

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

NICARAGUA

GLOBAL MULTISECTOR CREDIT PROGRAM

(NI-L1046)

LOAN PROPOSAL

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PRINTED ANNEXES	
Annex I	Summary DEM
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Electronic Links	
REQUIRED	
1.	Annual work plan Not applicable
2.	Monitoring and evaluation arrangements http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=2101552
3.	Procurement plan Not applicable
4.	Social and environmental strategy http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=2042452
OPTIONAL	
1.	Sector issues 1 [Central Bank of Nicaragua] http://www.bcn.gob.ni
2.	Sector issues [Financial system] http://www.superintendencia.gob.ni
3.	Sector issues 3 [Financiera Nicaragüense de Inversiones] http://www.fni.com.ni
4.	Exclusion list http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=2141465

ABBREVIATIONS

ASOMIF	Asociación Nicaragüense de Instituciones de Microfinanzas [Nicaraguan Association of Microfinance Institutions]
BANADES	Banco Nacional de Desarrollo [National Development Bank]
BLADEX	Banco Latinoamericano de Exportaciones [Latin American Export Bank]
FNI	Financiera Nicaragüense de Inversiones, S.A.
FSO	Fund for Special Operations
IDB	Inter-American Development Bank
MFI	Microfinance intermediary
MIF	Multilateral Investment Fund
MSMEs	Micro-, small, and medium-sized enterprises
OC	Ordinary capital
PCR	Program credit regulation
PERZA	Proyecto de Electrificación Rural en Zonas Aisladas [Rural electrification project in isolated zones]
SIBOIF	Superintendencia de Bancos y Otras Instituciones Financieras [Superintendency of Banks and Other Financial Institutions]

PROJECT SUMMARY

NICARAGUA GLOBAL MULTISECTOR CREDIT PROGRAM (NI-L1046)

Financial Terms and Conditions				
Borrower: Republic of Nicaragua Executing agency: Financiera Nicaragüense de Inversiones (FNI)		Amortization period:	OC 30 years	FSO 40 years
		Grace period:	66 months	40 years
		Disbursement period:	5 years	
		Commitment period:	4.5 years	
Source	Amount (US\$ million)	Interest rate:	LIBOR ¹	0.25 %
IDB (Ordinary Capital)	10	Inspection and supervision fee:	*	0 %
IDB (FSO)	10		*	*
Local	0	Credit fee:	*	0%
Total	20	Currency:	U.S. dollars from the Single Currency Facility	U.S. dollars
Project at a glance				
Project objective/description: The <u>general objective</u> of the program is to support Nicaragua's productive system by facilitating the supply of medium and long-term credit. Its <u>specific objective</u> is to channel medium- and long-term financing to the Nicaraguan financial system, for onlending to the productive sector (paragraph 1.15).				
Special contractual clauses: Conditions precedent to the first disbursement: (i) The signing and entry into force of an agreement between the borrower and FNI, for the latter to act as program executing agency; the text of the agreement must have been approved in advance by the Bank (paragraph 3.1); (ii) entry into force of the program Credit Regulations (PCR); the text of the Regulations must have been approved in advance by the Bank (paragraph 3.5c). Other contractual conditions: The proceeds of loan recoveries will be administered through the program's special account, for five years from the date of the final disbursement (paragraph 2.13).				
Exceptions to Bank policies: None.				
Project consistent with country strategy: Yes [X] No []				
Project qualifies as: SEQ [] PTI [] Sector [] Geographic [] Headcount []				
Procurement: N/A				

¹ The credit fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable provisions of the Bank's policy on lending rate methodology for Ordinary Capital loans. In no case will the credit fee exceed 0.75% or the inspection and supervision fee exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

¹ Policy of mandatory setting of the interest rate (LIBOR).

