

NICARAGUA

1. General trends

Nicaragua's economy put in a favourable macroeconomic performance in 2023. Real gross domestic product (GDP) grew by 4.6%, compared with 3.8% in 2022. The acceleration in economic activity was driven by domestic demand, with the expansion of private consumption and gross fixed capital formation offsetting a decline in exports and public spending. Financial flows to households and the private sector from remittances, wages and financial system credit underpinned the trend in household consumption and private investment and became the main driver of economic growth. Inflation slowed sharply, ending the year at 5.6% (11.6% in 2022), as international prices gradually declined, inflation expectations were anchored by a reduction in the preannounced annual rate of gradual exchange-rate adjustment, subsidies were maintained, and monetary and fiscal policies were prudently managed in a way consistent with the financial balances.

The non-financial public sector recorded a surplus equivalent to 2.7% of GDP after grants (0.7% in 2022), thanks to a sharp contraction in the central government's nominal current expenditure, which translated into reduced employee compensation, goods and services procurement and social benefits. The current account of the balance of payments also recorded a surplus (7.7% of GDP, compared with a deficit of 2.5% in 2022), supported mainly by higher remittances and tourism receipts. The unemployment rate declined only marginally, from 3.5% in 2022 to 3.4% in 2023, despite accelerating economic growth.

The Economic Commission for Latin America and the Caribbean (ECLAC) forecasts economic growth of 3.7% for Nicaragua in 2024, supported by external demand from trading partners within and beyond the region and continued credit facilities for the private sector. This slower economic growth in 2024 is expected to be associated with a drop in domestic demand resulting from lower projected remittance inflows, which showed signs of weakening from late 2023 and over the first few months of 2024. The agricultural and fisheries sectors, which shrank in 2023, will be supported in 2024 and 2025 by a central government programme to revive production activities. On the employment front, the labour market is expected to absorb more workers, given the country's economic growth conditions and macroeconomic stability. ECLAC estimates that Nicaragua's GDP will grow by 3.2% at constant prices in 2025, a situation which will be influenced by demand conditions in the country's main trading partners within the region, slower growth in the United States and other advanced partner economies, and trends in remittances and credit conditions in the financial system.

According to official estimates, inflation is expected to fall within a range of 3.5% to 4.5% by the end of 2024 thanks to the gradual decline of international commodity prices and the anchoring of inflation expectations as the result of a monetary and fiscal policy framework supportive of price stability and the guidance issued by the exchange-rate authority setting the devaluation target at 0% from January 2024. However, there are strong concerns about geopolitical tensions, the disruption of trade routes and the excess of demand over supply, all of which are likely to generate inflationary pressures.

The non-financial public sector balance after grants is projected to be in the range of -1.0% to 0% of GDP in 2024, owing to higher public spending geared towards recovery in strategic economic activities such as agriculture and fisheries. With respect to the current account, a surplus of between 4.5% and 5.5%

of GDP is projected for 2024, potentially underpinned as before by family remittances from Nicaraguans abroad, tourism and international trade, given the favourable trend in the terms of trade.

2. Economic policy

Nicaragua's macroeconomic policy in 2023 was characterized by prudent management of the instruments at its disposal, given the trends in the main domestic and external economic variables.

(a) Fiscal policy

Total non-financial public sector revenue and expenditure declined as a share of GDP in 2023. Revenue fell only moderately, to 31.6% of GDP (32.0% in 2022), owing mainly to a contraction in social contributions; this translated into growth of 3.2% in real terms for the year (6% in 2022). Similarly, growth in total central government revenue decelerated to 4.5% in real terms in 2023 (8.1% in 2022). Net tax revenue held steady at 20.7% of GDP.

Non-financial public sector expenditure as a share of GDP declined proportionally more than revenue, to 24.1% (25.5% in 2022). This contraction was mostly distributed between employee compensation, goods and services procurement and social benefits, and amounted to 1.2% in real terms in 2023 (0.1% in 2022), while the fall in total central government expenditure was even larger, with a change of 9.0% in real terms in 2023 (7.9% in 2022). The non-financial public sector's net acquisition of non-financial assets (equivalent to public sector gross capital formation) declined to 4.8% of GDP in 2023 (6.1% in 2022).

