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REQUEST FOR A STAND-BY ARRANGEMENT AND AN ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY —STAFF REPORT; PRESS RELEASE

In the context of the 2014 request for a Stand-By Arrangement and an Arrangement under the Stand-By Credit Facility, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 3, 2014, following discussions that ended on October 8, 2014 with the officials of Honduras on economic developments and policies underpinning the arrangements. Based on information available at the time of these discussions, the staff report was completed on November 17, 2014
- An **Informational Annex** prepared by the IMF.
- A **Press Release** on the Executive Board's consideration of the request for the arrangements on December 3, 2014.
- The documents listed below have been or will be separately released.

  Letter of Intent sent to the IMF by the authorities of Honduras*
  Memorandum of Economic and Financial Policies by the authorities of Honduras*
  Technical Memorandum of Understanding*

  *Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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November 20, 2014

REQUEST FOR A STAND-BY ARRANGEMENT AND AN ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY

EXECUTIVE SUMMARY

Background. The government of President Hernandez inherited a difficult macroeconomic situation upon taking office in January 2014. Economic growth decelerated significantly in 2013, driven mainly by lower private demand from policy uncertainty and by weaker trade-partner growth. The fiscal accounts weakened considerably in 2011–13, reflecting sizeable increases in government spending and in the deficit of the state-owned electricity company. The relaxation of fiscal policy has led to a rapid increase in public debt, which would continue into the medium term absent a change in economic policies. The balance of payments position has also weakened over the last three years, reflecting both expansionary macroeconomic policies and a less favorable terms of trade.

Key program features. The program would seek to preserve macroeconomic stability by strengthening the public finances and the external sector position. A multi-year arrangement would be required to give time for a major fiscal consolidation that would contain the rapid growth of public debt and the implementation of a broad structural reform agenda. With substantial revenue measures adopted in December 2013, the program would focus on reducing expenditure and lowering electricity sector losses; improving tax administration; strengthening the monetary and fiscal frameworks; and improving the conditions for sustainable inclusive growth to support poverty reduction.

Program modalities. The authorities have requested a precautionary, three-year Stand-By Arrangement (SBA) and an arrangement under the Standby Credit Facility (SCF). Access under the program would be 100 percent of quota (SDR 129.5 million). SDR 38.85 million will be available upon Board approval of the SBA/SCF arrangements and the remainder in six varying tranches upon completion of semi-annual program reviews.

Approved By
Robert Rennhack (WHD) and Mary Goodman (SPR)

Discussions took place in Tegucigalpa during September 2–12 and at Headquarters during September 29–October 3. The staff team comprised L. Abrego (Head), P. Druck, F. Amui (all WHD), J. Kapsoli and N. Novta (both FAD), M. Appendino (SPR), and M. Dehesa (Resident Representative).

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BACKGROUND AND RECENT ECONOMIC DEVELOPMENTS

1. **The government that took office in January 2014 has vowed to reduce macroeconomic imbalances, promote inclusive economic growth, and improve domestic security.** Fiscal imbalances widened and public debt rose markedly during 2011–13 while the external position weakened. The government of President Hernandez has stressed its commitment to improve economic policy management. It views a Fund-supported program as key to bolstering confidence, facilitating the implementation of fiscal consolidation and structural reforms, and catalyzing external budget support. The government does not have a congressional majority, but has been working with a major opposition party to approve legislation. The authorities have also been taking important steps to improve security and reduce Honduras' high crime rates.

2. **The authorities have adopted several measures aimed at strengthening the public finances and advancing structural reforms.** A substantial package centered on revenue measures was approved by congress in December 2013. The package also included measures to reduce expenditures, freeze transfers to other public entities and lower electricity subsidies, all of which are being implemented and supported by measures to improve discipline in the budget process. The government has also increased efforts to strengthen tax administration and reduce evasion. These fiscal measures have been followed by the approval of legislation to reform the electricity sector and pension funds, which are also being implemented. On the monetary side, a law to recapitalize the central bank (BCH) was also approved and is under implementation.

