with public sector enterprise limit competition and create inefficiencies. USAID will work to create conditions which force public sector enterprise to compete on the same footing with the private sector. USAID will also push for progress in privatization efforts which are the most effective means of forcing public sector firms to compete in the market.

Competition Indicators/Benchmarks

Domestic prices in line with neighboring countries and world prices

Decreased number of commodities facing trade restrictions; reduced quantitative restrictions and tariff levels

Privatization of significant number of public sector firms

Increased number of licensed businesses

Increased percentage of sales by private sector firms in areas that were formerly under monopoly control

Increased number of products exported; non-traditional exports increase in volume and percentage of total exports

Increased value-added in manufacturing and processing

Certification of all agriculture and meat exports to U.S.

Increased private sector involvement in areas previously under monopoly control - Monopoly conditions in a number of major commodities (including coffee, rice, and cotton) eliminated competitive pressures and created inefficiencies and price distortions. USAID has pressed for policy change to eliminate such monopoly arrangements or the conditions that create them. Though legal barriers in these areas have largely been eliminated, AID will work to assure greater private sector competition and involvement.

Reduction of trade barriers - Nicaragua needs to become competitive in the world market and have access to production inputs and new technology at world price levels. USAID will press for a liberalized trade regime with special emphasis on elimination of quantitative restrictions. This will also reduce monopolistic and oligopolistic behavior.

Policy dialogue regarding structure of the economy - In policy discussions USAID will stress the importance of eliminating requirements, restrictions and barriers that would prevent new types of enterprise from being established and the potential for promotion of new types of business will be a part of all investment promotion activities.

Support for Privatization - Privatization is critical to creating an environment open to expanded competition and the manner in which it takes place will have important implications on the degree of concentration of ownership. To encourage more rapid movement in privatization and structuring of the process to maximize broad ownership, USAID will provide technical assistance to the *Corporaciones Nacionales del Sector Publico* (CORNAP) which is overseeing the privatization effort.

Medium-Term Credit - USAID will utilize local currency generations from cash transfers and food assistance to provide medium-term credit to agricultural producers and businesses through appropriate institutions. Local currency generations from the Private Sector Commodity Import Program will remain in private financial institutions.

Support for Diversification and Broader Export Sales - Broadening the structure of the Nicaraguan economy offers new opportunities for private sector entrepreneurs and reduces Nicaragua's vulnerability to world price fluctuations while improving its ability to earn foreign exchange. USAID will provide assistance to Nicaraguan producers in gaining market access and establishing producer/market linkages for a wide range of products. In policy discussions, USAID will address requirements for access to U.S. markets and will provide assistance in establishing contacts. Export promotion activities supported with technical and operational assistance will focus on non-traditional exports which have greater need for promotion than established traditional export commodities.

Technology Transfer - If Nicaragua is to improve its competitiveness in the world market it must renew its technological base and re-capitalize the productive sectors. Technical assistance and activities designed to introduce new technologies in new fields with investment and export potential in Nicaragua will be financed by AID where practicable. Emphasis will be on

potential non-traditional exports; activities will be consistent with statutory restrictions involving products that compete with U.S. production.

Participant Training - The Mission's participant training program will contribute to improving the level of human capital necessary to bring greater competitiveness to the Nicaraguan economy by targeting appropriate training opportunities to the private sector.

Infrastructure - USAID/Nicaragua does not intend to directly finance major infrastructure construction or rehabilitation for reasons stated elsewhere (see Section IV.B). However, the most critical infrastructure problems, electricity and telecommunications, lend themselves to a private sector solution. To the extent that private sector investors and producers identify particular infrastructure constraints to private sector expansion, AID may consider limited involvement in infrastructure projects through co-financing of feasibility studies and discussions with the government and other donors to facilitate other donor and private sector investment. In addition, USAID may consider limited involvement in maintenance and cost recovery efforts in areas where AID has relevant experience and there are private sector alternatives. USAID would consider such involvement in infrastructure only toward the end of the CDSS period.

3. Increased participation in the economy

To ensure that economic growth is broad-based and the benefits of growth reach as many as possible, USAID/Nicaragua will undertake the following interventions:

Employment Generation Activities - It will take time for private sector development to generate new employment opportunities; in the meantime there will be a need to create short-term employment opportunities for Nicaraguan men and women in order to address the serious unemployment problems facing the country. Early in the CDSS period the Mission will continue Employment Generation activities until other donor financing takes over and/or economic reactivation begins producing long-term stable employment.

Policy Dialogue Related to Structure of Ownership - In policy dialogue discussions regarding the creation of new financial institutions, privatization, and the direction of investment promotion efforts, USAID will attempt to focus attention on the need for broad ownership and the need to maximize employment potential. A first step will be to assure that legislative and bureaucratic restrictions on economic activity are eliminated. Cash transfer resources will be focused in this direction.

Participation Indicators/Benchmarks

- Reduction in unemployment rate by 25%
 - Number of registered businesses increases by 40%
 - Number of business owners/agricultural producers increases
 - Increased number of viable small/micro enterprises
-

Policy Dialogue Related to Credit Allocation - USAID will discuss credit allocations with the government to assure that credit is available to a broad range of producers in all sectors and that the criteria used in granting credit is merit-based and properly. Qualifications for credit should not discriminate against women. USAID will ensure that access to foreign exchange from cash transfer disbursements is as broad as possible. Allocations of local currency and conditionality in cash transfers can form the basis for discussions in these areas.

Support for Credit Unions - Because of their ability to provide financial services to segments of the population not likely to be reached by private banks, USAID will provide technical assistance to credit unions and access to medium-term resources similar to that available to private banks.

Support for Micro-enterprise - Training and technical assistance will be provided to small and micro-entrepreneurs through programs managed by private financial institutions. Such programs may also create mechanisms to increase access of micro-enterprises to credit. Special consideration in the programs will be given to the disabled.

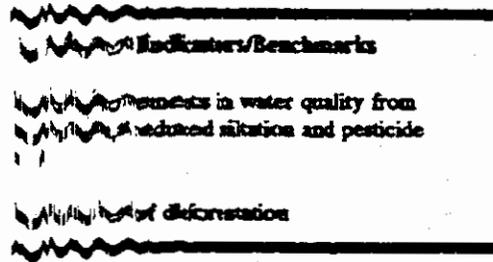
Technical Assistance for Privatization - Because privatization takes place has important implications on the degree of concentration, USAID's technical assistance to the organization overseeing privatization will emphasize the importance of broad ownership.

