Country Report

Nicaragua

Generated on April 23rd 2019

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The Economist Intelligence Unit

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ISSN 2047-5454

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"0 or 0.0" means nil or negligible;"n/a" means not available; "-" means not applicable

Nicaragua

Summary

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Briefing sheet

Editor: **Abhijit Surya**

Forecast Closing Date: **April 5, 2019**

Political and economic outlook

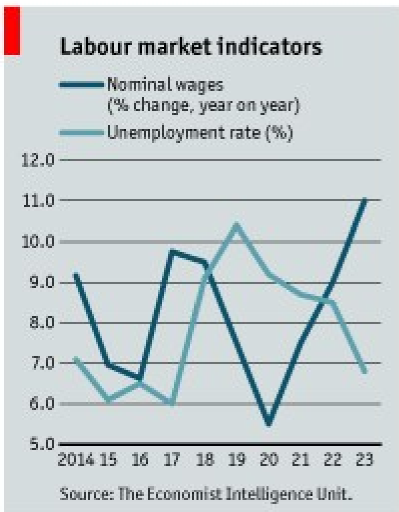
- Political risk remains extremely high. The president, Daniel Ortega, is under increasing pressure from both domestic and international actors to undertake far-reaching political reform and hold early elections (which are officially due in 2021).
- The US government has sanctioned five high-level Nicaraguan public officials, including the vice-president and first lady, Rosario Murillo. There is a high likelihood that additional sanctions will follow, curtailing Nicaragua's access to new multilateral lending.
- Mr Ortega shows no willingness to forge a negotiated resolution to the crisis, as attempts to unseat him have thus far proven unsuccessful. Consequently, The Economist Intelligence Unit expects resistance from the domestic opposition to weaken over time.
- An economic recession, which began as a result of political crisis, will persist in the short term amid extremely high uncertainty.
- Assuming gradual political and economic normalisation, we expect a return to growth in the latter part of our 2019-23 forecast period. However, growth will be well below that of pre-crisis years.
- Recently enacted tax and social security changes will help to contain the widening of the overall fiscal deficit. However, given that these are pro-cyclical reforms, improvements to fiscal accounts will be slow to materialise, keeping the financing requirement high.
- The current account will remain in surplus throughout the forecast period, as extremely weak domestic demand will keep the import bill in check while the secondary income surplus (largely workers' remittances from abroad) continues to grow.

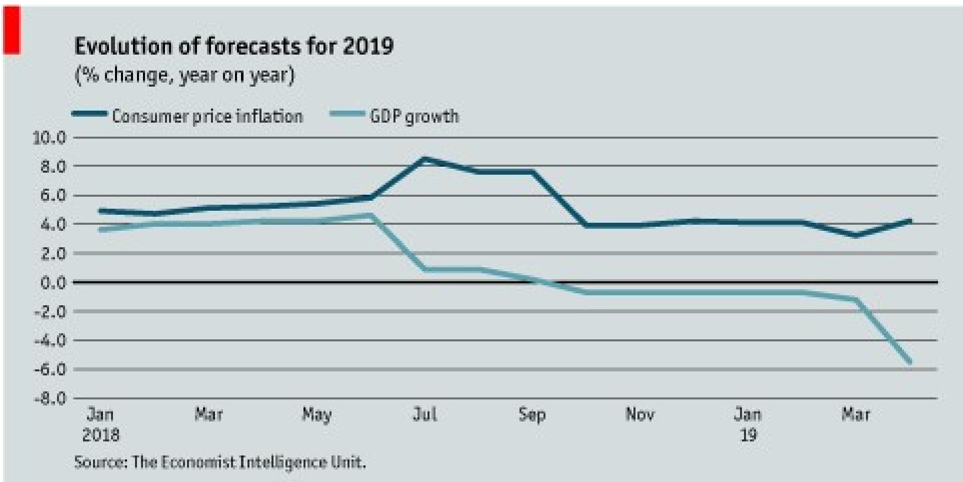
Key indicators

	2018[a]	2019[b]	2020[b]	2021[b]	2022[b]	2023[b]
Real GDP growth (%)	-3.8[c]	-5.5	-2.6	1.3	1.5	2.3
Consumer price inflation (av; %)	4.9[c]	4.2	3.8	4.5	5.5	6.4
Government balance (% of GDP)	-4.1	-3.8	-3.5	-3.2	-3.2	-3.0
Current-account balance (% of GDP)	0.6	4.6	4.4	3.1	2.6	2.2
Money market rate (av; %)	6.7	7.1	6.2	5.3	5.1	4.9
Unemployment rate (%)	9.1	10.4	9.2	8.7	8.5	6.8
Exchange rate C:US$ (av)	31.55[c]	33.19	34.84	36.58	38.41	40.33

[a] Economist Intelligence Unit estimates. [b] Economist Intelligence Unit forecasts. [c] Actual.

Market opportunities





Key changes since February 25th

- The Ortega regime and the domestic opposition restarted political negotiations in March, but as at early-April these have once again stalled. These developments reinforce our view that a political compromise remains a distant prospect.
- We now forecast a much steeper economic contraction in 2019 and 2020, before a return to positive (but still-weak) growth from 2021 onwards, assuming that political normalisation, and by extension economic normalisation, eventually materialises.
- We now expect a steeper GDP contraction of 5.5% in 2019, followed by an additional decline of 2.6% in 2020. Thereafter, we expect weak growth of 1.7% in 2021-23. We previously anticipated a return to growth from 2020.
- The revisions to our outlook stem from our view that, in the absence of a political resolution, consumption and investment will both continue to contract in the short term. Recently enacted pro-cyclical fiscal adjustments will add to the headwinds.

The month ahead

- **TBC—Economic activity, January:** Leading indicators suggest that economic conditions have continued to worsen in January. For instance, imports of consumer goods, intermediate goods and capital goods all declined by double digits in January, suggesting extremely weak domestic demand.

Major risks to our forecast

Scenarios, Q1 2019	Probability	Impact	Intensity
Monetary financing of the fiscal deficit is ramped up considerably, raising inflationary pressures	High	Very high	20
State control over the economy increases	High	Very high	20
The banking sector faces solvency problems	High	Very high	20
The loss of international reserves prompts the imposition of capital controls	High	Very high	20
The opposition successfully calls for an indefinite national strike	High	Very high	20

Note: Scenarios and scores are taken from our Risk Briefing product. Risk scenarios are potential developments that might substantially change the business operating environment over the coming two years. Risk intensity is a product of probability and impact, on a 25-point scale.
Source: The Economist Intelligence Unit.

Outlook for 2019-23

Political stability

Despite Nicaragua's high-risk political environment, amid growing domestic and international opposition, The Economist Intelligence Unit expects the ruling Frente Sandinista de Liberación Nacional (FSLN, the Sandinistas) to remain in power until the end of the term of the current president, Daniel Ortega, in 2022, and beyond. The country is now nearly one year into a political crisis that began in April 2018 amid a public uprising against the perceived undemocratic rule of Mr Ortega and the vice-president, Rosario Murillo (Mr Ortega's wife). The presidential couple have adopted an increasingly authoritarian approach to governance—presidential term limits have been removed and the government exerts strong influence over all public institutions. The FSLN has used its two-thirds legislative majority to strengthen presidential powers as well as the (already strong) state security apparatus.

Leading the movement against the presidential couple is the Alianza Cívica (AC), a coalition of students, peasant farmers, civil society groups and business people, which aims to bring about a democratic transition in the country. Peaceful demonstrations by the AC have been violently put down by pro-government forces (the death toll since April 2018 is in the hundreds), while a number of dissenters have been imprisoned on what international observers deem spurious charges.

The political turmoil has led to a dramatic deterioration in economic conditions, increasing the pressure on the Ortega regime to find a negotiated resolution to the crisis. However, efforts to kick start a political dialogue (first in May 2018, and more recently in March 2019) have repeatedly failed. The latest round of political negotiations initially appeared to be making better progress, with the government committing to releasing political prisoners, restoring legal freedoms to media and non-governmental organisations, and allowing freedom of assembly. However, disagreements on other key issues (including the advancement of general elections due in 2021) led to a new impasse.

In a context in which the opposition holds little in terms of political leverage, and which features a lack of political will on the part of the government to undertake serious democratic reform, we believe that prospects for a political compromise remain distant. Indeed, even though further bouts of political instability remain a distinct possibility, we expect that the opposition's efforts to unseat Mr Ortega will yield no results. Over time we expect domestic resistance to the regime to weaken, and for economic actors to eventually adapt to a new political reality, which should give business a modicum of predictability to increase operations. However, investors are likely to factor in a much weaker recovery in aggregate demand, which means that growth will remain subdued well into the medium term.