Because non-financial public sector expenditure fell by more than revenue, with both calculated as shares of GDP, it follows that the fiscal policy stance was tight, and the result was a surplus of 2.7% in 2023 (0.7% in 2022). Public debt as a share of GDP also declined, since while the debt stock increased (because of central bank debt issues), higher economic growth offset this, and the process was also helped by a reduction in financing needs due to the favourable balances of the non-financial public sector, including central government. Thus, total public debt declined to 56.6% of GDP in 2023 (60.6% in 2022), with external debt accounting for 47.9 points and domestic debt for the remaining 8.7 points. According to the Central Bank of Nicaragua, debt sustainability analyses indicate that Nicaragua's public debt remains at sustainable levels in the long term, with a moderate risk of stress in the event of shocks.

The fiscal policy stance in 2024 is expected to be expansionary, as indicated above, with a shift from a financial surplus to a deficit of between 1.0% and 0% of GDP. One of the main challenges facing the economic authorities in 2024 is the revival of agricultural, fisheries and aquaculture production. To this end, in May 2024 the government announced the National Production, Consumption and Trade Plan for the period 2024–2025, the objective of which is to achieve more and better production, mainly of agricultural and fisheries goods. The Plan will be coordinated and executed by the institutions of the National System of Production, Consumption and Trade, led by the central bank. At the time of writing, there was no information on budget execution by the non-financial public sector or central government in 2024.

(b) Monetary policy and exchange-rate policy

The benchmark monetary policy rate was kept at 7.0% in 2023 and remained at that level in the first few months of 2024. This was higher than the central bank's estimated natural nominal interest rate of between 6.5% and 6.7%, which would indicate that the central bank's policy stance was restrictive. Open market operations and facilities for placing funds in cash deposits with the central bank were aimed at tapping surplus liquidity in the banking and financial system in 2023. These operations also continued in

the early months of 2024, helping to reduce upward pressures on inflation. In addition, the central bank left the daily and 14-month local currency reserve requirements unchanged at 10% and 15%, respectively.

Short-term lending rates rose from 9.1% (-2.2% in real terms) at the end of 2022 to 12.3% (6.3% in real terms) in December 2023. Deposit rates on one-month deposits increased proportionally less, from 1.5% (-9.0% in real terms) at the end of 2022 to 3.9% (-1.6% in real terms) in December 2023. According to central bank data, the annualized implicit lending rate was 11.9% in December 2023, while the annualized implicit deposit rate was 1.5%, yielding an annualized implicit financial margin in the banking and financial system of 10.4 percentage points, a level projected to change little in the first few months of 2024.

Financial system lending was very buoyant in 2023, supported by increased public deposits, which rose by a nominal 14.5% over the year. Similarly, nominal growth in the banking system credit portfolio had accelerated to 17.5% year-on-year by the end of 2023. Outstanding banking system loans in 2023 were structured as follows: commerce with 38.3%, private consumption (including credit cards) with 23.9%, manufacturing with 12.8%, real estate (including housing) with 12.6% and agriculture and livestock with 11.3%. The financial intermediation activities of the banking and financial system held steady in the early months of 2024. In fact, public deposits posted a year-on-year increase of 14.4% to April 2024, while lending rose sharply, with a 16% increase over the same month the previous year.

Large inflows of foreign exchange, mainly in the form of family remittances from Nicaraguans in the United States, boosted net currency purchases at the central bank's foreign exchange desk in 2023 and continued in the first few months of 2024, leading to the build-up of substantial gross international reserves. Thus, these reserves increased from US\$ 4.404 billion at the end of 2022 to US\$ 5.447 billion at the end of 2023, equivalent to 7.9 months of imports. Thanks to the continued strong inflow of remittances from abroad and the influx of external resources into the non-financial public sector, the central bank's gross international reserves totalled US\$ 5.778 billion in April 2024, equivalent to 8.4 months of imports.