Participant Training - The Mission's participant training program will provide opportunities for expanded participation in the economy in its formal sector. The participant training program will recruit broadly with special attention given in areas in which they are under-represented and disadvantaged groups.

Broad-based Technology Transfer Programs - In supporting technology transfer (e.g. agriculture extension) special effort will be made to reach small producers.

4. Improved productive/extractive practices

The primary focus of this objective is to manage resources in a sustainable way so they form the basis for long-term growth. The most effective means of conserving, protecting and improving the resource base is to change the productive and extractive practices which affect resource management. In trying to change the way individuals, government, and businesses use and extract resources for productive purposes to achieve sustainable resource management, USAID will undertake the following activities:



Policy Dialogue Regarding Resource Use - Incentives and disincentives involved in various productive and extractive practices can be the most important factors in changing behavior patterns. Government policy is often a primary factor in establishing the structure of incentives and disincentives and assuring that market prices reflect externalities and encourage sound practices. Policy action can therefore be the quickest and most effective means of addressing resource use patterns. A policy inventory will be undertaken early in the CDSS period and will be the starting point for further analysis and discussion with the government. AID will consider non-project assistance to affect critical policy areas identified in this process and will focus project interventions on policy areas as appropriate.

Institutional Strengthening of IRENA - The Nicaraguan Institute for National Resources and Environment (IRENA) can play a major role in addressing resource use through its regulatory and investigative functions. In addition, it should become the focus for policy analysis and formulation related to resource use and environmental protection. Plans are already underway to provide significant technical assistance and training to IRENA so that it can play its intended role in improving sustainability of resource use. These activities will continue throughout the CDSS period.

Improvement of Agricultural Practices and Watershed Management - Specific problem areas related to water quality as affected by agricultural practice and soil conservation will be addressed through project activities. Currently, AID contemplates project activities to address pesticide use practices, and project development of watershed management projects for funding by other donors such as the World Bank or Inter-American Development Bank.

Re-Oriented Economic Activity related to Protected Areas - AID intends to focus project activities on resource extraction and productive activities centered in and around newly protected forest and wildland reserves. They will address sustainable management and extraction of forest resources, and alternative economic activities such as appropriate agricultural practices, commercial fuelwood processing, and eco-tourism. AID will also support the development and implementation of management plans for the reserves themselves.

Support for NGO's and PVO's Addressing Resource Use - AID will provide support to non-governmental organizations and private voluntary organizations undertaking projects which contribute to sustainable resource use.

Technology Transfer - AID-supported technology transfer programs will emphasize technologies which are appropriate and conducive to sustainable resource use.

Environmental Education - AID will support public information campaigns and incorporation of environmental/resource use study into the formal school curriculum.

B. DEMOCRATIZATION

While growth is the most critical need for Nicaragua during the next five years, this period is also critical for the consolidation of democracy and the two broad goals are interlinked. Without economic stabilization and growth, democracy is not likely to flourish; economic improvement will require effective action by democratic institutions and political freedom is an important complement to the operation of a free market economy. In the Nicaraguan context, a successful democratic transition and improved functioning of key institutions will clearly play a role in improving investor confidence and providing the foundation for economic stabilization and growth. The second major priority area in USAID's strategy is support for the consolidation of democracy in Nicaragua.

The Mission believes that transformation of the political culture is essential to the firm establishment of a democratic system of government in Nicaragua and will orient its support to institutions and activities around that guiding principle:

1. Greater Consensus on Democratic Values

As the Mission has considered how best to promote democracy in Nicaragua, it has carefully reviewed a broad range of potential interventions, many of which have become standard elements of AID Democratic Initiatives projects in other Missions. The mission believes, however that the key element necessary for the growth of democracy in Nicaragua is some consensus on the rules of the game or the underlying values which give shape and substance to democratic society. Of the variety of activities the Mission could undertake which could have a positive impact on the operation of democratic government, the Mission will focus its interventions around the achievement of a consensus on democratic values as its primary strategic objective leading toward a functioning stable democracy and support activities with direct and

Democracy Indicators/Benchmarks

- Increased acceptance of democratic values as measured in independent surveys
 - Free and fair elections successfully implemented in 1996
 - Reduction in politically motivated disruption - strikes/demonstrations
 - Decreased levels of human rights abuse
 - Reduction in size of government in terms of percentage of GDP and number of government employees.
 - Devolution of budget authority to local governments for selected government functions.
 - Public perceptions of improved government effectiveness in key areas as measured by public opinion surveys: management of the economy, administering justice, fairness, provision of services.
 - Establishment of certified accounting systems and financial controls in key government entities.
 - Increased relevance of the National Assembly in decision making as measured by the ratio of legislation to decrees, amount of legislative revision to administrative initiatives, and surveys.
-

indirect impact in that area. The Mission views such a consensus as critical to the effective operation and legitimacy of democratic institutions and an important means of assuring that those in power act in accordance with the will of the people and protect individual rights. Without it, Nicaraguan democracy will remain fragile; there will be form without substance.

USAID places special importance on the following values/attitudes related to democratization in Nicaragua: 1) equal opportunity and merit, 2) protection and respect for basic political and economic rights, 3) majority rule and institutional means of resolving conflict, 4) accountability for public officials and checks on power, 5) access to information, 6) a limited economic role for government, and 7) the right to private property and importance of free, competitive enterprise. Activities in support of democratization will directly promote these and related value orientations and also strengthen key institutions critical to a functioning democracy and which play an important role in forging a consensus on the key elements of a democratic Nicaraguan political system and government:

Civic Education - AID will support efforts by private organizations and interest groups which initiate public education campaigns using media, workshops, and other means of promulgating information and promoting values conducive to democracy. School curriculum changes to incorporate civic education will also be supported.