3. **Performance under the last Fund-supported program was uneven**. Only two out of five program reviews were completed under the previous SBA/SCF arrangements (October 2010–March 2012). The program went off-track in late 2011 owing to expenditures overruns by the central government and growth of monetary aggregates higher than envisaged in the program. However, progress was made in several key areas, particularly in reducing the public sector wage bill and in pension reform. As part of the program, the authorities also moved from a fixed exchange rate to the current crawling-peg regime in mid-2011. As indicated below (¶ 11-12), the current authorities are strongly committed to restoring fiscal discipline and have opted for frontloading fiscal adjustment to minimize implementation risks. They are also committed to managing monetary policy proactively to keep growth of monetary aggregates in check, and continue strengthening and modernizing their operational framework (¶ 16–17).

4. **Macroeconomic developments have been broadly in line with the 2014 Article IV Consultation.** Real economic activity rose by 2.6 percent in the period January-August, compared with the same period last year, consistent with projected GDP growth of 3 percent for 2014. Effects from ongoing fiscal consolidation have been offset by more favorable external conditions and increased private investment related to the dissipation of political uncertainty (from last year's elections) and improved confidence. Driven by the December 2013 tax measures and weather-related factors, inflation increased to 6¼ percent year-on-year in

October (4.6 percent in the previous year), broadly in line with the staff's end-year projection of 6½ percent. The balance of payments has shown signs of strengthening, with an improving trade balance, solid growth of remittances, and higher international reserves.

5. **Growth of monetary aggregates remains moderate, but the real exchange rate has appreciated.** The BCH has kept the policy rate and reserve requirements unchanged while withdrawing liquidity through open market operations (the stock of BCH paper increased by 30 percent since December 2013), helping keep credit growth at about 10 percent (y/y). In the year ending September, the BCH allowed the lempira to depreciate by about 3 percent, which resulted in a small appreciation in real effective terms.

6. **The fiscal position has strengthened, but tax revenue has underperformed.** The combined public sector (CPS) deficit declined to 1.0 of GDP in January-August, from 3.3 percent of GDP in the same period last year. The improvement reflects higher revenue from the December 2013 measures and a reduction in primary spending. However, tax revenue growth has been below expectations and the authorities have revised their 2014 revenue projection downwards by ½ percent of GDP compared to the 2014 Article IV staff report. The underperformance reflects largely weaker-than-expected collections from 2013 income and, to a lesser degree, lower revenue from fuels taxes. The authorities are offsetting the revenue shortfall by reducing expenditure, including via a freeze of central government wages in 2014 (the budget envisaged a 5-percent wage increase).

OUTLOOK AND POLICIES UNDER THE PROGRAM

7. **The government's economic program seeks to preserve macroeconomic stability by strengthening the fiscal and external positions while improving conditions for sustainable inclusive growth.** With high fiscal and external disequilibria and a broad reform agenda, the required macroeconomic adjustment and structural reforms would need to be implemented over several years. A three-year program would provide an appropriate timeframe. On the fiscal side, the program would seek to restore discipline and contain public debt growth, which would require a cumulative adjustment (measured by the change in the CPS primary balance) of 6½ percent of GDP over 2014–2017. About 2 percentage points of this adjustment would take place in 2014, on the back of measures adopted earlier this year. Fiscal consolidation would also help reduce external imbalances. With substantial tax policy measures already adopted, fiscal policy should concentrate on reducing spending, improving tax administration, and lowering the deficit of the state-owned electricity company (ENEE). Monetary policy will have to be managed proactively to keep inflation in check and help strengthen the external position. The pace of exchange rate depreciation would need to be increased to support the external sector and ease the cost of fiscal adjustment. The structural reform program would seek to help bolster the public finances, strengthen the fiscal and monetary frameworks, and—combined with protecting social spending—raise sustainable inclusive growth.