Nonetheless, the political scene is highly volatile, and there are substantial risks to our forecast. One of the major vulnerabilities of the Ortega regime is its exposure to US actions. The administration of the US president, Donald Trump, has already sanctioned five high-ranking Nicaraguan officials, including Ms Murillo. More recently, in December 2018 the US Congress approved a renewed version of the Nicaraguan Investment Conditionality Act (NICA Act), which authorises the US government to impose sanctions on Nicaraguans deemed to have committed human rights abuses or acts of corruption. It also instructs US delegates to multilateral institutions to vote against new loans to Nicaragua unless Mr Trump attests that Mr Ortega is making good-faith efforts to restore democracy. However, uncertainty looms about how these sanctions will actually be enforced by the Trump administration, and to what end. Although there appears to be a general call for democratic reform, it is unclear whether the Trump administration envisages Mr Ortega being replaced by someone from the current opposition camp, or if it would accept a reconstituted FSLN government under new leadership.

In the event of a significant escalation in political or economic pressures, Mr Ortega's hold on power will be determined by the role played by the country's security forces. Currently, Mr Ortega exerts significant influence over both the police and the military. The most senior officers in the military have been placated with access to commercial assets and revenue thereof. Meanwhile, the regime has used the active participation of police forces in stamping out political insurrection to cement institutional cohesion and instil fears of retribution should the opposition come to power. Although this has thus far been sufficient to ensure the loyalty of the security forces, there is a high risk of fractures within the regime if economic or political conditions worsen.

Election watch

The next legislative and presidential elections are not due until November 2021. Given the probable lack of a negotiated solution to the ongoing political conflict, we expect that Mr Ortega, or someone he chooses to run in his stead at the next elections, will remain at the helm of the government over the forecast period. Although Mr Ortega may make concessions on electoral reform as a reconciliatory gesture to opposition members and to the international community, these are likely be superficial, as the FSLN would retain control over the Supreme Electoral Council, the judiciary and other key institutions. There is a risk of greater social and economic instability as the next elections draw closer.

International relations

Nicaragua's foreign policy will focus on deepening diplomatic ties with the Bolivarian Alliance (an intergovernmental organisation composed mostly of left-wing governments such as Bolivia, Cuba and Venezuela). However, financial support from those countries is unlikely to be forthcoming. Nicaragua will remain committed to the Dominican Republic-Central America Free-Trade Agreement (DR-CAFTA), of which the US, Nicaragua’s main trade and investment partner, is a signatory. However, tension with the US will be high, owing to that country's increasingly hawkish foreign policy. The US government has already passed the NICA Act, which paves the way for the blocking of new loans from multilateral institutions such as the World Bank and the Inter-American Development Bank, which Nicaragua relies on for concessional lending. If sanctions are duly enforced, we assume that the Nicaraguan government will be able to secure finance from alternative sources, such as the Central American Bank of Economic Integration (CABEI). However, there are serious risks to this assumption given Nicaragua's increasing regional and global isolation.

Policy trends

The government's most pressing priority will be to stem the ongoing economic deterioration, but gaining investor confidence amid political turmoil and lack of faith in the rule of law will prove extremely challenging. Land occupations have been a significant occurrence since the onset of the political crisis—the main agricultural producers' association claims that, as at November 2018, about 3,900 ha of agricultural land remains illegally occupied by pro-government groups. Even so, land grabs have been limited in scope and appear to be aimed at undermining domestic opponents. The risk of expropriation for foreign-owned companies remains limited, as Nicaragua is a signatory to the DR-CAFTA, and the pact provides foreign investors protection from expropriation other than in conformity with customary international law. The Nicaraguan government will not risk its membership to the DR-CAFTA, given Nicaragua's reliance on an export-oriented development model.

A more serious concern for private enterprise will be the fragile state of the financial system. The political crisis in 2018 heightened economic uncertainty and led to large withdrawals of deposits from banks. This in turn led to a throttling of private-sector credit, and prevented businesses from borrowing to carry out productive activity. All the while, continued economic deterioration has led to a worsening of banks' asset portfolios. To stave off serious banking sector problems, the government has enacted regulation to help households and small businesses affected by the political crisis to restructure debt. Banks have also been able to take on short-term debt from abroad in order to address concerns about liquidity. Although financial soundness and profitability indicators are likely to worsen in the short term, there are few signs of a systemic banking crisis and, as such, we do not expect one to materialise.

Fiscal policy

The government will institute measures to contain the non-financial public-sector (NFPS) deficit over the forecast period. The NFPS deficit more than doubled in 2018, to 4.1% of GDP, owing primarily to a steep fall in tax revenues (as formal jobs were hit hard by the knock-on effects of the political crisis) as well as a ballooning deficit in the INSS (the social security system). To address the latter, the Ortega government passed a number of changes to the INSS to make it more financially viable. The government has mandated increases to employee and employer contribution rates to raise revenue, while also considerably reducing the size of pension payments to cut costs. We believe that these measures will help to tide the INSS over the forecast period.

In order to address the issue of lower tax revenues, the government has implemented major changes to the tax code, which involve significant increases to income taxes and value-added taxes (VAT), and as well as excise taxes. However, in the current economic circumstances, pro-cyclical tax measures will only aggravate already-weak consumer and investor sentiment, effectively mitigating the extent to which these tax reforms will help to bring in fresh revenues. Indeed, we expect the NFPS deficit to narrow only slightly over the course of our forecast period, to 3% of GDP by 2023.

However, even a fiscal deficit of this size will be problematic for the government, given its constraints on raising finance. Both international assistance and concessional multilateral lending has been curtailed significantly since the 2018 political crisis. Meanwhile, domestic appetite for government bonds is also at a recent low. We currently expect that the government is likely to increase borrowing from non-concessional sources that do not fall under the scope of US sanctions. In February the government announced that Taiwan's export-import bank had granted Nicaragua a US$100m loan to cover the deficit in the 2019 public investment programme. Similarly, on April 5th the CABEI signed off on more than US$200m in development loans to Nicaragua.

Increased borrowing on non-concessional terms will drive up debt-servicing costs. We currently forecast the public debt/GDP ratio at an average of 65.5% of GDP in 2019-23, (a high level, considering Nicaragua's limited debt-servicing capacity), but risks are tilted towards the accumulation of even greater debt.

Monetary policy

The main objective of the Banco Central de Nicaragua (BCN, the central bank) is exchange-rate stability, which is maintained through a crawling-peg exchange-rate regime, wherein the córdoba is tied to the US dollar with an annual ceiling for depreciation set at 5%. The BCN uses short-term notes to maintain an adequate level of reserves to sustain the crawling peg.

On the lending side, the BCN uses three standing facilities to restrict the volatility of interbank rates. The BCN will seek to keep lending and deposit rates high in the short term, in order to manage liquidity and preserve its reserves position. However, given the weakness of policy transmission channels, we expect deposits to continue to fall in the short term, leading to lower issuance of new credit.

International assumptions

	2018	2019	2020	2021	2022	2023
Economic growth (%)						
US GDP	2.9	2.3	1.5	1.7	2.0	1.8
OECD GDP	2.2	1.8	1.6	1.8	2.0	1.9
World GDP	2.9	2.7	2.5	2.8	2.9	2.8
World trade	4.4	3.3	2.8	3.8	3.9	4.0
Inflation indicators (% unless otherwise indicated)						
US CPI	2.4	2.2	1.4	2.2	2.1	1.8
OECD CPI	2.5	2.3	1.9	2.1	2.2	2.1
Manufactures (measured in US$)	5.1	2.6	3.2	3.4	3.2	3.0
Oil (Brent; US$/b)	71.1	66.0	60.5	69.8	75.6	75.0
Non-oil commodities (measured in US$)	1.8	-2.5	4.5	2.4	1.4	0.8
Financial variables						
US$ 3-month commercial paper rate (av; %)	2.0	2.5	2.2	2.1	2.5	2.9
US$:€ (av)	1.18	1.16	1.22	1.21	1.24	1.24
¥:US$	110.43	110.18	109.12	104.88	100.46	96.08

Economic growth

Nicaragua's economic outlook will be seriously hampered by the consequences of the political crisis throughout our five-year forecast period. The latest data published by the BCN show that the depth of recession in 2018 was significantly greater than what leading indicators suggested. Real GDP contracted by 3.8% year on year in 2018, significantly worse than our initial estimate of a 3% contraction. In the short term, domestic demand will continue on a downward trend. Private consumption will remain in the red owing to high levels of joblessness and stagnation of wages, while investment will fall amid unavailability of credit, weaker business confidence, and greater economic and legal insecurity. On this basis, we forecast a more rapid GDP contraction, of 5.5%, in 2019, followed by an additional 2.6% decline in 2020. Although growth will return thereafter, under our benign assumption that consumers and firms will adjust to a new political and economic reality, GDP per head will not return to pre-crisis levels even by the end of our forecast period in 2023.

On the supply side, the tourism sector will be the worst hit, as the social instability generated by recent events will have all but destroyed Nicaragua's erstwhile reputation as the safest destination in Central America. Commercial activity will also decline significantly, owing to high joblessness levels. Agriculture growth will be dampened by relatively weak prices for agricultural commodities, as well as structural challenges facing the coffee sector. Manufacturing will be supported by foreign investment, particularly in the textiles sector, but the cigar industry will continue to struggle. A downturn in private building activity will keep the contribution from construction subdued. Growth prospects for the mining sector, also a key recipient of foreign investment, have improved slightly, with metal prices beginning to recover and output rising as a result of new gold mining capacity.