Support to Key Organizations for Forging a Consensus on Values - USAID will provide assistance to organizations, interest groups, and institutions that play important roles in the democratic process. A primary criterion for selecting these groups will be the role they play in articulating and promoting the values and attitudes that support democracy. These groups include:

The Press - Newspapers, magazines, and broadcast media play an important role in the dissemination and collective development of values and attitudes related to the political and economic system. The kind of stories and editorials that appear in the press, the type of investigative journalism conducted, the level of coverage of the processes of democratic government (legislature, cabinet, courts, etc.), and the degree of objectivity in the press all have an enormous impact on the values and attitudes of the Nicaraguan public. USAID will finance activities which support increased objectivity in the press (such as training for journalists), improved outreach, and a broader range of media outlets.

Support for Selected Interest Groups - USAID believes that private human rights groups which investigate and publicize human rights abuses play a pivotal role in developing values related to individual political and economic rights. Free democratic unions can offer alternatives to radicalized Sandinista unions by offering greater participation through internal democratic processes. Finally, political parties have a particularly important role to play in establishing standards and expectations regarding democracy in Nicaragua. To the extent they conduct their activities within the channels and processes of a democratic system they confer legitimacy on the institutions of democratic government and broader acceptance of democratic procedures and mechanisms. USAID will support groups such as these which

demonstrate a commitment to a democratic system of government in their efforts to create a greater consensus around democratic values.

Support for Constitutional Reform Efforts - Constitutional reform will likely be an expression of societal consensus around democratic values. To the extent AID can play a constructive role in this process, appropriate activities will be considered.

Improved Government Effectiveness in Key Areas - Nicaraguan government institutions operating under a democratic system of government must be able to at least partially meet the high expectations raised during the election and create a positive early experience with democratic rule. They must show progress in meeting the critical needs of society, demonstrate accountability, and appropriately represent the people of Nicaragua. Thus, a number of government institutions also play an important role in the development of attitudes and values related to democracy.

USAID/Nicaragua activities to improve government effectiveness will focus on 1) efforts in support of reducing the size and scope of government activities and decentralizing government functions where appropriate, and 2) supporting improved operation of those government entities which perform functions critical to improved representation, justice, and accountability.

Support for Efforts to Reduce the Size of Government and Decentralize Appropriate Government Functions to Local Levels - USAID/Nicaragua firmly believes that the scope of government in Nicaragua must be radically reduced to restore greater efficiency and effectiveness to those essential government functions of regulation, enforcement, and provision of certain limited social services. Economic stabilization pressures push for reducing the size of government and Nicaragua's limited internal capacity argues for concentrating skilled personnel and scarce budgetary resources on essential functions. Appropriate decentralization of decision-making, implementation, and budget authority can create improved responsiveness and effectiveness in important areas of government responsibility.

Policy discussions related to cash transfers or non-project assistance will focus on privatization of public sector enterprises and functions to the maximum extent possible and/or decentralization to local levels as appropriate. AID will support voluntary retirement programs, privatization processes, and other efforts to reduce the size of government. Where private sector alternatives to government programs exist in areas central to the AID strategy, they will have preference for AID assistance.

Support for Government Institutions Critical to Functioning Democracy - USAID will provide support to those government entities whose effectiveness is critical to the functioning of a democratic system of government. Of primary importance are those institutions which carry out representative and judicial functions and assure accountability throughout the government. These include:

National Assembly - Support to the legislature will allow it to fulfil its role as the primary representative institution and establish greater institutional power vis a vis the executive branch. Assistance will also be provided to improve its internal operations in resolving conflict and forging consensus on divisive issues of national policy.

Electoral Commission - Late in the CDSS period, assistance will be provided to the Electoral Commission to prepare for and monitor the 1996 national elections.

Judicial Institutions - USAID will undertake a study of the judicial system early in the CDSS period to determine appropriate means of support for judicial institutions.

Comptroller General - To address the limited capacity for accounting, contracting and management in government institutions, USAID will provide support to the controller general to establish such systems and install financial controls.

Municipal Government and Decentralized Institutions - In conjunction with substantive policy movement toward decentralization and as a means of supporting devolution of authority to local levels, AID will consider direct assistance to local government institutions where appropriate in implementing its overall strategy.

Support for Government Institutions Critical to Progress in Other Strategy Areas - In areas where government has a legitimate and important role, USAID will provide technical assistance and support to those governmental institutions whose responsibilities are important to the success of other strategy initiatives. Such support is identified in the outline of other aspects of the strategy and includes such activities as support for the Superintendency of Banks, institutional strengthening of IRENA, and improved administrative efficiency in the Ministry of Education. Appropriate indicators of these activities are identified under other strategic objectives.

Participant Training - The Mission's participant training program incorporates a Caribbean and Latin America Scholarship Program component which includes an orientation to U.S. democratic institutions and processes. Participant training will be designed to focus on government organizations which play a key role in improving government effectiveness and will also provide opportunities for local leadership at regional and municipal levels.

C. QUALITY OF LIFE

While USAID/Nicaragua believes broad-based sustainable economic growth and democratization will have the largest impact on quality of life in Nicaragua there are other important factors that need to be addressed. Among the most critical inputs to both economic growth and democratization is education and it is a priority area for AID involvement. Unrestrained population growth will quickly dilute the impact of economic and social advances and limit the

prospects for widespread economic improvement in Nicaragua; thus, AID will support voluntary family planning efforts. Finally, AID will attempt to address the most critical health problems facing Nicaragua. The following strategic objectives reflect these concerns:

1. Improved quality & efficiency of Basic Education

The clear priority in the realm of education over the CDSS period is primary education focused on improved literacy and numeracy. USAID/Nicaragua views improved quality and efficiency of basic education as the foundation for improvements in education at other levels and, because it reaches the largest percentage of the population, particularly important in preparing Nicaraguans to participate effectively

in a revitalized economy and a democratic system of government. To improve the quality and efficiency of Basic Education USAID will support the following activities:

Education Indicators/Benchmarks

Increased percentage of children entering first grade graduating from sixth grade from 22% to 33% by 1995 equipped with greater skills

Reduced rates of repetition and drop-outs.