The strong build-up of reserves that thus began in 2023 prompted the exchange-rate authority to reduce the devaluation target of the mini-devaluation regime from 2% to 1% that year. From January 2024, the central bank announced that the mini-devaluation regime would be maintained, but the devaluation target would be reduced to 0%. As a result, the de facto exchange rate remained fixed at 36.6 córdobas to the dollar during the early months of 2024. The exchange-rate authority insisted on retaining the mini-devaluation regime and adjusting it in 2024 should currency market conditions change. In March 2024, the global real exchange-rate index reflected a strong cumulative appreciation of 3% from its 2021 level.

(c) Other policies

On the trade front, in 2023 Nicaragua signed a free trade agreement with China, which will boost trade flows and especially exports to China. The treaty entered into force on 1 January 2024 and is expected to benefit exports of coffee, sugar, fish, shrimp, lobsters, peanuts, rum, leather, coal, timber and automobile wiring harnesses, for example.

3. The main variables

(a) The external sector

Nicaragua's international trade was marked in 2023 by a slowdown in external demand from its main trading partner, the United States, and from the Central American countries, which were likewise affected by the loss of extra regional momentum. Goods exports expanded, albeit at a slowing pace, with

annual growth of 6% in 2023 (13.2% in 2022). Goods imports increased by 3.1% in 2023 (21.8% in 2022), which represented a sharper slowdown than for exports, resulting in a year-on-year reduction of 3.5% in the goods deficit. The combination of this smaller deficit, a reduced services deficit and a current transfers surplus produced a balance-of-payments current account surplus equivalent to 7.7% of GDP, as against a deficit of 2.5% in 2022.

Net secondary balance-of-payments receipts, also known as current transfers (consisting mainly of family remittances), totalled US\$ 4.543 billion in 2023 (US\$ 3.075 billion in 2022), with a large increase in remittances from the United States. This growth was driven by the humanitarian migration status granted in the United States to Nicaraguan nationals for a period of two years. Family remittances continued to increase during the first quarter of 2024, reaching US\$ 1.141 billion (US\$ 1.02 billion in the same quarter of 2023). However, the pace of growth was slower than in previous quarters (11.8% in the first quarter of 2024, compared with 61.3% in the same quarter of 2023). Single-digit growth in remittances is expected by the end of 2024.

The capital account of the balance of payments recorded a surplus of US\$ 59.6 million in 2023, mainly because of the strength of net capital transfers to the general government. The financial account balance showed a creditor position of US\$ 333 million with the rest of the world, made up of accumulated reserve assets worth US\$ 1.014 billion and the other investment account, in the amount of US\$ 717.1 million. Portfolio investment was in deficit by US\$ 199.1 million, and net debt of US\$ 1.199 billion was registered for the direct investment account. Thus, the overall result was net lending to the rest of the world of US\$ 1.441 billion in 2023 (as against net borrowing of US\$ 324 million in 2022).

In particular, gross foreign direct investment inflows, totalled US\$ 2.535 billion in 2023 (US\$ 1.842 billion in 2022), equivalent to an annual change of 37.6%, their destinations being the manufacturing, energy, mining, commerce and service sectors. The terms of trade showed a considerable improvement of 16.5% in 2023 (against a decline of 2.3% in 2022), as a result of higher prices, for agricultural and agro-industrial goods, forming part of the Nicaraguan export basket and lower average import prices, in particular, for petroleum derivatives.

In the first quarter of 2024, Nicaragua's international trade was affected by lower external demand, particularly for goods for processing, with goods exports and imports both registering negative rates of growth. In fact, goods exports were 4.5% lower in the first quarter of 2024 than in the same quarter the previous year, while goods imports also declined, at a year-on-year rate of 1.1%. The goods deficit increased by 26.0% year-on-year. The decline in goods exports and imports was due to the situation of industrial and agro-industrial businesses in free trade zone regimes (mostly textile and automobile harness maquila producers), which recorded fewer imports for processing because of the decline in external demand.