8. **Economic growth is expected to strengthen gradually under the program.** Growth is projected to remain at 3 percent in 2015, supported by more favorable terms of trade, a growth pick-up in the US (Honduras' main trading partner and source of most worker remittances), and a recovering coffee sector from rust-leaf disease (coffee is Honduras' main export product). These factors are expected to offset the dampening effects of fiscal consolidation, especially because the fiscal multiplier is estimated to be relatively modest (around 0.3) given the high degree of openness of the economy. With supportive macroeconomic policies and structural reforms, confidence and the business environment are expected to continue improving, leading to higher private investment. In this context, growth is expected to rise—though slowly—in subsequent years, reaching its estimated potential by 2018. Inflation is expected to decline next year, once the one-off effects from fiscal measures and weather-related factors dissipate, and stabilize at about 5½ percent over the medium term.

9. **A stronger policy mix and improved external conditions are expected to lead to a significant improvement in the external sector position.** The current account deficit is projected to decline to about 5½ percent of GDP over the medium term. The pick-up in economic growth would partially offset the effect of fiscal consolidation on imports but higher private investment and a weaker currency would boost export growth, along with the continued recovery of key trading partners (which would also increase worker remittances) and a more favorable terms of trade. Foreign direct investment is expected to remain high by regional levels, although on a falling trend from recent high levels, as low-cost opportunities for foreign investors gradually decline. International reserves are projected to continue to rise under the program, with reserve coverage reaching about 4 month of imports by 2017.

Honduras: Medium-Term Scenario

				Prel.	Projections					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
	(Annual percent change)									
Output and Inflation										
GDP at constant prices	3.7	3.8	4.1	2.6	3.0	3.0	3.3	3.5	3.7	3.7
Consumer prices (eop)	6.5	5.6	5.4	4.9	6.5	5.8	5.4	5.4	5.4	5.4
	(In percent of GDP, unless otherwise indicated)									
Public Sector										
CPS overall balance	-2.8	-2.8	-4.2	-7.6	-5.9	-3.2	-2.2	-1.8	-1.4	-1.2
CPS primary balance	-3.4	-3.0	-4.3	-7.1	-5.2	-2.1	-0.9	-0.6	-0.3	-0.1
Public sector debt	29.8	32.1	34.4	45.1	47.8	49.4	50.5	50.8	50.5	49.9
External sector										
Current account balance	-4.3	-8.0	-8.5	-9.5	-7.8	-7.1	-6.8	-6.4	-6.0	-5.6
GIR (in months of non maquila imports)	3.6	3.6	3.3	3.7	3.7	3.8	3.8	3.9	4.0	4.1

Sources: Central Bank of Honduras, Ministry of Finance, and Fund staff estimates and projections.

10. **Risks to growth**. Staff views risks to the growth outlook as broadly balanced. Downside risks stem mainly from weaker global growth, while higher private investment, reflecting confidence

effects and improvements in the business climate, could lead to a faster pick-up in economic activity than currently projected. The authorities see staff growth projections as conservative, but were open to exploring measures that could be adopted should downside risks identified by staff materialize. They have suggested that, to the extent that it is allowed by inflation developments and while ensuring that program targets are met, some monetary easing could be feasible to support economic growth and employment, especially given the high levels of market real interest rates.

A. Fiscal Policy

11. **The authorities' fiscal consolidation strategy aims at keeping public debt on a sustainable path.** The authorities are strongly committed to restoring fiscal discipline and containing the growth of public debt, and prefer a frontloaded adjustment to help limit risks (paragraph 21). The program would seek to keep the public debt ratio at about 50 percent of GDP in 2016–2018 and set the basis for its decline in subsequent years. It targets a reduction in the CPS deficit to about 2 percent of GDP (3 percent for the central government) by 2017, with the bulk of the adjustment taking place in 2014–15. This deficit is consistent with declining public debt as a share of GDP, given that the real borrowing costs are low owing to the concessionality of a significant portion of external debt. Achieving these targets would rely mainly on reducing expenditure and strengthening ENEE's finances, in addition to locking in the higher tax revenue from the measures already adopted. The 2015 budget bill submitted to congress in September is consistent with the program targets for next year.