I. DESCRIPTION AND RESULTS MONITORING

A. Frame of reference, problem addressed, rationale

1. Sector characteristics

- 1.1 **The financial sector. Background and recent trends.** The banking segment of the Nicaraguan financial system consists of 10 financial intermediaries: eight banks and two finance companies. There is also a second-tier bank, Financiera Nicaragüense de Inversiones (FNI), and a leasing company. Other nonbank financial institutions that contribute to the country's economic development include a stock exchange, six brokerage firms, a securities depository, six insurance companies, and four bonded warehouses. Total system assets are about US\$3.7 billion, equivalent to 60% of GDP. There is also a large unregulated microfinance sector, which will be discussed below.
- 1.2 Bank supervision was improved considerably after the severe banking crisis that occurred in 2000-2001. The legal and regulatory framework was also substantially updated with the passage of several laws in 2005, including the new Bank Act which raises bank capital requirements to a level above that recommended by Basel I and also regulates banking confidentiality, share transfers, and corporate governance. Laws were also passed on deposit insurance, and a bank supervision legislation enacted by the Superintendency of Banks and Other Financial Institutions (SIBOIF). Recently, additional steps were taken, including the creation of a Financial Transactions Credit Bureau, a Credit Information System attached to the SIBOIF, and supplementary regulations on the management of credit risk, liquidity risk, and maturity matching. All of this seeks to promote healthy systemic behavior in the new environment.
- 1.3 The Nicaraguan financial system has managed to stay relatively immune from the effects of the international financial crisis, and a review of relevant sector data gives a reasonably favorable picture of the situation. This is the result of: (i) regulatory measures adopted by the SIBOIF and the central bank; and (ii) precautionary measures taken by financial institutions. Specifically:
- a. The liquidity ratio is 32%, well above the regulation level. Such high liquidity levels reflect the highly conservative, cautious stance adopted by the banking system in response to the crisis;
 - b. Portfolio quality is reasonably good, with 94% of loans rated in categories A and B, and an arrears ratio of 2.25%.² Although this has risen by half a percentage point since last year, it remains at very acceptable levels.

² Overdue loans represented 2.25% of the gross portfolio, compared to 1.98% in December 2008. This increase is a warning sign since it could be reflecting the sensitivity of the portfolio to consumption financed mainly by credit cards, which are a large component of the credit structure.

- c. System capitalization is relatively prudent, with a capital ratio of 15%. This is also comfortably above the 16% minimum level required by SIBOIF under Nicaraguan legislation.
 - d. Loans and deposits have fallen by 5.57% so far in 2009, following strong growth, averaging 27%, over last two years. This reflects the following: (i) a reduction in the demand for credit in the wake of the crisis; and (ii) and a more conservative stance adopted by the banking system in managing its assets; and
 - e. Rates of return, although somewhat lower than in previous years, remain at more than acceptable levels, with an ROA of 1.6%, and an ROE of 15%.
- 1.4 In conclusion, the data reviewed show that, without a radical and sudden recovery in the international economy, the national financial system is expected to deteriorate somewhat. In the absence of extreme scenarios, there are certainly no latent dangers to suggest a systemic risk event of any kind.
- 1.5 Nonetheless, some of the repercussions of the crisis on the financial system also impact the real productive system and are clearly related to the objectives of this program. These include: (i) stronger liquidity levels and prudential provisions; (ii) slow deposit growth; (iii) reduced external credit both to the banking system and to large export enterprises; and (iv) less supplier credit.
- 1.6 All of these factors have combined to produce an estimated funding gap of approximately US\$200 million, broken down as follows: US\$100 million for large firms, US\$60 million for medium-sized enterprises, and US\$40 million for small businesses. This global financing deficit has two components: (i) a short-term component, relating to international trade financing; and (ii) medium- and long-term components in terms of funding for investment projects and permanent working capital in the micro, small, and medium-sized enterprise (MSME) category.
- 1.7 **The microfinance sector.** Nicaragua's unregulated microfinance industry is one of the most developed in the region, with a total of 19 microfinance institutions (MFIs), grouped together in the Nicaraguan Association of Microfinance Institutions (ASOMIF). These have over 350,000 clients and a portfolio of approximately US\$250 million. The largest institutions in terms of portfolio size and number of clients have a presence throughout the country, whereas the others operate only in the central region (Managua and Matagalpa) or other parts of the country. There are also nearly 2,000 credit cooperatives and credit unions providing intermediation services, albeit on a small scale in terms of volume and target market. This diversity of supply, particularly in the central region, means strong competition between the different institutions.
- 1.8 The most important MFIs were created in the early 1990s during the first financial sector reform, in response to the disappearance of National Development Bank (BANADES). In the past, particularly when the first Sandinista government was in

power in the 1980s, BANADES was a major source of funding for MSMEs, especially in areas outside the central region. The opportunity for MFIs arose because the traditional regulated financial sector, created during the 1990s, has focused on corporate borrowing and consumer credit. The first MFIs were created with support from specialized international cooperation agencies (Procredit, FMO, Acción Internacional), and their good results then attracted other investors into the sector although international cooperation continues to be provided. The Multilateral Investment Fund (MIF) has also been providing support through several operations (see below).