Economic growth

%	2018[a]	2019[b]	2020[b]	2021[b]	2022[b]	2023[b]
GDP	-3.8	-5.5	-2.6	1.3	1.5	2.3
Private consumption	-4.8	-5.4	-4.4	0.7	1.2	2.0
Government consumption	-2.8	-2.5	-0.2	4.4	2.0	2.0
Gross fixed investment	-19.7	-26.0	-12.0	1.9	4.0	6.0
Exports of goods & services	-2.6	-5.2	-2.7	2.3	3.4	3.7
Imports of goods & services	-14.0	-12.7	-7.2	4.2	3.5	4.1
Domestic demand	-9.1	-9.4	-4.9	2.3	1.7	2.6
Agriculture	0.5	-2.0	3.4	2.8	3.0	3.0
Industry	-0.9	-2.5	-1.9	1.5	1.8	2.2
Services	-4.7	-6.4	-4.0	1.1	1.4	2.0

[a] Actual. [b] Economist Intelligence Unit forecasts.

Inflation

Price pressures will be relatively subdued early in our forecast period, owing to extremely weak demand-side pressures. However, assuming a gradual improvement in economic conditions, as well as a recovery in oil prices in the latter half of our forecast period, we expect inflation to pick up, reaching 6.5% by end-2023. Commodities prices will act as a key risk to our forecasts, given the share of food and fuel in the overall consumption basket. Similarly, natural disasters will remain an ever-present threat to price stability.

Exchange rates

In line with the BCN's crawling-peg framework, we expect the nominal value of the córdoba to depreciate by 5% annually, from C32.33:US$1 at end-2018 to C41.24:US$1 at end-2023. Although we expect that the BCN will be able to maintain international reserves to support this exchange-rate policy, there are some risks to this forecast. Nicaragua's financial system is highly dollarised and the political crisis has led to a sharp fall in international reserves, from US$3bn in April 2018 to US$2.3bn (providing four months of import cover) at end-2018. A failure to sustain foreign reserves (not our baseline forecast), would impede the sustainability of the crawling peg and force the central bank to devalue the currency.

External sector

The current account will largely mirror movements on the trade balance. We expect the trade deficit be well below that of pre-crisis years, at an average of 7.5% of GDP in 2019-20, owing to depressed import demand and moderate oil prices. This will help to produce an average current-account surplus of 4.5% of GDP in 2019-20. Thereafter, assuming slightly improved economic growth and resurgent oil prices, the current account-surplus will gradually narrow, to 2.2% of GDP in 2023.

The services surplus will remain weak throughout the forecast period, as the tourism sector will take a long time to recover from the damage done by the political crisis. The services surplus will amount to only 1.8% of GDP in 2019-23, down from a peak of 3.8% of GDP in 2017. We expect the primary income deficit to remain broadly stable, at an average of 3.8% of GDP. The secondary income (transfers) surplus—mainly comprised of remittances from workers in the US, Costa Rica and Spain—will remain large at 14.4% of GDP in 2019-23.

Forecast summary

Forecast summary
(% unless otherwise indicated)

	2018[a]	2019[b]	2020[b]	2021[b]	2022[b]	2023[b]
Real GDP growth	-3.8	-5.5	-2.6	1.3	1.5	2.3
Gross fixed investment growth	-19.7	-26.0	-12.0	1.9	4.0	6.0
Unemployment rate (av)	9.1[c]	10.4	9.2	8.7	8.5	6.8
Consumer price inflation (av)	4.9	4.2	3.8	4.5	5.5	6.4
Consumer price inflation (end-period)	3.9	4.5	3.3	5.2	6.1	6.5
Lending interest rate	10.9	12.2	11.4	8.5	8.1	8.1
NFPS fiscal balance (% of GDP)	-4.1[c]	-3.8	-3.5	-3.2	-3.2	-3.0
Exports of goods fob (US$ bn)	4.2[c]	4.1	4.1	4.3	4.6	4.9
Imports of goods fob (US$ bn)	5.8[c]	5.0	5.0	5.4	5.9	6.2
Current-account balance (US$ bn)	0.1[c]	0.6	0.5	0.4	0.3	0.3
Current-account balance (% of GDP)	0.6[c]	4.6	4.4	3.1	2.6	2.2
External debt (year-end; US$ bn)	11.5[c]	11.9	12.3	12.8	13.0	13.1
Exchange rate C:US$ (av)	31.55	33.19	34.84	36.58	38.41	40.33
Exchange rate C:US$ (end-period)	32.33	33.94	35.63	37.41	39.28	41.24
Exchange rate C:€ (end-period)	37.02	40.89	43.29	45.83	48.90	51.34
Exchange rate C:SDR (end-period)	44.94	47.94	50.88	53.64	57.04	59.94

[a] Actual. [b] Economist Intelligence Unit forecasts. [c] Economist Intelligence Unit estimates.

Data and charts

Annual data and forecast

	2014[a]	2015[a]	2016[a]	2017[a]	2018[b]	2019[c]	2020[c]
GDP							
Nominal GDP (US$ m)	11,880	12,757	13,286	13,844	13,118[a]	12,193	11,690
Nominal GDP (C m)	308,402	347,707	380,260	416,013	413,910[a]	404,679	407,346
Real GDP growth (%)	4.8	4.8	4.6	4.7	-3.8[a]	-5.5	-2.6
Expenditure on GDP (% real change)							
Private consumption	4.2	5.2	5.7	5.8	-4.8[a]	-5.4	-4.4
Government consumption	6.0	5.6	8.2	3.8	-2.8[a]	-2.5	-0.2
Gross fixed investment	3.3	17.0	1.4	-0.6	-19.7[a]	-26.0	-12.0
Exports of goods & services	6.4	-1.0	4.6	9.7	-2.6[a]	-5.2	-2.7
Imports of goods & services	3.1	12.0	4.1	3.9	-14.0[a]	-12.7	-7.2
Origin of GDP (% real change)							
Agriculture	2.4	-0.8	4.6	8.5	0.5[a]	-2.0	3.4
Industry	6.5	5.0	3.1	2.8	-0.9[a]	-2.5	-1.9
Services	5.1	5.2	5.4	4.6	-4.7[a]	-6.4	-4.0
Population and income							
Population (m)	6.0	6.1	6.1	6.2	6.3	6.4	6.4
GDP per head (US$ at PPP)	5,041	5,339	5,576	5,855	5,677	5,398	5,312
Fiscal indicators (% of GDP)							
Non-financial public-sector revenue	25.4	26.5	28.2	28.6	27.1	28.3	29.8
Non-financial public-sector expenditure	26.9	28.1	30.1	30.6	31.2	32.1	33.3
Non-financial public sector balance	-1.5	-1.6	-2.0	-2.0	-4.1	-3.8	-3.5
Net public debt	49.0	45.3	44.8	47.0	52.5	60.2	65.7
Prices and financial indicators							
Exchange rate C:US$ (end-period)	26.60	27.93	29.33	30.79	32.33[a]	33.94	35.63
Consumer prices (end-period; %)	6.5	3.1	3.1	5.7	3.9[a]	4.5	3.3
Stock of money M1 (% change)	17.0	21.6	0.2	17.0[b]	15.2	13.0	12.0
Stock of money M2 (% change)	15.7	17.7	-0.2	16.4[b]	13.1	12.0	11.6
Lending interest rate (av; %)	13.5	12.1	11.4	10.8	10.9[a]	12.2	11.4
Current account (US$ m)							
Trade balance	-2,169	-2,545	-2,612	-2,470	-1,633	-921	-877
Goods: exports fob	4,150	3,859	3,772	4,143	4,168	4,079	4,109
Goods: imports fob	-6,319	-6,405	-6,384	-6,613	-5,802	-5,000	-4,986
Services balance	188	232	394	514	414	244	207
Primary income balance	-314	-346	-357	-390	-310	-408	-441
Secondary income balance	1,449	1,514	1,585	1,653	1,611	1,647	1,625
Current-account balance	-845	-1,145	-991	-694	83	561	514
External debt (US$ m)							
Debt stock	10,079	10,489	10,982	11,457	11,480	11,897	12,293
Debt service paid	700	792	829	1,139	1,391	1,502	1,243
Principal repayments	535	593	605	869	1,087	1,178	939
Interest	165	199	225	270	304	325	304
International reserves (US$ m)							
Total international reserves	2,276	2,492	2,448	2,758	2,261	2,035	2,015

[a] Actual. [b] Economist Intelligence Unit estimates. [c] Economist Intelligence Unit forecasts.
Source: IMF, International Financial Statistics.