Curriculum Development - Technical assistance and equipment will be provided to improve the capacity of the Ministry of Education to develop an integrated curriculum appropriate to Nicaraguan needs and incorporate modern learning theory approaches. This assistance will also develop the capacity to produce textbooks locally so future textbooks can be procured/replaced by the Ministry. Curriculum development activities will include incorporation of civic and environmental education.

in-Service Teacher Training - USAID will support a series of workshops addressing instructional techniques which utilize demonstration, hands-on training, and role playing to address a limited number of concepts. In addition, AID will support development of innovative Teacher Training Centers for coordinated and de-centralized training of primary school teachers using existing teacher training institutions in each Region including revitalized training curriculum. Other alternative strategies for accrediting teachers will also be explored. Budget support from local currency generation may be provided so that teacher salaries can be increased. Trainers of trainers will be targeted under the Mission's CLASP program to further inculcate democratic values.

Improvement of Ministry of Education Administrative Efficiency - Technical assistance to re-organize the Ministry of Education will be provided to improve its overall efficiency. Policy dialogue and some conditionality may be necessary to address legal obstacles to improved organization of the Ministry.

2. Improved maternal and child health

USAID's objectives in the health sector reflect the fact that the most critical health problems facing Nicaragua affect mothers and children disproportionately and are best addressed through a primary health care approach. Therefore, USAID will focus on interventions which improve the health conditions of children and address problems related to childbirth. Certain regions of the country are more affected by poor health conditions as reflected by Ministry of Health indicators. These regions, designated by the Ministry as priority regions, will receive special emphasis through USAID programs. To fully address health problems in these regions, activities to improve rural water and sanitation must also be implemented.

Population Indicators/Benchmarks

Reduction in infant mortality as measured in various regions of Nicaragua

Contraceptive Prevalence Rates increase by 10% by 1996.

AID's priorities in the health sector are to improve the primary health care delivery system, reduce mortality and morbidity rates due to diarrhea through improved water and sanitation services, assure that basic measures for ensuring the health of children are widespread practices, and increase contraceptive prevalence. Projects directly managed by AID and by USAID-funded PVO's will reflect a regional approach. Because the issue of health care financing has budgetary repercussions related to public health measures, AID will undertake policy discussions in that area. AID will support the following activities in coordination with numerous other donors in the health sector:

Maternal/Child Health Activities - AID will support activities which focus on child survival interventions (oral rehydration therapy, immunization, promotion of breast feeding, growth monitoring, etc.) in priority regional areas and municipalities. AID will also support regional and municipal level programs of the Ministry of Health focused on maternal/child health in the priority regions of the Ministry of Health's Master Plan.

Improved Rural Water and Sanitation - AID will consider support for installation of potable water systems using appropriate technologies - gravity-fed piped systems and drilled or shallow wells with hand pumps - in small rural communities and construction and use of simple or composting latrines as appropriate. AID's work in this area will be contingent on level of assistance generated by other major donors, particularly the IDB, and will be coordinated with their efforts. In coordination with construction of water and sanitation systems, AID would support health and hygiene education efforts undertaken by community health workers and participating PVO's in rural communities.

Health Financing Reform - AID will provide technical assistance to the Ministry of Health to present and analyze options for financing health care at various levels in Nicaragua. AID will also consider non-project assistance in support of identified policy changes related to health financing and/or privatization of portions of government health infrastructure. Non-project

support funds could be provided to create a revolving fund for procurement of medicines for the health sector.

Increased contraceptive prevalence - The key element necessary to bring about improved family planning in Nicaragua is increased use of contraceptives. AID will support the efforts of private family planning organizations working in the following areas:

Expansion and regionalization of family planning service delivery networks to all regions of the country.

Provision of regular and low-dose oral contraceptives, condoms, and spermicides at affordable prices.

Establishment of family planning education programs to emphasize the benefits of family planning and birth spacing to include maternal and child health education; family planning education; sex education for adolescents; design, testing, and publication of informational materials; and other promotional activities.

Training of volunteer contraceptive distributors, physicians and nurses from the Ministry of Public Health, social workers, and community leaders.

Development of strategies to foster the development of alternative family planning service delivery systems.

D. TRAINING

USAID/Nicaragua is designing a major participant training program to support work in all areas of the strategy and provide alternative training and educational opportunities for Nicaraguan men and women. As noted above, training is targeted to both the private sector and selected public sector entities with key functions in relation to the Mission's objectives. Training activities undertaken by the Mission will include long-term academic training at U.S. universities but will focus primarily on medium-term training in the U.S. and third countries designed to address particular technical and managerial needs. An important component of the project will be the Caribbean and Latin American Scholarship Program (CLASP) which provides training in technical skills or management as well as a basic orientation to the functioning of democratic government in the United States and bolsters the Mission's democratic values objective. The CLASP program will support mission efforts in agriculture, education, democratic initiatives, and health. Other areas of emphasis will be key ministries, critical infrastructure and services, and private sector associations. The Mission estimates that up to 1200 Nicaraguans will receive some type of training through USAID programs over the next five years; special effort will be made to provide access to training for women and disadvantaged groups.

E. ATLANTIC COAST

The strategic objectives outlined above all touch on problems facing the Atlantic Coast. Ongoing and planned AID activities to stabilize the economy, promote increased agricultural production, improve basic education, etc. will have positive impact in the Atlantic Coast region. In a number of areas, however, AID will make a special effort to assure that its programs reach this area and address its particular needs. These efforts include:

Employment Generation - AID has designed a specific component of its Employment Generation project to address short-term employment needs on the Atlantic Coast as part of a broader economic reactivation effort for the region. As with other AID programs, employment generation efforts will include opportunities for both men and women.

Infrastructure Improvement - Employment generation activities will be focused on small social and physical infrastructure and maintenance and improvements to the major roads and river transportation routes in the region. AID is also financing a major Rural Electrification effort in the Bluefields area.

Natural Resource Protection/Resource Use Economic Reorientation - AID intends to support the establishment and management of at least one protected area in the Atlantic Coast region. This includes support for management of the reserve and economic reorientation activities with the local population. In addition, employment generation activities include thinning and reforestation of large expanses of regenerating forest lands.

Agriculture Reactivation - AID is providing seed and tools through CIAV/OEA for agriculture reactivation in the region and development of fruit tree seedlings.