12. **Key elements of the fiscal program include**:

- **Revenue.** The December 2013 tax measures are now expected to increase revenue by 1¾ percent of GDP in 2014–15 (Memorandum of Economic and Financial Policies (MEFP), ¶ 8). The downward revision compared to the 2014 Article IV Staff Report reflects temporarily lower income tax revenue, due mainly to last year's decline in coffee output (losses are carried over a couple of years), and a lower estimated yield from the elimination of tax exemptions. The authorities informed the mission about a legal challenge at the Supreme Court (on constitutional grounds) to one of the tax measures (advance income tax payment, whose yield is estimated at ¼ percent of GDP) adopted in December 2013, and were confident that the Court will uphold the tax.

- The authorities also indicated that, with the government lacking a congressional majority and given the substantial revenue measures already approved, there is not much scope for further tax rate increases during the current administration. They will therefore offset any revenue underperformance, notably in 2014–15, by reducing expenditure. They are also moving forward with the implementation of further measures to strengthen tax administration, partly building on FAD recommendations (MEFP, ¶ 8). These measures are expected to contribute to increasing revenue in the short term. However, the program conservatively assumes that improvements in tax administration will boost revenue only over the medium term.

- **Expenditure.** The authorities plan a substantial reduction in the wage bill over the next three years (MEFP, ¶ 9). They see this as key to create space for social spending and protect public investment while lowering the fiscal deficit. To this effect, the government plans to extend this year's wage freeze to 2015 for all central government employees and limit wage increases to 5 percent annually (somewhat below projected inflation) in 2016–17, including for education and health workers that in the past have enjoyed compensation privileges. In addition, an initiative to reform the public administration and reduce the public sector payroll is already underway. As part of this process, the government has started to eliminate redundant positions in a wide range of public institutions, and plans to continue with this process in 2015 after completing an ongoing public servants' census later this year (structural benchmark, December 2014). The authorities expect these public employment losses to be more than offset through overall job growth in the economy derived from the ongoing growth recovery.

Consolidated Public Sector: Proposed Adjustment

(Change with respect to the previous year; in percent of GDP)

	2014	2015	2016	2017	2014-17
Total primary revenue and grants	**1.5**	**0.1**	**0.5**	**0.3**	**2.3**
Of which					
Tax revenue	1.7	-0.3	0.3	0.2	1.9
Of which					
VAT	1.1	0.0	0.1	0.1	1.3
Income tax	0.2	0.0	0.1	0.1	0.4
Gasoline	0.2	0.0	0.0	0.0	0.3
Operating balance of SOEs	0.1	0.7	0.5	0.2	1.5
Total primary expenditure	**-0.4**	**-3.0**	**-0.7**	**0.0**	**-4.2**
Of which					
Wages and salaries	-0.4	-0.6	-0.4	-0.3	-1.7
Of which					
Cap on CG wage growth	-0.4	-0.3	-0.2	-0.2	-1.2
Goods and services	-0.3	-0.4	-0.1	0.2	-0.5
Capital expenditure	-0.2	-1.7	0.0	0.0	-1.8
Of which					
Fixed capital	-0.3	-1.3	0.1	0.0	-1.4
Adjustment	**1.9**	**3.1**	**1.2**	**0.3**	**6.5**

Source: Fund staff projections.

- The government plans to keep constant in nominal terms transfers to local government and other public entities, and conduct a careful review of the public investment program to ensure that plans are realistic and focus on high priority projects (MEFP, ¶ 9). The authorities have also adopted a mechanism to strengthen controls on various expenditure items, including wages (MEFP, ¶ 9–10). Given the importance of reducing the high wage bill, the program includes an indicative target for this variable.

