



## Executive Brief - Nicaragua

### Effects of the Financial Crisis on Vulnerable Households

**Background:** This brief is part of a series of five presenting the findings of case studies on the impact of the global financial and economic crisis on households' food security, conducted in March and April 2009.<sup>1</sup>

#### Overview

Nicaragua is a small Central American country with a population of 5.6 million inhabitants, of which 59% is urban. Most of the population is concentrated in the Pacific lowlands.

Nicaragua is a Low Income Country. Its economy is small, open and highly dependent on the United States for exports (garment and car equipment manufacture, coffee and seafood), employment in US firms based in Nicaragua, and remittances. Remittances are the country's second largest incoming resource flow (after agricultural exports), representing 13 percent of GDP. The country's main imports are food, fuel and energy, capita goods and agricultural inputs. The country is therefore **particularly vulnerable to the effects of the slow-down** of the US economy and decreased demand for its export commodities.

#### What is the macro-economic impact on the country?

In the last years, the country experienced positive economic growth, led by growth in the manufacture sectors. After reaching 2.9% in 2007, economic growth slowed down in 2008 due to a decrease in investment and rising wages, food prices and energy costs. The global high food and fuel prices, compounded by the damage caused by Hurricane Felix and heavy flooding in 2007 and 2008, translated into a **34% peak of domestic food price inflation** in August and 29% in October 2008.

- ✓ At the time of the study in March 2009, no major macro-economic effects of the global crisis were apparent, except for a decreased of exports compared to previous years and plateau remittances since the end of 2007.
- ✓ However, significant negative effects are anticipated in the near future, as a result of further slowing down of exports and decreased remittance flows from migrants in the US, Costa Rica and El Salvador. Balance of trade is thus anticipated to worsen and GDP growth to decrease in 2009 (projected at 3% for 2008, down to 1.5% for 2009). Foreign Direct Investment may also decrease slightly (from 7.1% of GDP in 2008 to 6.1% in 2009), while official aid would remain about the same (11% of GDP).
- ✓ The slow-down of the US economy is expected to affect employment and outputs of the 100 US-related companies operating in Nicaragua. Employment is anticipated to shrink, especially in the garment industry, as the US demand is decreasing. An estimated **19,000 workers have already been laid off since end 2008**. Although not yet apparent, agricultural labourers in export-oriented commodities will be affected by the expected decrease of exports (coffee, seafood, meat, sugar cane, groundnuts). Furthermore, lower access to credit and inputs will decrease yields and area cultivated and also reduce agricultural labour opportunities.

#### What is the impact on households' food security?

- ✓ Even though the full effects of the global financial crisis are yet to unfold in Nicaragua, it is clear that they will aggravate a pre-crisis situation of widespread chronic poverty, food insecurity and malnutrition. These conditions are themselves related to basic agro-ecological and socio-economic factors compounded by the high vulnerability of Nicaragua to natural disasters.
- ✓ Households most likely to be affected by the economic slowdown include those for which a significant share of income comes from remittances or wages from employment in export-oriented activities, or from sales of handicraft. While the poorest may not be the ones receiving remittances or having a formal job, they are affected by second-run effects on informal employment and depressed local economy.
- ✓ Households' food insecurity in Nicaragua is **essentially a problem of economic access to food**. Persistent high food prices have led to a change of food consumption patterns, particularly a decreased intake of meat and dairy products. However, decreased economic access to food is compounded by lower incomes resulting from: (i) decreased employment opportunities abroad (remittances) and locally, including agricultural labour, mines and export-oriented factories (e.g. seafood), and (ii) lower earnings from sales of agricultural products sales (low producer prices, high cost of inputs) or handicraft (reduced demand, high raw material cost).

<sup>1</sup> Analysis has been undertaken in Armenia, Nicaragua, Ghana, Bangladesh, and Zambia.

- ✓ Depressed local economy also translates into the closure of small businesses and tightening of credit conditions by local shop-keepers, further limiting access to food by poor households.
- ✓ While the proportion of households relying on remittances for most of their income is relatively low (7% urban and 4% rural households) and while remittance beneficiaries were seldom extremely poor, remittances make a significant contribution to poverty reduction. They are instrumental to pay for agricultural inputs, invest in land and animals, cover education costs and carry out housing improvement,
- ✓ The deterioration of households' economic situation is translating into **poorer diet (with less animal products and oil) lower incentives to cultivate and keep animals, decreased essential expenditures for health and education, and engagement into low-earning, informal income earning activities** (e.g. petty trade). Less important expenses are also suspended, including for clothes, shoes and house improvement. In future, households intend to increase out-migration and efforts to obtain credit, despite the risk of indebtedness that these entail. Other negative coping strategies are sales of animals and domestic assets, and environmentally damaging activities such as firewood collection for sale.

### **How is the situation likely to evolve?**

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- ✓ It is highly unlikely that Nicaragua will reach its extreme poverty Millennium Development Goal in 2015 (9.7% from 14.9% in 2005). Instead, **poverty is likely to augment in a context of already high poverty rates**: about half of the population was poor before the crisis (living with less than US\$1 per day) and 15% extremely poor (less than US\$0.5 per day). While needs for social assistance will increase, the government budgetary capacity to expand existing programmes will decrease.
- ✓ Decreased food availability at household, local and national level cannot be excluded due to discouragement of cultivation resulting from the high cost of agricultural inputs, low producer prices and decreased exports. This will worsen household food access as well as the national balance of trade.
- ✓ Dietary changes may translate into **higher chronic malnutrition rates among children under-5** (stunting is already affecting one out of 5 children) and worsen energy and micronutrient deficiencies among other vulnerable groups such as pregnant and lactating women, the elderly and the chronically sick. Decreased health expenditures will have further negative effects on the nutritional status of vulnerable individuals. The capacity of the government to expand the currently low coverage by water and sanitation services and improve the quality of health care will be limited by the budgetary effects of the economic crisis.
- ✓ Reduced households' investment education is also likely to impair future livelihoods. There are **worries of a possible increase of insecurity and violence** due to expected high unemployment, especially in urban areas.

### **What are the ongoing responses and recommendations?**

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- ❖ Specific interventions of the government and international organizations to address the effects of the financial crisis are not clearly spelled out yet. Measures taken in response to the high food and fuel prices could be usefully expanded. These include the Integral School Nutrition Programme (supported by the World Bank and WFP), the Agro-Seeds and Productive Food Programmes (supported by the World Bank and FAO), and opening of fair-price shops for basic foods in poor urban neighbourhoods.
- ❖ Interventions in response to the financial crisis should not only mitigate the immediate effects on specific population groups (small-scale and landless rural poor, newly unemployed in urban areas, children in poor households) but also continue to tackle the basic causes of poverty and food insecurity, including improvement of services (health, water, sanitation, education), infrastructures, agricultural productivity and access to credit.
- ❖ With no clear sense of the length and depth of the crisis, contingency planning and enhanced monitoring of evolving economic, fiscal and household food security situation is also critical.

#### **For more information on the case study, please contact:**

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**How was the assessment done?** It is based on a secondary data review of macro-economic indicators and a rapid qualitative food security assessment of households in 19 locations (10 rural and 9 urban) selected on the basis of the vulnerability of their livelihoods to the financial crisis. 125 households and 28 key informants were interviewed and 24 focus group discussions organised.