Monitoring of Health and Nutritional Status - Though initial assessments indicate that there are not exceptional health or nutritional problems in the region, AID will support a continuing study of the health and nutrition needs of the region and will also repair a number of rural health centers.

Resettlement Activities - AID will continue to monitor the CIAV/OEA/UNHCR and government programs for refugee and resistance resettlement in the region.

F. RESETTLEMENT

Integration of the ex-Resistance and returning refugees in Nicaraguan society is important for both political and economic progress and AID has supported this process through its support to CIAV/OEA. Consistent with the winding down of this assistance and the Mission's Short-Term Strategy, USAID believes that the development of special programs or projects designed with the ex-Resistance as sole beneficiaries is neither developmentally sound nor politically

advantageous. All USAID program and projects will be designed so that the ex-Resistance will be able to participate fully and equally with all other Nicaraguan citizens. USAID/Nicaraguan will undertake the following activities in support of reintegration goals:

Extension of Support for CIAV Security Program - Though support for broader CIAV programs will be phased out, support for the Security Program will continue through June of 1992 to assure the safety of those resettled and contribute to maintenance of social order in regions populated by the ex-Resistance. USAID will not provide additional assistance to CIAV beyond this extension.

Tracking of RN Participation in USAID Programs - USAID/Nicaragua will make a special effort to track the level of participation of ex-Resistance members in specified programs to assure that they have access commensurate with other groups in Nicaraguan society. For example, AID will track ex-Resistance participation in training programs and employment generation. AID will also make a special effort to assure that the geographic focus of its activities encompasses areas that are heavily populated by the ex-Resistance. The Atlantic Coast activities outlined above are an example.

IV. ROADS NOT TAKEN

In laying out and explaining the strategy that will guide USAID/Nicaragua over the next five years, it may be as important to state clearly those areas in which AID does not intend to be active as to identify plans for action. USAID/Nicaragua has received innumerable requests for assistance in a wide variety of activities which address critical needs in Nicaragua and are generally well intentioned. However, given the limits on USAID budget and personnel resources, the Mission simply cannot respond to them all. This section attempts to clearly outline those areas which do not fit into the mission strategy and explain why they are not included.

There are also some areas which are not included in the strategy due to lack of sufficient information at the time the CDSS was drafted. Generally these fit within the strategic objectives outlined above, but the mission intends to retain flexibility in considering these and other options for addressing its objectives.

A. Roads Deferred

The mission may yet consider activity in the following areas later in the CDSS period. At this point there are still some holes in the mission knowledge base - while the destination may be promising, there is no map. The CDSS proposes a number of studies or assessments to outline the needs and opportunities presented in these areas which could form the basis for project design or some type of non-project assistance. They include:

INDUSTRY/MANUFACTURING - Though at this point the Mission is confident that a focus on agriculture is appropriate, there is very little information available on the state of industry and manufacturing in Nicaragua. Once more information is available on other productive sectors, the mission may consider some type of involvement to address particular needs or opportunities.

ADMINISTRATION OF JUSTICE - While there are obviously problems to be addressed in the judicial system, means of addressing them have not yet been identified clearly. A planned study will provide an assessment of the judicial system and recommend areas for USAID involvement.

MUNICIPAL GOVERNMENT - USAID recognizes the importance of decentralization as a means of providing citizens with a greater degree of control and improving efficiency of government. A study will help determine where there is a useful role for AID to play in strengthening capacity at local and municipal levels or supporting the process of decentralization and devolution of power to local levels.

B. Roads Not Chosen

In establishing its strategy, USAID/Nicaragua has chosen not to be involved in a number of critical areas. The reasons these areas are not a part of AID's strategy are generally one of the following:

Other Donors are already active or plan to be active in that area; USAID activity would crowd the field and have relatively less impact.

Higher priorities have been determined in the strategy and take precedence.

Costs involved would detract from other priority areas in USAID's strategy.

Institutions or counterparts who would be involved in potential activities are so politicized at this time that USAID involvement would not be productive.

Lack of Expertise or Experience in that area on the part of AID; it is not part of AID's comparative advantage.

AID and LAC Bureau Objectives are not furthered by such activities.

AID Regional Programs can better handle these activities.

Among the substantive areas that are not included in this CDSS are:

Infrastructure - Except for a relatively small effort in the Atlantic Coast region, USAID/Nicaragua does not intend to directly finance major rehabilitation/reconstruction or new construction of physical infrastructure. Though infrastructure improvement is a critical need in Nicaragua and will contribute to the investment climate and overall productivity, the Mission believes that the costs associated with these programs are prohibitive, and that for AID to take on this kind of responsibility would severely limit the availability of financial resources to respond to program and policy areas which are likely to have the type of long-term impact needed to restore economic and financial viability to the Nicaraguan system. USAID/Nicaragua staffing limitations also foreclose significant involvement in infrastructure programs.

Thus, USAID/Nicaragua does not intend to become involved in construction and/or rehabilitation of hospitals, schools, and municipal buildings, provision and installation of electrical generation equipment, building or refurbishing roads, replacement of telecommunications equipment, financing irrigation systems, construction and furnishing radio and television broadcasting facilities, financing of warehouse facilities, etc.

These types of activities are among the strengths of the major international financial institutions and AID will encourage the World Bank and IDB to consider investments in these areas. USAID also believes that some aspects of Nicaraguan infrastructure could be privatized and would be able to attract private investment funds. As noted in the strategy, AID may be willing to facilitate movement in this direction.

Housing - USAID does not plan to become involved in housing construction for reasons cited above related to other infrastructure. AID's approach to housing is to support housing finance schemes in support of a private sector solution to housing needs. Though USAID believes economic growth will be the most effective means of addressing housing needs, the Mission will continue to work with the RHUDO Office in Honduras, to see what assistance can be offered in finding private sector alternatives to deal with housing conditions in Nicaragua.

University, Vocational, and Secondary Education - Though there are clear needs in areas beyond basic education, AID priorities will be on primary education. The participant training project will also address needs for advanced training.

Secondary education will benefit from general reorganization of the Ministry of Education and from some curriculum development efforts but will not be a major focus of AID programs in Nicaragua. The most critical need is for the primary education system to produce more and better qualified entrants to secondary school.