- **ENEE** (MEFP, ¶ 11)**.** The deficit of ENEE (1.8 percent of GDP in 2013) derives mainly from below-cost electricity tariffs, high technical and non-technical losses (estimated at about 33 percent of ENEE's output), and operational inefficiencies. ENEE's costs have risen rapidly in recent years as reliance of electricity generation on more expensive fuel sources has increased; and electricity tariffs have not kept up with this trend. The program targets a substantial improvement of the financial situation of the company through a series of revenue-enhancing and expenditure reducing measures. The measures aim to restore positive operating margins and eliminate ENEE's overall deficit progressively by 2018. The overall deficit, excluding government transfers, is targeted to be limited to 1.4 and 0.8 percent of GDP in 2014 and 2015, respectively, with concurrent improvement in the operating deficits to 0.9 and 0.2 percent of GDP. To this effect, the reform includes increases in average electricity tariffs equivalent to 12 percent in 2014 before correcting for the reduction in costs arising from recent declines in oil prices and a further increase of 2.5 percent in 2015 to be implemented by the new sector's regulator (CREE) (¶ 20 below, and ¶ 11 and Appendix I of MEFP); these will help raise the annual operating revenue-to-spending ratio to 0.85 by end-2014 and to 0.97 by end-2015. In addition, the program envisages a reduction of 7 percentage points in ENEE's technical and non-technical losses during 2015–17.[1] The authorities also plan to lower ENEE's wage bill by about ¼ percent of GDP (excluding severance payments) from 2015 onward as a result of a reduction in its workforce. One-time severance payments are estimated at about 0.2 percent of GDP and will be offset by higher revenue from lower losses and a small reduction in capital spending.

- **Financing.** Most program financing is expected to come from external sources, mainly the World Bank and the Inter-American Development Bank (IDB). MDBs are expected to disburse about US$920 million (4.5 percent of GDP) during 2014–16 for regular financing. In addition, the authorities expect to receive budget support from the World Bank, IDB, and European Commission totaling about US$220 million in 2014, which would be disbursed following the approval of the Fund arrangements. A substantial portion of the latter resources was allocated to Honduras for 2013–14 but has not been used due to the lack of a Fund-supported program. Budget support is expected to decline starting in 2015, with average annual disbursements of around US$85 million. For 2014, the authorities also expect to contract loans with domestic banks equivalent to US$250 million to help cover ENEE's deficit. The program also envisages tapping international markets for around US$300 million to help meet remaining financing needs in 2015–16.

- **Domestic arrears.** Public sector arrears (which are included in public debt figures) were estimated at about 3 percent of GDP at end-2013. The authorities will conduct an audit of these arrears, with the aim of regularizing them once the audit is completed (MEFP, ¶ 16; structural benchmark, June 2015). Given the program's tight financing, validated arrears will

[1] Losses rose by 8 percentage points in the last four years. The reduction included in the program can thus be seen as being on the conservative side; the authorities believe that they will outperform it, which would provide the program with a cushion from this source.

be settled through bonds. The program envisages that arrears are cleared in 2015, with no net accumulation of domestic arrears during 2014–17.

13. **The authorities are implementing liability management to ease the debt burden.** Their goal is to replace high-interest, short-maturity domestic debt with cheaper and longer-maturity external debt. To this effect, in 2013 the government contracted from the Central American Bank for Economic Integration (CABEI) a US$300 million loan carrying a variable interest rate and 20-year maturity. Under the loan agreement, the government would use the resources to buyback bonds held by pension funds; the latter, in turn, would create a trust fund to invest the proceeds in projects being financed by CABEI. The authorities agreed with staff that these investments could entail risks to pension funds, and plan to strengthen the funds' investment regulations to limit risks (MEFP, ¶ 15). They have also decided not to move forward with plans to request a US$120 million loan augmentation to retire more debt held by pension funds, which would have allowed these institutions to purchase CABEI portfolio.

B. Social Protection

14. **The program envisages safeguarding social spending to support poverty reduction and protect low-income groups from the effects of fiscal adjustment** (MEFP, ¶ 12)**.** The authorities plan to keep spending in key social programs at 1.6 percent of GDP in 2014–15, thus preserving the expansion that these programs experienced in recent years. This will substantially increase the share of social spending in overall primary spending. The government plans to use part of this spending on improving housing for low-income families under their recently-established *Vida Mejor* program, which will consolidate existing social programs (notably the conditional cash-transfer program *Bono 10 mil*). The fiscal program envisages allocating part of the savings from reductions in the wage bill to *Vida Mejor*. The government is in the process of conducting a thorough review of their social programs, with the aim of improving their targeting. The authorities are also implementing a subsidy scheme for families with monthly electricity consumption below 75KW, which protect them from increases in electricity tariffs. The fiscal program envisages a floor on social expenditure.