Quarterly data

	2017			2018				2019
	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr
Non-financial public sector balance (C m)								
Revenue & grants	28,488	27,547	29,399	n/a	n/a	n/a	n/a	n/a
Expenditure & net lending	29,606	28,947	37,403	n/a	n/a	n/a	n/a	n/a
Balance	-1,117	-1,400	-8,004	n/a	n/a	n/a	n/a	n/a
Wages and prices								
Wages (C per month)								
Arable & livestock	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Construction	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Public sector (govt employees)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Consumer prices (av; 1994=100)	203.5	204.6	208.6	212.0	214.1	215.0	217.9	n/a
Consumer prices (% change, year on year)	3.1	3.6	5.1	5.0	5.3	5.1	4.5	n/a
Financial indicators								
Exchange rate C:US$ (av)	29.86	30.23	30.60	30.98	31.36	31.74	32.13	32.53
Exchange rate C:US$ (end-period)	30.04	30.42	30.79	31.16	31.55	31.94	32.33	32.71
Deposit rate (av; %)	1.2	1.0	1.6	n/a	n/a	n/a	n/a	n/a
Lending rate (av; %)	12.5	9.6	10.2	n/a	n/a	n/a	n/a	n/a
M1 (end-period; C bn)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M1 (% change, year on year)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (end-period; C bn)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (% change, year on year)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Foreign trade (US$ m)								
Exports fob	715.3	591.8	500.7	n/a	n/a	n/a	n/a	n/a
Coffee	202.7	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Imports cif	-1,377.9	-1,399.9	-1,558.9	n/a	n/a	n/a	n/a	n/a
Trade balance	-662.7	-808.1	-1,058.2	n/a	n/a	n/a	n/a	n/a
Foreign payments (US$ m)								
Merchandise trade balance	-536.3	-620.8	-898.2	-447.8	-462.6	-239.9	n/a	n/a
Services balance	160.9	122.9	110.5	173.0	86.8	64.4	n/a	n/a
Primary income balance	-110.8	-92.9	-100.6	-95.2	-60.9	-45.6	n/a	n/a
Net transfer payments	390.7	435.6	443.2	403.4	426.2	412.8	n/a	n/a
Current-account balance	-95.5	-155.2	-445.1	33.4	-10.5	191.7	n/a	n/a
Reserves excl gold (end-period)	2,573.1	2,542.6	2,757.8	2,891.7	2,654.2	2,301.6	2,261.1	n/a

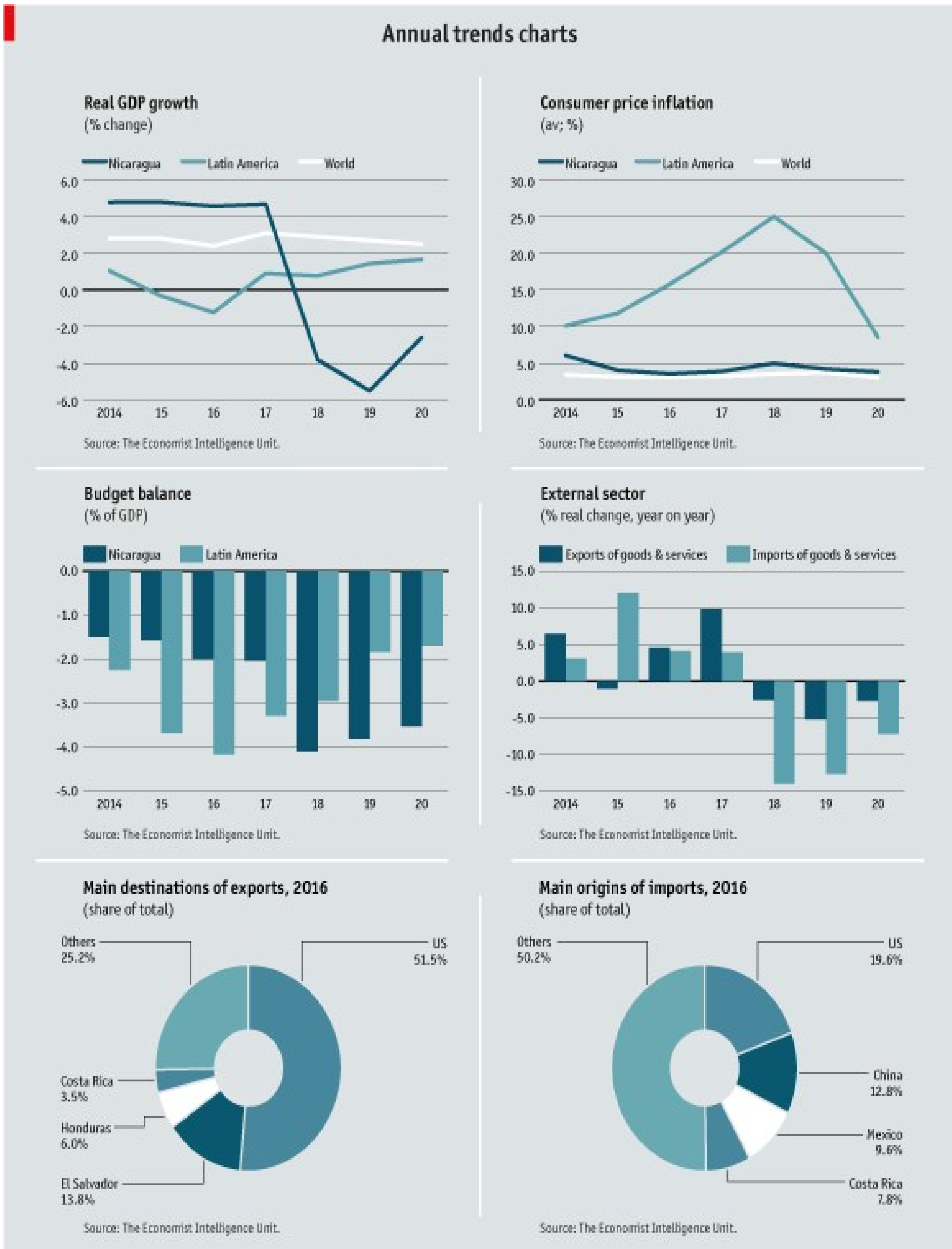
Sources: Banco Central de Nicaragua; IMF, International Financial Statistics.

Monthly data

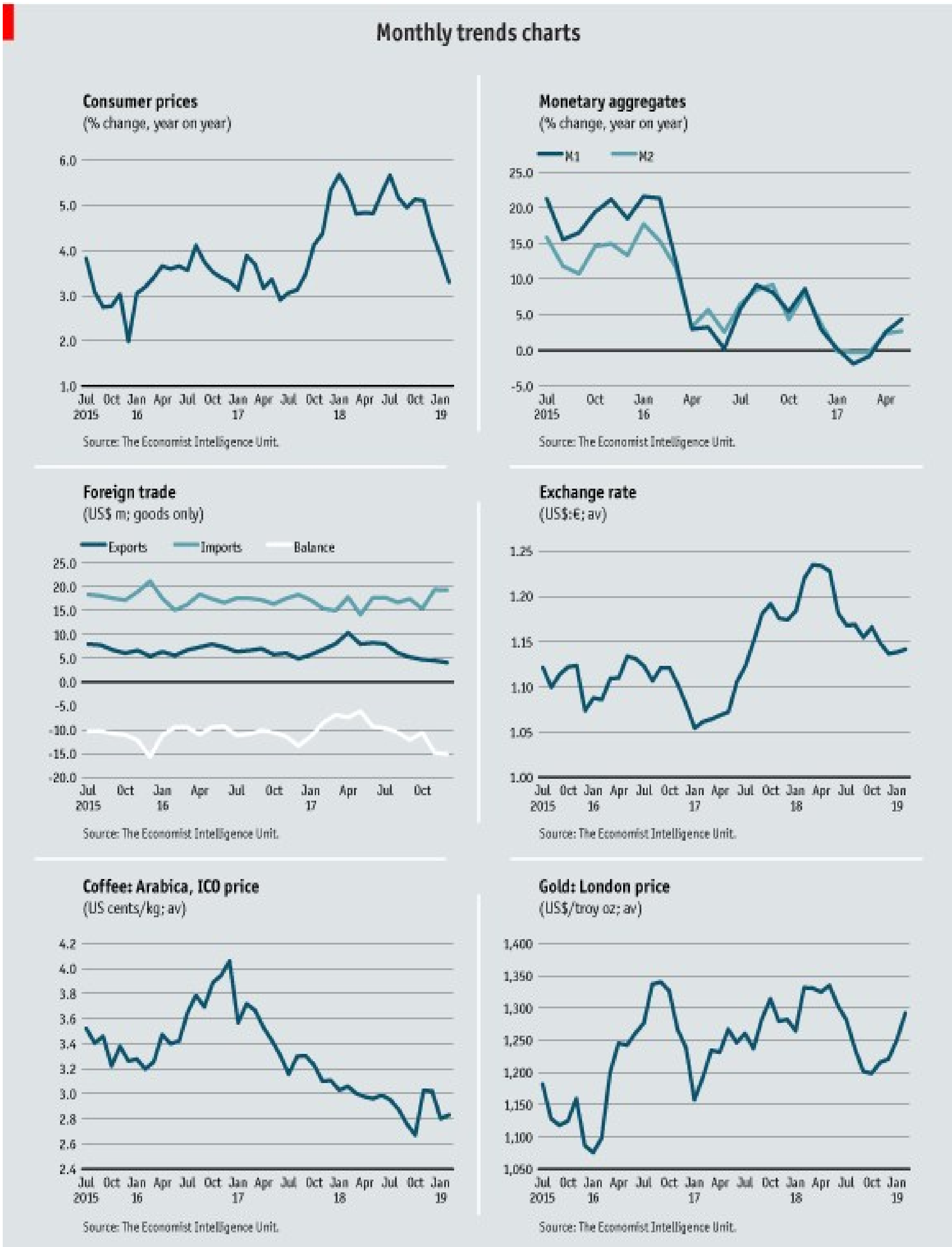
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Exchange rate C:US$ (av)												
2017	29.39	29.50	29.62	29.74	29.86	29.98	30.11	30.23	30.36	30.48	30.60	30.73
2018	30.86	30.98	31.10	31.23	31.36	31.48	31.61	31.74	31.87	32.00	32.13	32.27
2019	32.40	32.53	32.66	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Exchange rate C:US$ (end-period)												
2017	29.45	29.56	29.68	29.80	29.92	30.04	30.17	30.29	30.42	30.54	30.66	30.79
2018	30.92	31.03	31.16	31.29	31.42	31.55	31.68	31.81	31.94	32.07	32.20	32.33
2019	32.46	32.59	32.71	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M1 (% change, year on year)												
2017	-1.9	-0.8	2.6	4.4	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2018	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2019	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (% change, year on year)												
2017	-0.3	-0.3	2.4	2.7	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2018	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2019	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Deposit rate (av; %)												
2017	1.3	1.1	1.1	1.0	1.3	1.3	0.7	0.6	1.8	3.2	0.6	1.2
2018	2.6	0.5	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2019	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Lending rate (av; %)												
2017	10.6	12.0	9.9	13.1	12.1	12.3	10.2	10.7	7.9	8.3	10.5	11.8
2018	12.9	8.5	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2019	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Consumer prices (av; % change, year on year)												
2017	3.9	3.7	3.2	3.4	2.9	3.1	3.1	3.5	4.1	4.4	5.3	5.7
2018	5.4	4.8	4.8	4.8	5.3	5.7	5.2	5.0	5.1	5.1	4.4	3.9
2019	3.3	3.4	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Foreign-exchange reserves excl gold (US$ m)												
2017	2,459.8	2,433.1	2,462.4	2,500.0	2,554.1	2,573.1	2,624.1	2,570.7	2,542.6	2,598.0	2,703.4	2,757.8
2018	2,782.4	2,813.2	2,891.7	2,970.2	2,902.3	2,654.2	2,496.3	2,446.7	2,301.6	2,260.1	2,250.6	2,261.1
2019	2,179.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a