Vocational education proposals from PVO's will be considered for funding under USAID's PVO Co-Financing Project. Given USAID's assessment of vocational training needs, however, there does not appear to be a need for additional investment in vocational training until more jobs have been created to employ those already skilled in the workforce.

Universities will benefit from a University Textbook program run through the RTAC project which will provide students with access to textbooks currently unavailable. Until the universities become more effectively administered and less politicized, additional AID assistance is not likely to be effective.

In the area of primary education, a USAID assessment has recommended that a school feeding program be initiated to address nutritional constraints to learning. Because previous AID experience with school feeding programs has not been positive, AID will encourage other donors, possibly the World Food Program, to support such a program in Nicaragua. Other bilateral donors may have an interest in school feeding programs and ROCAP is working on the development of a "school cookie" to provide basic nutrition to students.

Centralized Ministry of Health Programs - The Health Sector is crowded with bilateral, multilateral, and PVO assistance from other donors. This support from other donors addresses both institutional support for the Ministry of Health as well as programs in child survival emphasized by AID. While AID strategy is to support such initiatives through PVO's and local governmental institutions, there is no compelling reason to become involved in ongoing centralized efforts given the level of other donor support. USAID assistance in health financing will probably have an impact on centralized programs by addressing their efficiency and their potential for privatization.

Rehabilitation - The years of war have meant that many Nicaraguans have suffered disabling injuries and their rehabilitation needs have been extensive. However, a USAID assessment indicates that ongoing programs, a number of which were funded under early USAID programs in 1990, are meeting the demand for rehabilitation services and additional USAID involvement would be counterproductive. The more critical need for disabled veterans or victims of the war is for employment opportunities which AID will address through micro-enterprise programs and other job-creation activities.

C. Sidetrips - Targets of Opportunity

It is impossible to foresee the future. Though the Mission is confident of the overall thrust of the strategy outlined here, there will inevitably arise unforeseen opportunities and urgent needs which AID will be well situated to address. An example is the university textbook program which does not fit into the strategic focus on basic education but presents the mission with a high-profile, high-impact activity with a low management and resource burden for the mission. Where such opportunities arise within limited resource constraints, the mission will retain some flexibility to depart from the strategy focus to address compelling opportunities and emergency needs.

V. RELATIONSHIP TO LAC BUREAU OBJECTIVES

USAID/Nicaragua's strategy for the next five years fully supports the LAC Bureau objectives; in most areas there is total convergence between the Nicaragua strategy and Bureau objectives.

Broad-based, Sustainable Economic Growth - The primary Bureau and Nicaragua country specific goals are identical and the strategy focus on policy to support investment, productive employment, and competition and diversification coincides directly with Bureau objectives as does the concentration on private sector response. The mission's objective of improving productive and extractive practices is designed to further preservation and sustainable use of the natural resource base and is based squarely on affecting the policy framework, institutional capacity, and management of resources as identified in the objectives.

The Mission's strategy addresses Bureau objectives of improving opportunities for the historically disadvantaged through its focus on expanded participation in the economy and the "quality of life" strategic objectives addressing quality and efficiency of basic education, and improved maternal and child health. While these have clear linkages to economic growth, the Mission has separated them out because of their broader implications for democratization and general social well-being. The strategy's emphasis on the Atlantic Coast region and resettlement of the ex-Resistance also supports improved opportunities for the historically disadvantaged.

Support for the Evolution of Stable Democratic Societies - The Mission focus on building consensus surrounding democratic values and improving the effectiveness of selected government institutions coincides with the Bureau objectives related to support for democracy and the strategy largely focuses on the Bureau's performance indicators related to those objectives.

Responding to Specific Challenges - The Mission's attention to resettlement needs of the ex-Resistance in cooperation with CIAV/OEA and its work to prevent environmental degradation address specific challenges requiring international cooperation.

VI. RELATIONSHIP TO OTHER DONOR ACTIVITIES

With arrangements in place to clear Nicaraguan arrears with the World Bank and Inter-American Development Banks it is expected that they will become the principal multilateral donors. The strategy presented here will complement what has been articulated by representatives of these institutions.

World Bank - Once its arrears are cleared, it is expected that the World Bank will undertake a major program of IDA-funded assistance. The Bank's program in its early years will emphasize fast-disbursing, policy-based assistance. The Bank is expected to provide an Economic

Recovery Credit of approximately \$100 million in 1991. Much of this, however, will be required to repay the bridge financing used to eliminate arrears to the Bank itself. However, in 1992, the Bank is expected to provide another Economic Recovery Credit of a comparable amount which will provide substantial assistance to the balance of payments. It is also likely that the Bank will provide a policy-based program in one of the social sectors in the first half of our CDSS period.

The Bank's policy matrix closely parallels that of AID. In the early stages, the Bank will emphasize reforms in trade policy and the reform of the financial sector. The bank will also be studying policies related to infrastructure, property rights issues, privatization, and environmental issues. As the World Bank moves to take the lead in issues of macro-economic policy, USAID will focus greater attention on sectoral policy issues with particular emphasis on the private sector and creating a "level playing" field within the economy.

Inter-American Development Bank - The IDB, once its arrears are cleared, is expected to be a major supplier of resources to Nicaragua. Design is already well advanced for a \$60 million water and sewerage rehabilitation project as well as a \$30 million project, co-financed with the Government of Denmark, to rehabilitate the electrical system. The IDB is also likely to undertake a feeder roads project in the \$30-40 million range in late 1992. In addition, the Bank will undertake major micro-enterprise activities if institutional obstacles can be overcome. The IDB will be supplying major balance of payments support over the CDSS period, including a financial sector adjustment loan and probably an agricultural sector adjustment loan. Later in the period, the IDB may undertake a major project in the health sector.

Finally, the Bank will have an unusually large technical assistance program, reflecting the weaknesses of Nicaraguan public institutions, with emphasis on strengthening the Social Emergency Fund (FISE), CORNAP, the Central Bank, agricultural institutions in general, and other institutions which will be implementing IDB projects.