- 1.9 **The MSME sector.** The Nicaraguan business fabric consists predominantly of MSMEs, which play a crucial role in fueling growth and creating jobs. The National Institute of Statistics and the Census (General Household Survey) reports that 69% of all employed persons work in microenterprises and 15% in small firms, jointly accounting for 84% of all employment in the country. The informal private sector contributes an estimated 45% of GDP. The microenterprise sector is the main source of employment in Nicaragua, absorbing over 50% of the country's economically active population (EAP). The number of microenterprises is estimated at about 575,000, of which 275,000 (48%) are in urban areas, and 300,000 (52%) in rural zones. MSMEs account for roughly 247,660 jobs in urban areas, 74% of the total. Some 56% of urban MSMEs operate in the trade and services sector, 17% in manufacturing, and the rest in other sectors. In the rural area, the large proportion of agricultural loans in MFI portfolios reflects the importance of this sector both in the Nicaraguan economy and in the sector composition of MSMEs.

2. Problem to be addressed and rationale for the program

- 1.10 The funding gap in the MSME sector. MSMEs have been the hardest hit by the crisis and the ensuing credit crunch. Naturally, the smaller the firm, the more likely it is to be affected by credit constraints. Although the international financial crisis has diminished overall demand for credit, supply has contracted by even more (for the reasons noted above), resulting in an estimated funding deficit in the SME sector of approximately US\$100 million—US\$60 million for medium-sized firms and US\$40 million for small ones.
- 1.11 Proposed program. Given the macroeconomic and financial prospects described earlier, the proposed program seeks to mitigate the financing problems faced by the private sector in recent months, and thus underpin the pace of domestic economic activity in a particularly difficult and uncertain international economic and financial climate that still shows no clear signs of recovery.
- 1.12 The program is consistent with the Bank's Strategy with Nicaragua (2004-2008), which seeks to support sustainable growth through: (i) a stronger institutional environment and fiscal sustainability; (ii) more reliable electric energy sources and a better road system; (iii) better management and scope of social services, including the promotion of a sustainable social security program; (iv) productive

development; and (v) a strengthening of the country's natural disaster response and prevention capacity. The proposed program fits in with point (iv) of the Strategy.

3. Coordination with other multilateral institutions:

- 1.13 In preparing this operation, the Bank has maintained permanent contact with the authorities of the International Monetary Fund, the World Bank, and other members of the donor community in Nicaragua. Coordination meetings have been held with the other donors in all missions to prepare the operation.
- 1.14 The project team is also coordinating the program design and implementation with the technical team assigned to MIF operations. The MIF-financed portfolio in execution and in preparation contains technical assistance, equity investment, and financial products, including the following programs relating to credit access for the productive sector: Improving access to credit for MSMEs through innovative techniques (ATN/ME-9864-RG, RG-M1082); and Improving the competitiveness of small and medium-sized forestry enterprises (TC010303/ATN/ME-7953-RG). The MIF portfolio stands at US\$7.4 million. Coordination between the Bank and MIF teams would maintain cohesion and complementarity, thus optimizing the use of resources and the impact of the operations funded by both institutions.

B. Program objectives, characteristics, and components

- 1.15 **Objective.** The program's general objective will be to support the national productive system by facilitating the supply of medium and long-term credit. Its specific objective will be to provide medium- and long-term funds to the Nicaraguan financial system for onlending to the productive sector.
- 1.16 **Characteristics.** The program will form part of the Bank's strategy to support private sector development. It will use public funds to support financial intermediation processes in situations where the market has failed, specifically offsetting the shortage of business financing for the productive fabric.
- 1.17 The proposed program is a global multisector credit program to support private sector business development, especially small and medium-sized enterprises, by expanding the supply of short-, medium-, and long-term credit. The program is fairly standard in all respects, except one. The second-tier vehicle will operate two facilities: (i) one for regulated financial intermediaries (i.e. banks and finance houses); and (ii) another for unregulated MFIs declared eligible for loans under the program, in accordance with the risk management regulations in the PCR.
- 1.18 The second window is being opened for MFIs because these financial institutions basically serve small businesses and microenterprises in rural production, which are virtually ignored by regulated financial intermediaries. This target population is the most credit-starved group in economic and financial circumstances such as those currently facing the Nicaraguan economy as a result of the international crisis.
- 1.19 In fact, MFIs have not been immune from the impact of the crisis, however, and their funding needs have shrunk considerably. Nonetheless the microenterprise

sector still has an estimated funding gap of around US\$12 million,³ which means that the microfinance sector is facing the same problems of access to financing as the regulated financial sector. Hence, the program provides for funding this type of financial intermediary.