Sources: Banco Central de Nicaragua; IMF, International Financial Statistics; Haver Analytics.

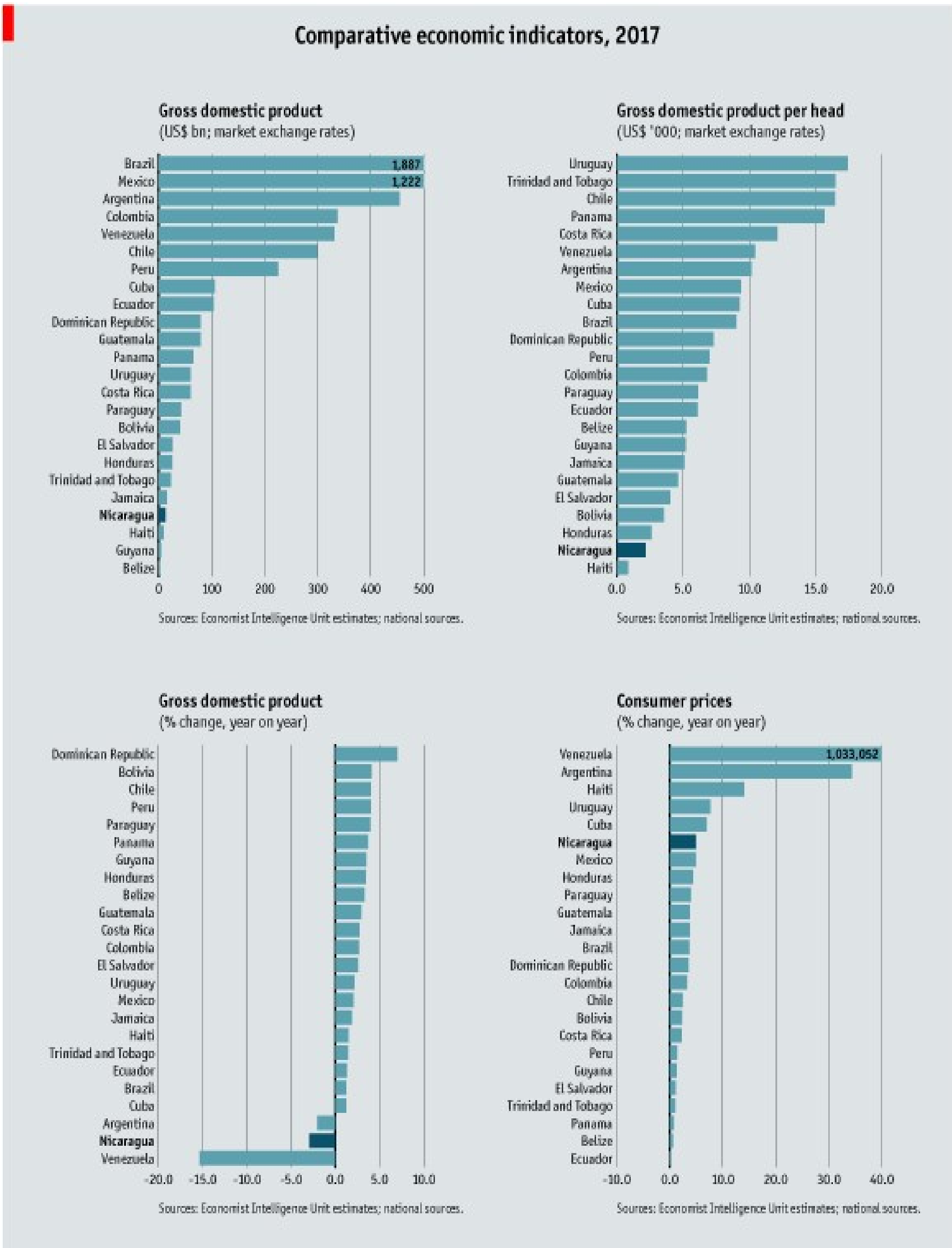
Annual trends charts



Monthly trends charts



Comparative economic indicators



Basic data

Land area

121,428 sq km; mountainous upland in the central area, with a wide plain on the western coast and tropical forest on the eastern coast

Population

6.2m (mid-2014 official estimate)

Main towns

Population in ’000 (2012 official estimate)

Managua (capital): 1,448

Matagalpa: 542

Chinandega: 423

León: 404

Masaya: 348

Nueva Segovia: 243

Estelí: 221

Climate

Semi-tropical; tropical rainforest on the Atlantic coast

Weather in Managua (altitude 83 metres)

Hottest month, May, 27-32°C (average daily minimum and maximum); coldest month, January, 23-30°C; driest month, January; wettest month, October

Languages

The official language is Spanish. Miskito, Mayangna, Garífuna and English are spoken on the Atlantic coast

Measures

Metric system, but imperial measures are in popular use. Other measures include:

Quintal = 46 kg

Manzana = 0.7 ha

Currency

Córdoba (C); average exchange rate in 2017: C30.1:US$1

Time

6 hours behind GMT

Public holidays

January 1st (New Year’s Day); April 18th (Maundy Thursday); April 19th (Good Friday); May 1st (Labour Day); July 19th (Sandinista Revolution Day); September 14th (Battle of San Jacinto); September 15th (Independence Day); December 8th (Immaculate Conception); December 25th (Christmas Day)

Political structure

Official name

Republic of Nicaragua

Form of state

Presidential democracy, with National Assembly

The executive

The president is head of state, head of government and commander-in-chief of the armed forces. He or she is elected for a period of five years and appoints a cabinet

National legislature

National Assembly: a 92-member unicameral legislature, elected by proportional representation for five years

Legal system

Supreme Court, at the apex of a subordinate court system, elected by the National Assembly for five years

National elections

Last elections: November 6th 2016 (presidential and National Assembly). Next elections: November 2021

National government

The president, Daniel Ortega Saavedra, governs with the support of the Frente Sandinista de

Liberación Nacional (FSLN, the Sandinistas)

Main political organisations

Government: FSLN

Opposition: Partido Liberal Constitucionalista (PLC); Partido Liberal Independiente (PLI); Alianza Liberal Nicaragüense (ALN, formed by ex-PLC members); Movimiento Renovador Sandinista (MRS, formed by ex-FSLN members)

Key ministers

President: Daniel Ortega Saavedra

Vice-president: Rosario Murillo

Agriculture: Edward Francisco Centeno

Defence: Martha Elena Ruiz Sevilla

Development, industry & commerce: Orlando Solórzano

Economy, family & community: Justa Pérez Acuña

Education, culture & Sports: Miriam Soledad Ráudez

Environment & natural resources: María José Corea Pérez

Family: Johana Vanessa Flores Jiménez

Finance & public credit: Iván Acosta

Foreign affairs: Denis Moncada Colindres

Health: Sonia Castro González

Interior: María Amelia Coronel Kinloch

Labour: Alba Luz Torres Briones

Mines & energy: Salvador Mansell Castrillo

Transport & infrastructure: Óscar Salvador Mojica Obregón

Central bank president

Leonardo Reyes Ramírez

Recent analysis

Generated on April 23rd 2019

The following articles have been written in response to events occurring since our most recent forecast was released, and indicate how we expect these events to affect our next forecast.