15. **The government plans to reform the pension and healthcare systems to increase coverage** (MEFP, ¶ 13). The reform aims at gradually moving toward universal pension and healthcare coverage while adhering to the fiscal targets envisaged under the program. Draft legislation providing for this reform was submitted to congress in September. To fit the reform costs into the program's fiscal targets and maintain intertemporal sustainability, the authorities will amend the draft legislation before bringing it to discussion in congress. With assistance from the World Bank and the IDB, the authorities will also revise the design of the safety net included in the draft legislation to improve its efficiency while keeping costs at fiscally-affordable levels.

C. Monetary and Exchange Rate Policies

16. **Monetary policy remains broadly appropriate.** Credit growth remains moderate, following the tightening of monetary conditions during 2012–13 and continued liquidity withdrawal by the BCH during 2014. The BCH plans to keep liquidity (net domestic assets) in line with the monetary program and international reserve targets. This will require maintaining the policy rate above projected inflation while allowing the yields on BCH paper to rise as needed (MEFP, ¶ 17). The program envisages a zero limit on BCH lending to the non-financial public sector, as well as providing no new financing to Banhprovi—a second-tier bank serving construction and agriculture—beyond that approved under the 2013 trust fund. The authorities plan to phase out during the program period banks' use of government bonds to meet a portion of reserve requirements.

17. **The central bank plans to continue strengthening the monetary policy framework** (MEFP, ¶ 18 and 20). A multi-year program to recapitalize the BCH is being implemented starting this year. The fiscal program provisions for the recapitalization of the BCH through non-negotiable bonds bearing a positive real interest rate—in line with the recapitalization law. Following IMF recommendations, the BCH has adopted a plan to modernize its policy framework, including by improving short-term liquidity management and enhancing the reporting of monetary and economic data necessary for decision making by the monetary policy committee.

18. **The authorities will allow for increased exchange rate flexibility within the current regime, and plan to take steps to move to a more flexible system over the medium term** (MEFP, ¶ 19)**.** Estimates based on the CGER approach suggest a slight overvaluation of the lempira (7–10 percent), which depreciated by about 2½ percent during the year following the BCH modification of the exchange rate inner band in mid-2013. The BCH envisages an increase in the pace of currency depreciation, starting in the last quarter of 2014. This would allow for a small depreciation in real effective terms after 2014 and a gradual correction of relative prices. This relatively modest change is expected to have only a limited impact on inflation and banks' balance sheets. As pointed out in the 2014 Article IV Staff Report (where results from stress testing following a hypothetical sizeable currency depreciation are reported), banks would be able to handle the rate of depreciation envisaged in the program, with very limited impact on their capital levels. The authorities also agreed to the gradual removal of FX surrender requirements (structural benchmark, December 2015). This should further increase exchange rate flexibility and foster the development of an interbank FX market.

D. Financial Sector

19. **Financial soundness indicators look generally strong, but currency mismatches by borrowers remain a source of risk in the banking system.** Banks are well-capitalized and non-performing loans are low and fully provisioned. However, about one-third of bank deposits and lending is in foreign currency, and mismatches are significant, with about 45 percent of

foreign currency credit going to unhedged borrowers. The authorities have imposed higher capital requirements on this type of lending, but without much success in terms of reducing mismatches. The authorities plan to increase efforts to discourage foreign-currency borrowing by unhedged agents by formally setting more stringent loan-to-value and debt service-to-income ratios for unhedged borrowers (MEFP, ¶ 21). Thus far, banks have had full discretion in setting limits on these ratios, with practice varying significantly across institutions. The authorities also plan to resume publication of the financial stability report in early 2015. They are in the process of adopting new AML/CFT legislation in line with the 2012 FATF standard (a bill was submitted to congress in early 2014, MEFP, ¶ 21) as part of wider efforts to combat crime.