Bi-Lateral Donors - In addition to the multilateral agencies, Nicaragua continues to receive a wide variety of assistance, especially from European donors. While it is difficult to summarize this assistance which goes to a wide variety of destinations in relatively small amounts, the most important areas of other bilateral donor involvement are in a range of health activities. In addition, German assistance is being provided to rehabilitate the electrical system and both German and French assistance is being provided to assist in the rehabilitation of the phone system. The Swedes have been involved in environmental and forestry issues and other European bilateral donors are supporting government sponsored vocational education. Significant amounts of other bilateral assistance has been pledged to support arrears clearing as well as emergency employment and other countries provide emergency food assistance.

Since the major multi-lateral donors are only just beginning to develop their program, AID will work closely with them to assure that major programs are coordinated to avoid duplication or overlap and serve to complement on-going efforts. The Mission will adjust and focus its program in relation to that of other multi-lateral and bilateral donors as appropriate.

VII. RESOURCES

Ultimately, the USAID/Nicaragua strategy must be translated into budget and staff levels which reflect the strategic focus and priorities. Outlined below is an initial attempt to attach numbers to objectives and goals.

A. Program Funding Resources

The strategy articulated here requires a yearly program budget of at least \$200 million in combined Economic Support Funds and Development Assistance throughout the CDSS period and also assumes additional resources through food assistance. The external assistance needs of Nicaragua are so enormous that even with the opening of financing through the World Bank and Inter-American Development Bank, large flows of U.S. assistance will be required to stimulate economic development and support efforts to consolidate democracy and address social needs. The government of Nicaragua's economic stabilization and recovery plans are based on consistently high levels of balance of payments support from AID and the project portfolio is an essential complement to these efforts.

The Resource Table on the next page, based on Approved Planning Levels for the 1993 Annual Budget Submission, provides an illustrative look at how the strategy translates into budget levels. The Table extrapolates forward from projects and programs currently underway to suggest how the strategic focus presented here might manifest itself in projects and programs throughout the period. The specific projects and programs identified are clearly only illustrative for the latter portion of the CDSS period as determinations regarding interventions will be based on further study, experience in ongoing projects, evaluation results, changes in the political, economic, and social situation in the country, and the activities of other donors. Plans for the next two years are more firm but remain flexible in order to be responsive to changes within the Nicaragua, and new information. Further refining of this Resource Table will come in successive Action Plans.

Though the Resource Table presented can only be considered illustrative, it highlights some basic underlying themes and trends related to USAID/Nicaragua's planned use of resources:

Allocation of Resources Toward Major Objectives - The Table shows approximately 75% of program resources dedicated to objectives leading toward the goal of broad-based, sustainable economic growth. The remaining 25% is split more or less equally between democratization and social objectives. This approximation reflects the Mission's general sense of relative priorities and needs for the CDSS period.

Allocations of Balance of Payments Support - The Mission intends to allocate its balance of payments support to three major programs: 1) direct cash transfers to the government with policy conditionality, 2) a private sector commodity import program run through private financial institutions, and 3) non-project assistance to support occupational conversion plans to

reduce the size of government and other sectoral policy objectives. The Table suggests the relative split the mission sees between these programs.

Increased Consideration of Non-Project Assistance - The Mission believes that non-project assistance modes may prove to be effective alternatives to projectized assistance in the latter portion of the CDSS period. At that point, the policy bottlenecks will be clearer and USAID will be in a better position to analyze sector needs and initiate policy dialogue on specific sector issues. In a mission with relatively low staff levels compared to other missions with similar programming levels, non-project assistance is also a means of limiting the management burden on USAID staff.

High ESF requirement - Unless Nicaragua is designated as a Relatively Less Developed Country (RLDC) for all AID purposes, the Mission's minimal ESF needs will be in the range of \$175 million per year throughout the CDSS period. While the Mission has a fairly large and diverse portfolio, the Nicaraguan government is not in a position to provide the 25% counterpart contribution required in DA projects - which can be waived only for designated RLDCs. Nicaragua meets all the requirements for designation as an RLDC but has been designated an RLDC for the purpose of debt forgiveness only. Inability to waive the government contribution has created significant design problems for the mission and is a serious constraint to the use of DA funds for a broad range of project activities.

Food Assistance - Planning levels for the CDSS period are considerably lower than Food for Progress levels in the first years of the USAID/Nicaragua program and are identified as Title III. The Mission believes the planning levels represent only a minimum level of food assistance for the CDSS period. Food for Progress is a more flexible and appropriate allocation for the Nicaragua program than Title III.

Mortgage Buy-Down - The rapid start-up of the Nicaragua mission in a situation where AID is the only major donor has led to a large project/program portfolio which was created with only minimal initial obligations. The Mission's mortgage level at the end of FY-92 is expected to be \$90-\$100 million. New project starts are expected to be minimal in FY-93 in order to buy down the mortgage and concentrate mission attention on implementation.

Local Currency Use - The Resource Table does not reflect local currency allocations or levels. Local currency is expected to be generated from cash transfers, the private sector CIP, food assistance, and some non-project assistance. The primary use of this local currency will be for medium-term credit through appropriate institutions.

B. Staffing and Operating Expenses

USAID/Nicaragua recognizes that budget austerity creates constraints for staffing and operating expense levels over the course of the CDSS period. In response, the Mission is making a concerted effort to keep its program as focussed and uncomplicated as possible to minimize the management burden to the mission. Nonetheless, the Mission cannot establish and implement a

program meeting essential Nicaraguan development needs as outlined in this strategy without a minimum of 24 U.S. direct hire positions and 5 U.S. personal services contractors funded from operating expense funds. Current planning levels for staffing and operating expenses are unrealistic for a program that already exceeds one-half billion dollars and must meet high levels of accountability. Over the early part of the CDSS, USAID/Nicaragua is extremely dependent on its U.S. direct hire staff because of the limited availability of Nicaraguan bilingual professionals and support staff. For several more years, USAID/Nicaragua will be hiring and training a local staff to establish a normal FSN workforce. U.S. direct hire staff will continue to have to carry out their own responsibilities as well as those they would normally delegate to local staff.