Politics

Forecast updates

US announces new sanctions on Venezuela, Cuba and Nicaragua

April 18, 2019: International relations

Event

At an event in Miami on April 17th the US national security advisor, John Bolton, announced new sanctions on the governments of Venezuela, Cuba and Nicaragua.

Analysis

The sanctions on Venezuela are meant to prod the Venezuelan president, Nicolás Maduro, to leave power in favour of the self-proclaimed interim president and president of the Venezuelan National Assembly, Juan Guaidó, who is recognised as the legitimate Venezuelan president by the US and 54 other (mainly Western) countries. Sanctions on Cuba and Nicaragua are to punish those governments for their support of and aid to the Maduro regime.

On Venezuela, the new sanctions target the Banco Central de Venezuela (BCV, the Central Bank). The US government will restrict the BCV's access to the US financial system and use of US dollars in a bid to cut off a funding source for the Venezuelan government. New sanctions on Nicaragua were likewise financial, with Mr Bolton saying the US will levy new penalties against Bancorp, Nicaragua's largest bank, which already faces US sanctions for its ties to the Venezuelan state oil company, PDVSA. Mr Bolton called Bancorp a "slush fund" for the president, Daniel Ortega. The US government will also blacklist Laureano Ortega, Mr Ortega's son, claiming he is being groomed as the successor to his father. Given existing sanctions against both countries, however, the real disruption is likely to be minimal.

The harshest penalties—and those likely to have the most impact, were on Cuba. Mr Bolton said the government would restrict all travel by US citizens to the country except for family visits. He also said the administration would limit the amount of remittances Cubans could send to the island (currently unlimited) to US$1,000 every three months. Most significantly, the administration announced earlier in the day that it would allow Title III of the 1996 Helms-Burton Act to come into effect.

The announcement, with Mr Bolton vowing in his speech to rid the hemisphere and the US of communism and socialism, was aimed at domestic US consumption ahead of the 2020 election, and securing the votes of the conservative-leaning Cuban-, Venezuelan-, and Nicaraguan-American communities in south Florida. Still, it shows a continued shift, particularly in US policy towards Cuba, to a focus on regime change.

Impact on the forecast

Given existing sanctions on Nicaragua and Venezuela, we expect the effect of new sanctions to be minimal. We will be revising downwards our real GDP forecast for Cuba for 2019-20.

Analysis

Political dialogue suspended yet again

April 16, 2019

Contrary to the hopes of both parties involved, the political dialogue between the government of the president, Daniel Ortega, and the opposition Alianza Cívica (AC), aimed at finding a solution to Nicaragua's long-festering conflict, ran aground on April 3rd. In an atmosphere of severe polarisation and extreme distrust between the parties, neither side now appears able to make the concessions necessary to negotiate a solution to the crisis. A different process may soon replace the dialogue begun on February 28th, but this is also unlikely to bear fruit.

At the insistence of the AC, the dialogue tried to broach four issues in sequential fashion. On March 29th, the two parties reached framework accords on the release of political prisoners and the restoration of public liberties. However, progress halted when they tried to address issues such as justice for the victims of repression; electoral reform and bringing forwards the presidential vote currently scheduled for 2021. Here, both parties drew red lines in the sand. After insisting on incorporating international human rights bodies as guarantors of the prisoners' release, the AC went on to demand the institutionalisation of an international truth commission to investigate alleged government crimes, as well as an early ballot. However, Mr Ortega and his vice-president, Rosario Murillo (also Mr Ortega's wife), categorically rejected all of these demands.

Talks were "suspended" but resumption is doubtful

In an April 5th report to the Permanent Council of the Organisation of the American States (OAS), Luis Rosadilla, a witness and mediator for the regional body, referred to the suspension of the talks as a "pause for reflection". In fact, the two sides had expressed a willingness to develop the accords already reached, and have been meeting with the International Committee of the Red Cross to reconcile lists of political prisoners as part of the preparations for their eventual release.

Barriers to any further progress in the dialogue are nonetheless formidable. One is acute mutual distrust. Most opposition leaders believe the Ortegas are only playing for time, not bargaining in good faith and the AC firmly insists that it will not negotiate the rest of the agenda unless the government demonstrates a willingness to implement the agreements already reached. In a similar vein, it is very likely that the Ortegas look upon the AC as a spearhead for efforts by the international community (particularly the US) to unseat them, and doubt the sincerity of their opponents' intentions.

Both sides also face severe constraints on their ability to make concessions. Judging from their recent actions, AC delegates have found it difficult to resist pressure from wider opposition forces and the international community to achieve immediate prisoner release and restoration of the right to protest in the streets. These measures are threatening to the Ortegas, whose tight political control of the country is vulnerable if police and paramilitary forces, which have engaged in widespread repression, come to feel that their leaders are caving in to opposition demands that will expose them to legal retribution down the line. The Ortegas agreed in principle to some opposition demands on March 29th, but subsequently stalled their implementation, leading the AC to accuse them of hypocrisy.

Is there a viable basis for settling the conflict?

Given the extreme secrecy in which they operate, it is impossible to know whether Mr Ortega and Ms Murillo are genuinely committed to negotiating a solution to Nicaragua's crisis, especially if it means they must give up power. Indeed, the decision to reopen a political dialogue in February came at a time when the administration of the US president, Donald Trump, had begun its maximum-pressure campaign against the Ortegas' Venezuelan ally, Nicolás Maduro. However, the inability of the Venezuelan opposition leader, Juan Guaidó to score a quick victory over Mr Maduro appears to have led the Ortegas to dig in their heels and strengthen their ties with Venezuela and Cuba, rather than negotiate with the AC in good faith.

Indeed, the Ortegas seem to be moving in a direction that would not allow a political compromise to gel. On April 11th, a deputy of the ruling Frente Sandinista de Liberación Nacional (FSLN, the Sandinistas) proclaimed that the government would not countenance opposition demands for a complete overhaul of the Consejo Supremo Electoral (CSE, the electoral authority) after some of its members saw their mandates expire the day before. Replacing the existing cohort of government loyalists with professional, non-partisan magistrates is regarded as an indispensable step in making any new election credible.

In addition, signs have emerged that the government may soon transfer the whole dialogue process to the National Assembly and negotiate electoral changes of some sort with the minor political parties (whose opposition is largely nominal) represented there, excluding the AC from any further role. A bifurcated negotiating process could then ensue, with the government continuing to talk with the AC about implementing the two initial accords, while issues of justice and reparations for the victims of repression fall through the cracks.

It remains to be seen whether the OAS, which has already been invited to offer technical assistance to the electoral reform process, would play along with such a gambit, and whether any ensuing reforms would satisfy other international players that a genuinely democratic election was in preparation, but it does not seem very likely. The same question can be asked about local business people, who have staunchly supported the AC to date, but are increasingly anxious about what they see as an imminent collapse of Nicaragua's economy.

Sanctions are on the horizon

When the dialogue broke down on April 3rd, some observers believed that hardliners in the Trump administration would quickly clobber Nicaragua with economic and financial sanctions as tough as those already being applied to Venezuela. However, with many US foreign policy resources being devoted to the Venezuelan crisis, there has been less of a focus on Nicaragua, relieving some pressure on the Ortegas. Nonetheless, The Economist Intelligence Unit believe that this situation is temporary and that the respite will be brief.

With no credible political solution in sight, fresh sanctions against the Ortega regime are now likely in relatively short order, both from the US and the EU, although they will initially be targeted at individuals. Sanctions measures could accelerate and deepen, however, in the event that frustration in the camp of the wider Unidad Nacional Azul y Blanco (UNAB, which brings together the AC and a number of other civil society and political groupings) boils over into significant protest and sparks a new round of repression.

In summation, we continue to view the prospects for any kind of negotiated solution of Nicaragua's conflict as tenuous, given the entrenched positions both of domestic and international actors. The absence of a negotiated solution will retain the political status quo, as the Ortega regime continues to control all the levers of power. We currently assume that, as efforts to effect regime change yield no results, the opposition will gradually wear out, which will allow for a process of political normalisation—and by extension economic normalisation—in the medium term. However, risks to our forecast are high, and we cannot definitively rule out the descent of Nicaragua into a Venezuela-style quagmire.

Economy

Forecast updates

Construction activity plummets in Q4 2018

April 8, 2019: Economic growth

Event

Private-sector construction activity (as measured by the area of buildings under construction) fell by half in year-on-year terms in the fourth quarter of 2018, and by 21% in the year as a whole, according to data from the Banco Central de Nicaragua (the central bank).

Analysis

The year-on-year decline in fourth-quarter construction came on the heels of a 14% downturn in the third quarter of 2018. The decline in fourth-quarter building was the steepest recorded during the year and occurred across the country and across all sectors of activity. The consistency in the data indicates that the ongoing political crisis and post-April recession had by this point had a mammoth and sustained impact on building of all types.