E. Structural Reforms

20. **Structural reforms are expected to play a crucial role in supporting fiscal consolidation, strengthening fiscal management, and improving prospects for economic growth.** Key components of the reform program include (more details are provided in Appendix I of the MEFP):

- **Electricity sector.** The authorities are implementing the electricity sector reform approved by congress in early 2014. The reform would allow private participation in the key area of distribution and is expected to improve electricity-tariff setting and pave the way for the elimination of untargeted subsidies. A new independent regulator is being established and is expected to start work before year-end and become fully operational by March 2015 (MEFP, ¶ 22). With assistance for the IDB and the World Bank, the authorities are also in the process of seeking investors to take charge of the transmission and distribution segments through long-term concessions.

- **Telecommunications company (HONDUTEL)**. The authorities plan to have HONDUTEL managed by a private investor under a long-term concession contract (MEFP, ¶ 23). HONDUTEL has become uncompetitive in a sector dominated by private companies, and could become a burden to the budget were it to continue to be managed by the state. The government is in the process of restructuring the company, including by laying off redundant staff, in order to prepare it for private management. It is aiming at having a concession in place by March 2015.

- **Pension funds**. The reform of the public employees' pension fund (approved by congress in January in 2014) is now being implemented. The reform includes parametric changes (contribution rates, retirement age, and minimum years of services) and improvements in the fund's governance. The authorities plan to reform the Honduran Social Security Institute (provider of pension coverage for the private sector and a major provider of healthcare in the country) in order to strengthen its governance and reduce its actuarial deficit. A reform bill is being submitted to congress in March 2015 for its approval by June 2015 (structural benchmarks). The authorities also plan to strengthen pension fund regulations governing investment decisions to limit risks, including from investing in CABEI-financed projects.

- **Public-private partnerships (PPPs).** The authorities plan to reform the PPP legal framework, with the aim of limiting fiscal risks and costs from these arrangements. The reform (structural benchmark, December 2014) would give the ministry of finance a leading role in project evaluation and approval, including the power to stop projects that may jeopardize fiscal sustainability or do not provide good value for money (MEFP, ¶ 26). It will also strengthen the government's capacity to assess and quantify PPP-related risks, including by creating a special unit at the finance ministry. The authorities also plan to repeal legislation approved in early 2014 that allows issuing government guarantees for debt contracted by private companied involved in PPP projects (MEFP, ¶ 26; structural benchmark, December 2014).

- **Tax administration** (MEFP, ¶ 8). With Fund technical assistance, the National Tax Directorate (DEI) is implementing a program to strengthen tax administration, focused on the following areas: (i) *Large Taxpayer Unit (LTU)*. The government plans to bolster the LTU, notably by hiring new qualified personnel (structural benchmark, September 2015), as well as to increase the coverage of risk-based audits for large taxpayers. *(ii) Tax intelligence and risk analysis unit*. To streamline operations in this unit, the authorities will standardize information and introduce an adequate technology platform (data warehouse). *(iii) Customs.* Operational management within customs will be improved to facilitate controls, information sharing, and speed up processes. DEI is also in the process of revising procedures to improve control of fuel imports, with the goal of having a new system in place by March 2015.

PROGRAM RISKS

21. **Risks to the program derive mainly from potential slippages in the implementation of fiscal measures, and from less favorable external conditions**.

- **Fiscal area.** There may be strong resistance to measures to reduce the wage bill, and to those to lower ENEE's deficit. Implementation of these measures could become more difficult as the 2017 elections approach. To limit these risks, the program envisages frontloading these actions, especially raising electricity tariffs and reducing ENEE's payroll. The program's relatively conservative assumption on the reduction of losses would also provide some safeguard. There is also the risk that costs related to the reform of the safety net turn out higher than anticipated by the authorities.

- **Financing.** Potential delays in external disbursements for budget support this year could put at risk meeting fiscal and the international reserves targets. Similarly, negative developments in international financial markets could make it difficult to access private markets to meet program financing needs.