(b) Economic activity

Economic activity in 2023 as measured by quarterly GDP was consistent with the annual measures. The year-on-year rate of growth in the original GDP series accelerated to 6.1% in the third quarter, with an expansion of 5.2% in the fourth quarter (2.3% in the same quarter of 2022). GDP in the first quarter of 2024 reflected year-on-year growth of 3.7% (3.5% in the first quarter of 2023), although this was down on the year-on-year growth of 5.2% in the fourth quarter of 2023.

On the demand side, real annual GDP was strongly driven by domestic demand in 2023, evidenced in a 6.4% increase in household consumption (4.5% in 2022), and in the boost to total investment, which increased by 20% (down by 3% in 2022), offsetting declines in external demand, which fell by 29% (3.5% in 2022), and in government consumption, which contracted by 1.1% (1.3% in 2022). On the supply side,

the most dynamic branches of activity in 2023 were hotels and restaurants with annual growth of 23.3% (29.0% in 2022), mining and quarrying with 12.8% (3.4% in 2022), electricity with 12.7% (1.9% in 2022), construction with 8.1% (down by 12.2% in 2022) and commerce with 7.2% (7.2% in 2022).

The monthly index of economic activity, a high-frequency indicator of production activities, maintained the momentum seen in 2023 with a good performance in the first five months of 2024, albeit with some slackening that may be attributed to the slower pace of economic expansion in the country's main trading partner, the United States, despite an expansion of domestic demand driven by family remittance inflows and credit facilities in the banking and financial system. In fact, the seasonally adjusted monthly index for May 2024 rose by 3.7% year-on-year, a deceleration of 0.8 percentage points from the reading for the same month of 2023 (4.5%). Some of the most dynamic activities were energy and water, hotels and restaurants, construction, transport and communications, financial intermediation, and commerce. Fishing and aquaculture continued to record negative growth rates, and were joined by mining and quarrying, stockbreeding, and other services.

(c) Prices, wages and employment

As regards inflation, the rate of domestic price growth decelerated, as indicated above, to 5.6% in December 2023 (11.6% in 2022). The groups of goods and services with the largest impact on inflation in 2023 were beverages with an annual increase of 14.9%, restaurants and hotels with 10.2%, and food with 7.3%.

Consumer prices continued to rise in the first few months of 2024, albeit at a gradually slackening pace. Year-on-year inflation to June 2024 was 4.8%, which was 5.1 percentage points below the inflation rate in the same month the previous year, but only 0.8 percentage points below the rate at the end of 2023. The goods and services that contributed most to this rate, in order of importance, were food and non-alcoholic beverages, restaurants and hotels, and education. Core inflation, which is determined by excluding goods and services subject to supply shocks, stood at 4.2% in June 2024, seemingly pointing to possible inflation persistence in Nicaragua.

Given that supply factors are excluded from the measurement of core inflation, it is highly likely that the source of inflationary pressures lies in demand outstripping aggregate supply. Unless the central bank further tightens its monetary policy stance, there is a perceived risk that inflation may surpass the target of between 3.5% and 4.5% by the end of 2024.

As for the labour market, the unemployment rate averaged 3.4% in 2023 (3.5% in 2022), being higher for women (3.5%) than for men (3.2%), while affiliation to the social security system showed a small increase of 1.1% in the same year (1.9% in 2022). The branches of production activity that generated the most jobs were the agricultural sector with 27.9%, followed by commerce with 21.5%, services with 19.3% and manufacturing industry with 10.4%. The average annual underemployment rate increased slightly in 2023, to 39.4% (39.0% in 2022). The average labour participation rate also increased slightly in 2023, to 67.3% (66.7% in 2022), with figures of 79.7% for men and 56.5% for women. This rate has yet to return to the pre-pandemic level of more than 70%. The National Minimum Wage Commission increased the nominal minimum wage by 10% from March 2023, except in the industrial branches, which were granted an increase of 8%. These rises and slower inflation in 2023 resulted in real wages growing by 2.7% for workers affiliated with the Nicaraguan Social Security Institute (after falling by 3.6% in 2022) and by 3.7% for central government employees (7.3% in 2022).