The fourth-quarter statistics include a 44% year-on-year fall in residential building, which is the biggest component of construction activity. The decline was largest in the capital, Managua, where area under construction dropped by 60%; residential building in the rest of the country fell by 26%. Overall, the number of new housing starts decreased by 38% and the area planned for construction declined by 32%. Aggravating the trend, area in low cost housing developments slumped despite housing law reforms that have eased the rules for financing social housing.

In the services sector, second in importance to housing, building declined by 52% during the quarter, reflecting the depth of services contraction during that period. Similarly, construction of commercial locales nosedived as both wholesale and retail trade were adversely effected by extremely poor conditions for consumers. Finally, industrial building declined by a massive 82% as non-free-trade-zone manufacturing activity was adversely effected by weak investor confidence.

Whereas the third-quarter data displayed ups and downs, the severe and across the board contraction in fourth-quarter construction likely suggests that projects initiated before the April 2018 political crisis hit have now been finished, and that new ones have not arisen to take their place owing to a steep fall in demand and a decline in the availability of financing for building of all types.

Impact on the forecast

The new construction data came in well below our economic estimates for 2018. We will be making a significant downward revision to our forecast for a 1.2% contraction in real GDP growth in 2019. This owes in part to our view that investment, and by extension construction activity, will be slower to recover than we had previously anticipated.

NFPS deficit widens sharply owing to political crisis

April 9, 2019: Fiscal policy outlook

Event

According to the annual report of the Banco Central de Nicaragua (BCN, the central bank), the deficit after grants of the non-financial public sector (NFPS) widened to 4.1% of GDP in 2018, up from 2% of GDP at end-2017.

Analysis

2018 was a turbulent year for Nicaragua's public finances as political conflict caused a major revenue shortfall, sharp cuts in public investment spending and large losses in the social security administration due to rising unemployment, to cite the most important trends.

The NFPS deficit (4.1% of GDP) reflected a total revenue decline of 4.3% compared with end-2017, and a 3.4% increase in total spending. The central government deficit grew to 2% of GDP, from 0.6% of GDP in 2017, owing largely to a steep fall in tax receipts. Even though public capital spending fell by 2.3%—as some projects were disrupted or left without expected foreign financing—overall central government spending rose slightly, by 0.6%.

After the central government, the largest addition to this deficit came from the social security system, whose imbalances doubled over the previous year owing to the loss of 157,923 affiliated workers (most of whom were self-employed). The social security system deficit rose to 1.1% of GDP, compared with 0.6% of GDP in 2017. Rounding out the picture, Nicaragua's few public enterprises, which include state-run water and electricity companies, added another 1% of GDP to the deficit (0.8% in 2017).

Financing of the NFPS deficit proved very challenging given that net external loans—on which Nicaragua is heavily reliant—fell by a nominal 40.5% in 2018 as several multilateral donors curtailed their disbursements because of the crisis. The government thus had to resort to internal sources of financing to the tune of 2% of GDP to cover the shortfall. Although the Ministry of Finance tried to sell massive new quantities of Treasury bonds as well as other debt instruments, it found virtually no market for its issuance. Funding was thus found by drawing down public-sector deposits with the central bank and by issuing various types of short-term BCN notes.

Impact on the forecast

The new data exceeded our estimate for the NFPS deficit in 2018, and we will adjust our forecasts to show slightly wider fiscal deficits than previously anticipated. However, on the basis of recent reforms to the social security system and to the tax code, we maintain our view that the NFPS deficit will gradually narrow modestly over the forecast period (2019-23).

Consumer prices tick up in February

April 9, 2019: Inflation

Event

According to the Banco Central de Nicaragua (the central bank), the consumer price index (CPI) rose by 0.3% month on month. This lifted annual inflation slightly to 3.4% in February, up from 3.3% in January.

Analysis

The monthly increase in the CPI was driven especially by a 3.9% month-on-month rise in education prices. With February being a back-to-school month for Nicaraguan children, school fees shot up at all levels—pre-school, primary and secondary—at rates of 7-8% year on year in each case. This variable alone contributed to more than three-fourths of the overall CPI increase; however, this is a one-off effect.

The other major component of the CPI to rise, as a result of supply-side pressures, was transportation, which increased by 1.4% month on month. This price rise reflected trends in crude oil prices in the global markets, which rebounded slightly in February 2019 after weak oil prices in the preceding few months. Local prices for gasoline and diesel rose by 4% and 5.1% respectively.

A third category contributing to a higher CPI was furniture and home supplies, whose prices rose by 0.7% month on month. A fourth supply-side effect went in the opposite direction, with food prices falling for the second consecutive month. Although new output data have not been published, this suggests that local supplies have remained sufficient and that prices of imported foodstuffs continue to be low, as had been the pattern in 2018.

With the economy struggling to recover from the political crisis, demand-side pressures remained weak. Prices in the recreation and entertainment sector fell by 4.3% month on month, as declining incomes meant that consumers directed most of their purchases towards basic necessities. Hotel and restaurant prices remained stable month on month; business operators in the tourism industry have cut prices to attract local customers, as high-spending foreign visitors have stayed away since the onset of the political crisis.

Impact on the forecast

Price trends in early 2019 are in line with our forecast, which is for demand-side pressures to remain subdued as the economy goes on contracting, and for supply-side pressures to come mainly from foodstuffs and imported fuels.

Analysis

Real GDP nosedives in 2018

April 8, 2019

The latest data published by the Banco Central de Nicaragua (BCN, the central bank) show the extent of the recession last year, induced by the political crisis that sparked in April 2018. In the fourth quarter of 2018 real GDP contracted by a whopping 2.2% in seasonally adjusted quarter-on-quarter terms. As a result, the real GDP contraction in 2018 was much worse than previously estimated, at 3.8% for the full year. The collapse in investment—the largest driver of the economic deterioration—will prove extremely challenging to remedy in the absence of some form of political resolution. With prospects for the latter remaining distant, The Economist Intelligence Unit will make significant downward revisions to its economic forecasts for the 2019-23 forecast period.

The deep economic contraction in 2018 effectively reversed a lot of the benefits of strong economic growth in recent years. Indeed, in per-head terms, the BCN estimates that disposable income has effectively fallen to 2015 levels. On the expenditure side, this contraction can largely be explained by a collapse in domestic demand.

Real GDP by expenditure

(% change, year on year)

	2018				
	Q1	Q2	Q3	Q4	Full year
Private consumption	3.3	-5.8	-6.6	-9.7	-4.8
Government consumption	-6.5	1.7	-3.1	-2.8	-2.8
Gross fixed investment, of which:	-5.4	-17.3	-29.1	-26.7	-19.7
Private investment	-6.5	-13.7	-35.7	-29.5	-21.4
Public investment	-2.7	-32.7	-4.7	-19.9	-15.4
Exports of goods & services	7.0	-7.2	-3.7	-6.9	-2.6
Imports of goods & services	3.0	-6.6	-24.7	-25.6	-14.0
GDP	**2.4**	**-5.2**	**-4.4**	**-7.7**	**-3.8**

Source: Banco Central de Nicaragua.

The sharp decline in investment is related to a number of factors. The political crisis that began in April 2018 had a strongly negative impact on investor sentiment and on confidence in the rule of law. The crisis also weakened faith in financial institutions, leading to a massive drawdown of deposits (of close to 21%). The reduction in banks' asset bases in turn led to a throttling of credit to the non-financial private sector, which meant that businesses could not borrow the capital that they required to carry out investment activity in the majority of sectors. The period also had a direct impact on infrastructure, owing to damage done to property in the months since April 2018. According to a study conducted by the BCN and the Ministry of Finance, the value of the loss of infrastructure amounted to nearly US$205m (1.6% of GDP).

The decline in investment had knock-on effects on the labour market and on consumer conditions more broadly. According to the national statistics institute, unemployment rose to 6.2% in the third quarter of 2018 (latest available data), up significantly from 3.6% in the year-earlier period. Moreover, this statistic likely understates the depth of labour market deterioration, as it masks a decline in the labour force participation rate (which was itself down by three percentage points). Formal sector employment was the worst hit, as evidenced by a 11% fall in contributors to the social security system.

Tax reform creates new problems

The hit to formal sector activity was a major reason for a decline in government revenues in 2018, which ultimately pushed the government to undertake a slew of pro-cyclical fiscal reforms. Changes to the value-added tax (VAT) regime will lift production costs in many sectors, a significant portion of which are likely to be passed on by businesses to consumers. These higher prices, at a time of stagnant wages and rising unemployment, will only serve to further impede private consumption.

For the private sector, however, the most contentious issues are the income tax measures, which centre on raising a current 1% income tax retention on total sales to 2% for medium-sized businesses and 3% for large companies. Under the current scheme, retained income in excess of eventual tax obligations is supposed to be returned to its owners, but in practice it seldom is. Furthermore, the new income tax rules come on the heels of a steep rise in employer social security contributions. We expect that the passage of pro-cyclical tax reform will sustain the ongoing decline in fixed investment, which in turn will detrimentally affect both employment and consumption in the short to medium term.