- 1.20 **Components.** The program will have a single loan component, to which the proceeds of the financing will be assigned.

C. Outcome Indicators

- 1.21 Given the nature of the program, it is very important to keep in mind that one of its basic design premises is to ensure that credit reaches the best⁴ borrowers among those considered eligible to participate in the program.
- 1.22 To achieve this objective, the program will use an implementation mechanism that extends credit to a predefined set of financial intermediaries (including MFIs), on the assumption that the market in which this type of intermediary operates will select borrowers optimally in the sense defined in the foregoing paragraph.
- 1.23 An expeditious way to ensure that this mechanism operates adequately is to compare the arrears rate among borrowers whose projects have been financed by the program with the average arrears rate in the credit system. If the former is better or the same as the latter, the mechanism can be said to be functioning adequately.
- 1.24 Consequently, the aggregate impact of the operation will be whatever market circumstances allow. Thus, the levels achieved by the program's purpose or goal indicators can be used to measure the performance of the market mechanism and/or prevailing conditions, but not that of the operation's intrinsic attributes.
- 1.25 On this basis, the main program indicators are those contained in the Results Matrix annexed to this document: (i) in terms of *output*: (a) the opening of second-tier credit lines; and (b) the channeling of funds from financial intermediaries and MFIs to firms, assuming that the basic assumptions in this type of program are fulfilled (a reciprocal willingness among borrowers and financial intermediaries and MFIs to seek and grant credit). (ii) in terms of intermediate *outcomes*, the trend in credit maturity terms; and (iii) as final *outcomes*, the level of disbursements and portfolio quality.
- 1.26 Lastly, following the guidelines provided by the Bank's Office of Evaluation and Oversight on evaluating global multisector credit programs, and with a view to increasing the volume of information on program outcomes in addition to the results framework, ex post data will be collected for these purposes.

³ This figure of US\$12 million is in addition to the US\$200 million indicated above, which included large, medium-sized, and small businesses, but not microenterprises.

⁴ "Best" is defined in terms of the borrowers' risk/return ratio.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instrument

- 2.1 The borrower will be the Republic of Nicaragua.
- 2.2 Financiera Nicaragüense de Inversiones S.A. (FNI) will be the program executing agency. FNI is a financial corporation (*sociedad anónima* or S.A.), in which the Republic of Nicaragua has a majority interest. It is regulated by the SIBOIF and supervised by the Comptroller General. It was created by Law 289 of 26 March 1998, to finance projects funded with resources from private commercial banks and development agencies, including international agencies, by channeling those resources as loans to financial intermediaries and MFIs for onlending to the productive sector in the form of subloans for eligible projects.
- 2.3 The conditions under which FNI will manage program funds on behalf of the Republic of Nicaragua will be defined in a contract to be signed by both parties prior to the first disbursement of the financing, and subject to prior Bank approval.
- 2.4 The PCR will set the conditions under which the FNI will onlend to financial intermediaries and MFIs, and these in turn will lend the resources to the subborrowers. The transfer of funds from the FNI to the financial intermediaries and MFIs must not involve any type of financial or regulatory arbitrage.
- 2.5 Program costs are summarized in the following table:

Program cost by source of financing (US\$ million)			
Investment component	IDB	Local contribution	Total
Credit	20	0	20
Total	20	0	20

B. Risks

- 2.6 Macroeconomic risks. - The success of the program will depend on maintaining a macroeconomic framework and climate that encourages productive investment and private sector demand for credit. It should be said the Nicaraguan authorities are redoubling their efforts to preserve the stability of the framework in the current international setting.
- 2.7 Fiduciary risks. - The program is considered to be of medium fiduciary risk. Although FNI is given legal, administrative, and fiduciary independence under its establishing law, and has experience in managing Bank-financed projects, it should be recalled that Banco Produzcamos was created under Law 640 of 6 November 2007 (regulated by Decree 68.208 of 21 December 2008 and amended by Law 648 of 5 May 2009, in turn regulated by Decree 57-209 of 3 August 2009). This new bank will become the specialist entity for receiving, channeling, managing, and