VIII. CONCLUSION

The strategy presented in this document is an extremely ambitious one. It is difficult to overemphasize the degree of change in the Nicaraguan economy and Nicaraguan society which it envisions. Slightly more than one year ago, when the Chamorro Government assumed power, it faced a deeply polarized society with no tradition of democratic transfers of power or acceptance of the rule of the majority on the part of a losing minority. It immediately faced general strikes and an "uprising" from the minority but still well-organized Sandinista Front. The Government's control of the apparatus of state power was tenuous at best. The economy was a shambles, with aggregate demand totally out of control resulting in hyper-inflation and production a fraction of its peak of thirteen years before, after seven consecutive years of declining output. Social services, once supposedly the centerpiece of the Sandinista program, were heavily politicized, extremely inefficient because of mismanagement, and seriously underfunded due to the country's economic decline.

Moreover, the country's ability to cope with these problems had been disastrously eroded by the institutional damage brought by the Sandinista years. Large numbers of professionals, skilled workers, and entrepreneurs had either fled or been driven into exile, enriching their countries of destination but disastrously weakening Nicaragua's capacity for recovery. Banks, as financial institutions, had been totally destroyed. Much of the productive sector was in the hands of the state. Worst of all, years of politicization of the economy had eroded the work ethic.

The projected accomplishments of the CDSS period must be seen in light of this dismal starting point. Central to the achievement of any of the CDSS objectives is a beginning of economic recovery. Already, with substantial AID assistance, the GON has achieved a balance of aggregate supply and aggregate demand, although at a level unsustainable in the long run. As a result, inflation has moderated and confidence in the monetary unit has returned. Important progress has already been made with our assistance in reestablishing a financial system, returning state enterprises to private ownership, and restoring competition and market processes throughout the economy.

Over the course of the CDSS period, we anticipate a major transformation of the Nicaraguan economy and society. Although ambitious, nothing less will be sufficient to put Nicaragua on a sustainable growth path and create a society in which democratic values prevail, human rights are respected, and essential social services are available to the overwhelming majority of the population. By the end of this period, the economy will be dominated by the private sector, traditional exports will be growing rapidly, and a variety of non-traditional agricultural exports will be well established. By 1996, enclave manufacturing will have moved beyond an initial concentration in textiles into a wide variety of manufacturing operations. The United States will once again become Nicaragua's principal trading partner. Unfortunately, because of the time it will take to repair the institutional damage caused by the previous regime and restore confidence in the security of property and the rule of law, significant growth in per capita income will only be achieved toward the end of the period.

By the end of the CDSS period, civic education efforts and the spread of a wide range of ideas through the media will have helped achieve general acceptance of democratic ideas, attitudes and values. Such an acceptance of democracy and respect for human rights as the norm will be unique in the history of Nicaragua.

Finally, as a result of slowly but steadily increasing prosperity, and the implementation of key programs and policies, essential social services will be fundamentally transformed. A non-politicized primary educational curriculum and improved teacher training will provide the educated citizenry and trained work force which will extend and deepen the gains made during the CDSS period through the first decade of the next century. A focusing of the public health system's efforts and improvements in its management will continually improve levels of maternal and child health and steadily reduce levels of infant mortality. These improvements in the health and education begun during the CDSS period will, themselves, produce a more productive workforce which will be required as the Nicaraguan economy makes the transition into higher value added activities which will be required in the first decade of the next century.

Thus, during the CDSS period, we will lay the basis for a free, prosperous, and democratic Nicaragua which can realize its full potential in the decade 2000-2010.

RESOURCE TABLE

Objective	FY-90/91	FY-92	FY-93	FY-94	FY-95	FY-96	FY-99
Mortgage from Previous Year:							
TOTAL	541	194	224	224	224	224	224
BROAD-BASED SUSTAINABLE GROWTH							
Increased foreign and domestic investment	455	141	162	167	172	172	172
Policy change	386	123	137	137	137	136	136
Stabilization	236	80	Econ Rec. & Dev I	Econ Rec. & Dev II	Econ Rec. & Dev III	Econ Rec. & Dev IV	40
Financial system reform	117	Food Assistance	17				
Investment promotion	Private Sector Support	Private Sector CIP	Trade & Investment	Private Sector Support	Private Sector Support	Private Sector Support	76
Increased competition in the economy	Private Sector Support (PSS)	Private Sector Support	Trade & Investment	Private Sector Support	Private Sector Support	Private Sector Support	4
Policy liberalization/Privatization	EBR II & M/Fin Dept Support	EBR IV	EBRD I	EBRD II	EBRD III	EBRD IV	30
Privatization	Private Sector Support	Privatization Support	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	15
Credit (managerial currency)	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	1
Technology transfer	Private Ag Services (PaaS)	Private Sector Support	10				
Diversification/market linkages	PAS & PPS	Private Sector Support	4				
Training	Development Training	Development Training	Development Training	Development Training	Development Training	Development Training	4
Increase of participation in the economy	Employ Gen/CARE Title II	Employ Gen/CARE Title II	Employ Gen/CARE Title II	Employ Gen/CARE Title II	Employ Gen/CARE Title II	Employ Gen/CARE Title II	2
Public dialogue	Participation	Participation	Participation	Participation	Participation	Participation	2
Micro-enterprises/will union support	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	4
Improved productive/extractive practices	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	4
Resource policy dialogue	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	4
Institutional strengthening	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	Natural Resources Mgmt	4
Management of protected areas	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	PVO Co-Financing	4
Environmental education	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	Natural Resource Mgmt	4
DEMOCRATIZATION							
Greater consensus on democratic values	35	31	26	23	27	27	27
Civic education	26	31	26	23	27	27	27
Support to key democratic organization	3	5	6	8	10	10	10
Reducing size of government	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	Private Sector Support	12
Support for key government institutions	EBR II (Occup Com)	EBR IV (Occup Com)	EBRD I (Occup Com)	Municipal Govt Project	Judicial Project	Judicial Project	5
Training	Development Training	Development Training	Development Training	Development Training	Development Training	Development Training	5
QUALITY OF LIFE							
Improved quality/efficiency of basic education	32	20	32	32	23	23	23
Improved maternal and child health	12	Basic Education	5				
Improve preventive health	20	Preventive Health	15				
Child survival activities	2	Preventive Health	8				
Primary health care	5	Preventive Health	2				
Increased contraceptive prevalence	12	Preventive Health	2				
OTHER - POAS, OE, Rural Electric, Salesians	19	POAS	POAS	POAS	POAS	POAS	6