Prospects for a recovery have deteriorated

The outlook for the external sector has also worsened. In 2018 net external demand made a positive contribution to real GDP growth by virtue of the fact that the decline in real imports was much stronger than the fall in real exports. Although this trend is likely to persist in 2019, the decline in exports is likely to be larger than we previously anticipated, leading to a smaller overall contribution from net external demand. Indeed, according to preliminary data from Cetrex, the exports processing centre, export volumes fell by 18% year on year in January-March 2019.

Taken together, the latest data warrant significant downward revisions to our economic forecasts for Nicaragua. We had previously anticipated that the economic contraction would bottom out in

2019, before a return to positive, albeit tepid, growth in 2020. However, in the light of the passage of pro-cyclical tax reform, as well as the inability of the government and the domestic opposition to forge a political compromise, we now expect that economic and political normalisation will take much longer to materialise. Consequently, it is now likely that the Nicaraguan economy will experience a protracted recession, through 2019 and 2020, before a weak recovery begins to emerge in 2021, and we will adjust our forecasts to reflect this view.

EIU global forecast - Global economy continues to slow

April 17, 2019

The Economist Intelligence Unit has long been expecting a slowdown in global growth in 2019-20. This trend is now clear in the world's biggest economies. In China, growth is slowing as a result of both external factors, related to the trade war, and domestic factors, as financial de-risking efforts weigh on demand. Both factors are at play in softening industrial production, which recorded its lowest growth rate since 2002 as it grew by 5.3% year on year in January-February. Policymakers will continue to support the economy with monetary and fiscal stimulus, which will help to avoid a sharper downturn. However, this will not alter the trend in Chinese growth, with GDP growth set to moderate to 6.3% in 2019 and 6.1% in 2020, from 6.6% in 2018.

The external environment is also largely to blame for the slowdown in Germany, despite resilience in the domestic economy. In March the flash composite purchasing managers' index declined to a six-year low, driven mainly by a sharp fall in manufacturing sentiment, signalling that the downturn in the country's large export-oriented industrial sector had become entrenched. In the US, private residential fixed investment has continued to weaken since hitting its post-recession peak in the second quarter of 2018. Meanwhile, the spread between three-month and ten-year US Treasury securities turned negative—a phenomenon known as a yield curve inversion—for five days in late March. Although this does not guarantee a recession, it is a clear signal from markets that economic growth is coming under serious strain.

Notwithstanding the current trend in global growth, the outlook for 2020 is not as pessimistic as we had initially anticipated. Two key factors help to explain this. First, we expect the current negotiations between the US and China to result in a limited trade deal that will avoid further escalation in tariffs from both sides (although we continue to expect the tariffs already in place to remain and to be contingent on the enforcement of measures in the forthcoming deal). This is a significant relief for global economic conditions, given the further disruption to supply chains that would have resulted from the US imposing tariffs on all Chinese imports and increasing the rate from 10% to 25% for a selection of those goods from China. Second, we expect the Federal Reserve (Fed, the US central bank) to hold interest rates stable this year before cutting rates by 50 basis points in 2020. This path for monetary policy will cushion growth in 2019-20 and help to guard against a sharper downturn in US economic conditions. Given these factors, we now expect the US economy to grow by 1.7% in 2020, up from 1.5% previously. Global growth, similarly, will slow less than previously forecast, easing to 2.6% in 2020, up from 2.5% previously.

Political uncertainty will continue to weigh on growth in major markets

Despite this change to our outlook for 2020, it would be a mistake to assume that global economic conditions will be benign in 2019-20. Policy uncertainty, driven by political and geopolitical factors, will affect growth negatively in both years. In Brazil, despite the boost to confidence following Jair Bolsonaro's election as president, uncertainty over pension reform has resulted in a drag on economic activity. Although we expect some form of pension reform to be agreed, the lack of clarity over its timing is curtailing the pick-up in growth as the economy slowly recovers from the recession in 2015-16. In Europe, Brexit-related uncertainty is adding to a challenging external environment that is constraining growth. With the UK and the EU agreeing to extend the deadline for Brexit to October 31st, uncertainty over the future business environment will continue to weigh on growth in 2019 and will linger into 2020.

The administration of the US president, Donald Trump, also continues to inject uncertainty into the international business environment on a number of fronts. On April 4th Mr Trump reiterated his threat to close the border with Mexico in order to stem the flow of migrants across the southern border. Rather than close the border and halt trade, the aim was to extract concessions from either the US Congress or Mexico on this issue; however, the ongoing threat to the sophisticated supply chains between the two countries is affecting the investment and planning decisions of exporting firms in the region. On April 9th the president escalated the dispute with the EU over European subsidies to Airbus, threatening to impose tariffs on US$11bn-worth of EU imports. This comes on top of a threat to impose tariffs on imports of EU vehicles and parts that the Trump administration views as a threat to the country's national security. As long as Mr Trump continues with this negotiating tactic, global trade will suffer. Finally, the US has also created uncertainty over the roll-out of fifth generation (5G) hardware owing to security concerns over Chinese companies taking a central role in such critical infrastructure. Mike Pompeo, the secretary of state, has effectively forced US allies and partners to choose between a US-led and a Chinese-led technology sphere. This will delay the roll-out of 5G technology in a number of countries and slow down the technological development that will occur as 5G encourages productivity and innovation.

Risks to global growth loom large

Furthermore, the risks to global growth are firmly tilted to the downside. The US economy is at risk of recession in 2020 owing to the rising stock and deteriorating quality of US corporate debt. The latest Fed data show that corporate debt had climbed to US$9.8trn by the fourth quarter of 2018, equivalent to 47% of annual GDP, returning to the pre-financial crisis peak of 2007. Worryingly, the high level of corporate debt has coincided with a sharp deterioration in the quality of that debt: more than half of investment-grade corporate bonds are rated BBB, the lowest level before "junk". The risk, therefore, is that the slowdown in growth interacts with corporate debt concerns to tip the economy into recession. As growth inevitably slows, businesses may face higher borrowing costs or a tightening of credit availability, both of which would act as a drag on hiring and investment decisions. The global trading system could face further shocks in 2019 from events such as a hard Brexit, which is not our current forecast, or a serious escalation in US-EU trade tensions that result in bilateral tariffs being applied. Finally, despite the likelihood of a stop-gap trade deal between the US and China, we continue to expect economic and trade tensions to remain between the two countries. The focus is likely to shift to investment and technology issues as the countries embark on a technological arms race to be the world's dominant economy in the coming decades. These tensions will cast a long shadow over global growth and international business conditions for the foreseeable future.

World economy: Forecast summary										
	2014	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Real GDP growth (%)										
World (PPP[a] exchange rates)	**3.5**	**3.4**	**3.2**	**3.7**	**3.6**	**3.4**	**3.4**	**3.6**	**3.6**	**3.5**
World (market exchange rates)	**2.8**	**2.8**	**2.4**	**3.1**	**2.9**	**2.7**	**2.6**	**2.8**	**2.9**	**2.8**
US	2.5	2.9	1.6	2.2	2.9	2.2	1.7	1.7	2.0	1.8
Euro area	1.4	2.0	1.9	2.5	1.8	1.3	1.4	1.7	1.7	1.7
Europe	1.9	1.9	1.9	2.7	2.1	1.5	1.8	1.9	2.0	1.9
China	7.3	6.9	6.7	6.8	6.6	6.3	6.1	5.6	5.3	5.0
Asia and Australasia	4.4	4.6	4.4	4.8	4.5	4.4	4.2	4.3	4.3	4.1
Latin America	1.0	-0.3	-1.2	0.9	0.7	1.4	1.7	2.7	2.7	2.8
Middle East & Africa	2.9	2.3	4.7	1.5	1.3	1.9	2.5	3.0	3.2	3.2
Sub-Saharan Africa	4.6	2.7	0.7	2.3	3.0	3.2	2.0	3.8	4.1	4.4
World inflation (%; av)[b]	**3.4**	**3.1**	**3.1**	**3.2**	**3.5**	**3.7**	**3.1**	**3.2**	**3.2**	**3.0**
World trade growth (%)	**2.9**	**2.0**	**2.1**	**5.4**	**4.4**	**3.3**	**2.9**	**3.8**	**3.9**	**4.0**
Commodities										
Oil (US$/barrel; Brent)	98.9	52.4	44.0	54.4	71.1	66.5	60.5	69.8	75.6	75.0
Industrial raw materials (US$; % change)	-5.1	-15.2	-2.2	20.2	2.2	-2.9	2.5	5.2	-0.5	0.4
Food, feedstuffs & beverages (US$; % change)	-5.3	-18.4	-3.5	-1.0	1.6	-3.6	3.7	3.2	3.1	1.1
Exchange rates (av)										

¥:US$	105.9	121.0	108.8	112.1	110.4	110.2	108.9	104.9	100.5	96.1
US$:€	1.33	1.11	1.11	1.13	1.18	1.14	1.19	1.21	1.24	1.24

[a] Purchasing power parity. [b] Excludes Venezuela.

Source: The Economist Intelligence Unit.