- lending resources received from the international community for loans to promote, develop, and foster domestic production of various kinds in various stages of the productive process.
- 2.8 In addition, the independence of execution decisions and the use of program funds are guaranteed by the fact that the loans are being granted by financial intermediaries on the basis of risk analysis, using entirely financial and market criteria, under normal operating conditions.
- 2.9 Financial risks. - The program's financial viability and risks will be determined by: (i) the quality of SIBOIF supervision; (ii) the financing rate; (iii) the return/risk that FNI obtains on the loans it grants; (iv) the return/risk that the financial intermediaries and MFIs obtain under market conditions; and (v) the collateral set by FNI and, to a lesser extent, that required by the financial intermediaries and MFIs.
- 2.10 Environmental risks. - As the nature and impact of the products and activities to be financed by the subloans cannot be foreseen, these will be governed by the country's environmental systems and legislation. In accordance with the Bank's policy, and specifically Directive B.13 of the Environment and Safeguards Compliance Policy, the program will not require an environmental classification. Given its nature, FNI does not verify each subloan, leaving the first-tier entities to apply current legislation. Nonetheless, both the loan contract and the PCR will provide for the following: (i) a negative list of products and activities ineligible for financing; (ii) a list of sectors for which financing may be provided if the subborrowers submit the corresponding environmental documentation (including licenses and permits); (iii) all operations of subborrowers not covered by the foregoing cases will be eligible for financing provided they comply with national environmental legislation; (iv) any violation of environmental legislation will render such firms ineligible; and (v) in contracts between subborrowers and the financial intermediaries and MFIs it must be demonstrated that the subborrowers are complying with applicable environmental legislation. As part of its review, the Bank will verify that the subloans conform to environmental requirements and, if necessary, request additional information from the financial intermediaries and MFIs.
- 2.11 Executing agency risk. - As noted in paragraph 2.7, Banco Produzcamos was legally established to carry out some of the tasks now performed by FNI. Nonetheless, the new bank has not yet started operations, and Executive Decree 43-2009, of 16 June 2009, has appointed FNI as its ad hoc general manager. FNI continues to have its own equity and technical team. To ensure greater legal security for the proposed execution scheme, the authorities of the borrower country have undertaken to obtain confirmation from the SIBOIF and the Office of the Attorney General that FNI has legal capacity to act as program executing agency.
- 2.12 Although it might eventually prove necessary to change the program executing agency, everything would seem to suggest that Banco Produzcamos will be built on

the material and human base of the current FNI. Should that prove to be the case, the risk that Produzcamos might not be up to the task of program executing agency would be substantially mitigated.

- 2.13 In addition, the contractual condition that funds disbursed from the revolving fund and any recoveries of loans granted to subborrowers must be held in specific and separate bank accounts **and the contractual condition that the proceeds of loan recoveries must be administered through the program's special account for five years after the date of the final disbursement** will permit the Bank to monitor Banco Produzcamos's activities even if the latter eventually becomes an executing agency.
- 2.14 Financial intermediary risk. - Another incremental risk would be if the lending facility were opened for unregulated MFIs. This is mitigated by the fact that the FNI has long experience of financing MFIs, although it has always done so as a trustee of funds under management and never assuming MFI risk on its own balance sheet. Even so, the MFI arrears rate with funds managed by FNI has been zero, which shows that the latter's risk evaluation and management procedures are sufficiently effective.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

1. Borrower and executing agency

- 3.1 The borrower for the program will be the Republic of Nicaragua, and the executing agency Financiera Nicaragüense de Inversiones (FNI). As noted earlier, **a condition precedent to the first disbursement shall be signature and entry into effect of an agreement between the borrower and FNI, whereby the latter agrees to act as program executing agency. The text of the agreement must have been previously approved by the Bank.**
- 3.2 Bank lending programs executed by FNI. The Bank has already granted a loan to the Republic of Nicaragua that was executed by FNI. The operation (1122/SF-NI; NI-0167) was a global multisector credit program for US\$30 million. Of that amount, US\$29.2 million (98%) went to the credit component for business sector development, particularly small and medium-sized enterprises, while the remainder was used to finance technical assistance. The loan in question was approved by the Board of Executive Directors on 26 February 2003, and the first disbursement was made on 23 March 2004. The credit component was executed through financial intermediaries supervised by the SIBOIF and was absorbed in the first four years with a satisfactory level of execution. Since the inception of the program, the loan has been rolled over 2.3 times. This operation was expected to generate at least 360 subloans for an average of US\$100,000 each and maturity terms of at least 36 months; but these targets were surpassed in December 2008, by which time it had a portfolio of 4,564 financial intermediary subloan clients, with average loans

of US\$16,000 and average terms of 58 months. FNI will shortly be completing a program impact study.

3.3 Programs with other donors. FNI is also operating programs financed by other donors, including:

- a. A program with Banco Latino Americano de Exportación (BLADEX) to provide financing support for the export and import of productive goods;
- b. A fund administered for Campesino Development Fund (FONDECA) MFIs for the purpose of financing campesino production in the dry tropical region of northern Nicaragua. The fund's end clients are agricultural and forestry producers, rural microentrepreneurs (up to five employees), craftsmen, and independent trades people. The intermediaries are rural cooperatives or MFIs to ensure that rural financial services (savings and loans) can be offered to the FONDECA target population on a sustainable basis;
- c. The Microcredit Fund of the Rural Electrification Project in Isolated Zones of the National Interconnection System (PERZA). This fund is similar to the one described in the preceding paragraph;
- d. A loan contract in the amount of €2.8 million between the Republic of Nicaragua and Kreditanstalt für Wiederaufbau (KfW) that is being implemented through MFIs not regulated by SIBOIF, for the purpose of generating a loan portfolio in the microenterprise and small business segment.

2. Execution and administration

3.4 The executing agency will be responsible for: (i) channeling resources to eligible financial intermediaries and MFIs; (ii) ensuring that there is adequate custody and administration of the securities and/or credit documents received as collateral; (iii) the eligibility of subloans and their supervision and control; (iv) provision, as agreed, of the human, technological and budgetary resources needed for program execution; (v) presentation to the Bank of the documentation needed to fulfill the disbursement conditions; and (vi) other activities of an operational nature needed for execution. The program will be implemented and administered through individualized accounts recorded on the FNI balance sheet.

3.5 Credit Regulations. The program will be implemented on the basis of the PRC, in accordance with the following guidelines:

- a. it must be consistent with the terms of the loan contract between the Republic of Nicaragua and the Bank, the regulations and policies of FNI and the Bank, and Nicaraguan law and financial practices;
- b. it must stipulate that failure to fulfill its provisions will prevent access to financing;
- c. **approval of the text of the PRC with the Bank's no objection and its implementation will be a condition precedent to the first disbursement; and**

- d. any amendments to the Regulations will require the Bank's no objection.
- 3.6 Eligibility of financial intermediaries and MFIs. Financial intermediaries and MFIs will be eligible if they satisfy the risk parameters set out in the PCR. Those parameters set a risk quota for each financial intermediary and MFI, and the total amount of current loans at any time must not exceed the quota.
- 3.7 Main obligations of the financial intermediary and MFI. The main obligations of the financial intermediaries and MFIs participating in the program are as follows: (i) to request a credit line quota from FNI and sign the contract to join the program; (ii) to study and evaluate the activities to be funded, financial solvency, payment capacity, and collateral offered by the subborrowers; (iii) to request collateral in accordance with Credit Regulations; (iv) transfer resources to subborrowers in accordance with the Credit Regulations; (v) assume all credit risks arising from the subloans; (vi) make sure that subborrowers make correct use of the resources in accordance with declared and eligible purposes; and (vii) provide the Bank, FNI, the Republic of Nicaragua, and program auditors with information requested on the portfolio of loans granted using program funds.
- 3.8 Financing arrangement for financial intermediaries and MFIs. The terms of the arrangement for transferring funds from the FNI to the financial intermediaries and MFIs are set out in detail in the PCR. The main points are given below:
 - a. Granting of loans.- Loans to each financial intermediary and MFI will be granted in the order that requests are received and approved, provided program funds are available and the requesting entity has a quota available;
 - b. Maturity.- The program will lend to financial intermediaries and MFIs for a maximum period of 15 years, or the period specified in the PCR;
 - c. Interest rate and fees. – Interest on the loans will accrue at a rate set by the FNI, which must be high enough to cover program operating costs. The FNI may charge the financial intermediaries and MFIs such loan commissions and fees as are considered appropriate, as specified in the PCR;
 - d. Collateral. - The financing provided to financial intermediaries and MFIs will need to be guaranteed with first-tier assets, as specified in the PCR;
 - e. Nonfulfillment and penalties. - Participation in the program by financial intermediaries and MFIs implies that they knowingly accept the applicable regulations in effect and agree to be bound by FNI and SBOIF interpretation of such regulations and to be bound by FNI and SBOIF oversight and control (in their respective areas of authority).
- 3.9 Financing arrangement for subborrowers (subloans). The terms and conditions of the arrangement for transferring funds from the financial intermediaries and MFIs to the MSME subborrowers will be fully described in the PCR. The main terms and conditions are:

- a. The subloan conditions will be freely set by the financial intermediaries, the MFIs, and subborrowers, in keeping with the PCR.
- b. Program resources may not be used to finance: (i) the purchase of real estate; (ii) the payment of dividends or recovery of invested capital; (iii) the purchase of shares, bonds, or other securities; (iv) the subborrowers' general or administrative expenses; (v) projects that do not meet the criteria of Nicaraguan environmental legislation; and (vi) the refinancing of debt. Goods and services funded with the subloans must be used exclusively for the purposes specified in the loan contract insofar as they do not violate the negative list, and are sourced exclusively in the Bank's member countries.
- c. The subborrower will undertake to fulfill the corresponding environmental legislation, including presentation of the relevant environmental permits whenever it requests funding for activities, products, or companies working in environmentally sensitive sectors and subsectors. Subborrower operations not on the negative list, or on the list of environmentally sensitive sectors, will be eligible for financing, provided it can be formally demonstrated that they comply with environmental legislation in effect.
- d. Any subborrower that fails to fulfill these requirements may be liable to the following penalties: (i) suspension from participation in the program and all loans received under the program will become immediately due and payable; and (ii) ineligibility to continue participating in the program. These penalties notwithstanding, the subborrower may be subject to any other penalties applicable under current Nicaraguan law.

3. Characteristics of disbursements and execution

- 3.10 Plan of operations. The program does not require a plan of operations strictly speaking, or a procurement plan, since its output consists of opening or maintaining second-tier credit lines with FNI.
- 3.11 Commitment and disbursement period. The program will have a five-year disbursement period and a 54-month commitment period, reckoned from the effective date of the loan contract.
- 3.12 Revolving fund: The revolving fund for this program will be 5% of the loan amount.

B. Summary of arrangements for monitoring results

- 3.13 The program will apply the general procedures established by the Bank for the monitoring and evaluation of investment operations.
- 3.14 Reports. Program execution will be monitored through semiannual status reports prepared by the executing agency and submitted to the Bank by the deadline stipulated in the general contractual conditions. The reports will take as a reference fulfillment of the commitments agreed upon, as shown in the results matrix.

- 3.15 Supervision: (i) disbursements will be supervised ex post; and (ii) the Bank will schedule inspections of the financial intermediaries or MFIs in coordination with FNI, to verify fulfillment of the program's contractual clauses; and, if appropriate, it may engage technical consulting services to verify program audits performed by FNI as well as the eligibility of the subloans.
- 3.16 FNI will keep proper records of program expenses in accordance with the general contractual conditions.
- 3.17 Audits of program resources and the executing agency will be performed annually by a firm of public accountants acceptable to the Bank in accordance with the general contractual conditions. The firm will be selected according to terms of reference previously agreed upon with the Bank (document AF-400), and pursuant to the Bank's audit policy. The fees charged by the firm will be financed out of the proceeds of the loan.
- 3.18 Midterm evaluation. Within 24 months after the date of the first disbursement, or when 50% of the financing has been committed, whichever occurs first, a consultant or a consulting firm hired by the borrower, out of its own funds, will submit a midterm evaluation report on:
- a. The extent to which the objectives and outcomes have been achieved, based on the results matrix;
 - b. The extent to which the environmental requirements have been met;
 - c. The steps that may be taken in the event that the program is considered not to have substantially achieved its objectives. The program indicator base line will be determined before start-up of the program.
- 3.19 Depending on resources available, the Bank may perform an external evaluation at the end of the disbursement period, to assess the extent to which the program objectives have been fulfilled and gauge its development impact. The executing agency will keep all relevant information available to facilitate this evaluation.

ANNEX I

The information contained in this document is confidential.

NICARAGUA
GLOBAL MULTISECTOR CREDIT PROGRAM (NI-L1046)
RESULTS MATRIX

Program Objective							
To help restore the flow of credit to the real economy, by partly and temporarily offsetting the decline in the normal flow of financing to the productive sector as a result of the international financial crisis.							
Purpose of the Operation							
To channel loans in foreign exchange through financial intermediaries to the productive sector.							
Indicators ¹							Description
	Base level	Year 1	Year 2	Year 3	Year 4	Target	
SINGLE COMPONENT: FNI maintain/opens credit lines to financial intermediaries.							
Output							
Financial intermediaries have the possibility of accessing credit lines with IDB resources.	0	Up to 99%	Up to 99%	Up to 99%	Up to 99%	Up to 99%	This percentage indicates the capacity of FNI to place program funds (if the market is interested in absorbing them).
PURPOSE: The productive sector obtains funds to mitigate existing market failures.							
Intermediate outcome							
Trend of the maturities of multisector credit program loans compared to the average maturity of the commercial portfolio of the financial system.	Better than system average.	Better than system average.	Better than system average.	Better than system average.	Better than system average.	Better than system average.	This indicator shows the relation between the maturity of loans under the program and the average maturity in the system, thus indicating the need for the program. Each cell compares the average maturity in the program in the corresponding year, with the average maturity in the commercial portfolio of financial intermediaries in the system.
	Base	Year 1	Year 2	Year 3	Year 4	Target	
Cofinancing provided by financial intermediaries from the system in relation to program subloans.	7%	8%	9%	10%	11%	11%	The funds that the program releases in the form of loans from intermediaries with their own long-term resources will be a second measure of the need for additional credit lines of this type.

¹ In this operation, as in any other multisector credit program, financial intermediaries will select the most viable projects, so that their impact will be whatever market circumstances permit. Thus, the goal or purpose indicators are only an estimate of what the market could achieve.

Indicators ¹							Description
							Hence, the higher the arithmetic mean of the cofinancing percentages for investment projects financed by the program, the less will be the need for future similar programs. This percentage represents cofinancing by intermediaries in relation to the total amount of each loan.
Final outcome							
Financial intermediaries that have access to medium and long-term credit lines with IDB resources obtain program funds.	0%	25%	50%	75%	100%	100%	Level of program placements absorbed by existing demand. This percentage represents the cumulative degree of placements in relation to the total amount of the financing assigned by the Bank through the program.
Portfolio quality of program subloans for financial intermediaries compared to the system rating structure.	At least as good as the system.	At least as good as the system.	At least as good as the system.	At least as good as the system.	At least as good as the system.	At least as good as the system.	As financial intermediaries will be selecting the most viable firms and projects, the impact of financed projects will be whatever market circumstances allow. The financial intermediaries will choose the best firms and, insofar as the arrears rate remains similar to that of the system, the market itself will ensure that the best projects are selected. Thus, the relation between market portfolio quality and program portfolio quality is crucial for measuring the program's success. This indicator shows the behavior of program subborrowers to be maintained as financial intermediary customers. Each cell compares subloan portfolio quality to that of the system.

NICARAGUA
GLOBAL MULTISECTOR CREDIT PROGRAM (NI-L1046)
RESULTS FRAMEWORK

To increase the volume of information and make it possible to quantify the impact of the operation and the indicators matrix, ex post information will be collected on the following indicators:

FNI: The Nicaraguan productive and export system is strengthened						
Indicators	Year 1	Year 2	Year 3	Year 4	Year 5	Description
Level of program activity: <ul style="list-style-type: none"> by geographic area by sector by firm size 						This indicator shows the level of program activities, as a percentage of disbursements, in relation to: (i) regions of the country; (ii) sectors; and (iii) the size of some borrower firms.
Participation of the system in the program						This indicator demonstrates the participation of system financial intermediaries in the program. Each cell will show the relation between the assets of participating financial intermediaries and total system assets.
Average spread applied by financial intermediaries, by: <ul style="list-style-type: none"> firm size maturity of the financing 						This is a weighted average of the spread applied by financial intermediaries to the program subborrowers. It should be noted that, given the nature of program objectives: (i) a general increase in the maturity of placements could lead to an increase in the spread applied by the financial intermediaries; and (ii) as program subborrowers are smaller firms, the average spread could also trend upwards. The indicator will show the average spread applied by financial intermediaries, with a breakdown by firm size and loan maturity.
Program subborrower firms that have increased their annual gross sales.						This indicator shows the trend in the number of firms that have increased their annual gross sales.
Program subborrowers that have increased their operating profit margins						This indicator measures the program's impact on the productivity of subborrower firms. Each cell shows the number of firms that have increased their operating profit margins
Program subborrower firms that have started to serve new export markets.						This indicator shows the number of subborrower firms that have increased their export markets.