- **Trading-partner growth.** Slower growth in the U.S. and Europe would weaken domestic activity, which could affect government revenues and complicate the achievement of fiscal targets. It could also lead to weaker-than-projected exports and remittances, but imports would also adjust, helping protect the external sector position as it occurred during the 2008–09 global crisis.

- **Political factors.** Structural reforms that require legislative approval could face difficulties given that the government lacks a majority in congress.

22. **Additional policy measures would be needed if any of these risks were to materialize.** The authorities are committed to the adoption of any measures required to protect the program's targets. They see frontloading of key fiscal measures as crucial to limit risks from the political cycle. With good program implementation, they also view excess liquidity in domestic markets as a potential source of additional financing should conditions in external capital markets deteriorate and preclude access. A response to weaker growth could be along the lines described in paragraph 10. The authorities are committed to amending the safety net bill to minimize costs and to the gradual implementation of the reform to protect the program's fiscal targets. The government is also confident that it will be able to continue working with congress on the approval of legislation required for program implementation.

PROGRAM MODALITIES

23. **Program duration, conditionality and reviews.** A 36-month Fund-supported program would provide an appropriate timeframe to support the implementation of the envisaged sizable fiscal consolidation and broad structural reform agenda. Conditionality focuses on macro-critical areas and includes prior actions, structural benchmarks in several policy areas, and semi-annual quantitative performance criteria (Tables 11–12).

24. **Facility**. Honduras is a presumed blender. Consistent with the blending policy, concessional and GRA resources are normally used in equal proportions and the concessional portion does not exceed an annual average of 50 percent of quota. Since SCF arrangements cannot go beyond 2 years, the third year of the Fund-supported program would use only GRA resources.

25. **Access and phasing.** With no balance of payments gaps remaining, staff proposes an access level somewhat below the norm for a fully concessional arrangement (100 percent of quota, or SDR129.5 million). In the absence of protracted balance of payments problems and considering their implementation of stable and sustainable macroeconomic policies consistent with strong and durable poverty reduction, the authorities plan to treat the current SBA/SCF arrangements as precautionary, partly to limit costs to the central bank, which—as indicated above—is being recapitalized. Given a relatively modest reserve coverage, the proposed access would provide an adequate cushion in case of negative exogenous shocks (external economic developments or shocks to the agricultural sector) affecting the balance of payments. Access would be somewhat frontloaded—with Honduras having no outstanding credit in the GRA, the first purchase from that account must be at least 25 percent of quota (the first credit tranche, which is not subject to phasing or performance criteria). This would bring total access in the first year to 40 percent of

quota. The remainder would be available in semi-annual tranches over the next two years, upon conclusion of program reviews (Table 13).

26. **Capacity to repay the Fund.** Honduras has a strong capacity to repay the Fund. Its current obligations to the Fund are low (SDR 5.1 million, end-September 2014), the proposed access would not affect significantly the level of total external debt (36 percent of GDP at end-2013), and the risk of debt distress is moderate according to an updated debt sustainability analysis. (Appendix I).

27. **Safeguards assessment**. The last safeguards assessment was completed in March 2011. An assessment update would take place before the first program review, as required by the Fund's safeguards assessment policy.

STAFF APPRAISAL

28. **Macroeconomic performance has shown clear signs of improvement in 2014.** The fiscal accounts have strengthened on the back of the December 2013 tax reform and subsequent measures adopted by the government to reduce spending. The external sector position has improved, with a narrowing current account deficit and higher international reserves. Economic activity has also been strengthening, driven by higher confidence and more favorable external conditions, factors that have offset the effects of ongoing fiscal consolidation.

29. **The authorities are strongly committed to restoring fiscal discipline and implementing structural reforms.** The government of President Hernandez is implementing substantive fiscal measures both on the revenue and expenditure side—including the significant increases in tax rates adopted by the previous administration and reductions in the wage bill—to bolster the public finances. It is committed to further reducing current spending and strengthening tax administration to continue supporting revenue growth. The authorities have also begun implementing key structural reforms in the electricity and pension sectors, and to strengthen the fiscal policy and monetary frameworks. In addition to supporting the adjustment effort, some of these reforms are expected to help raise overall efficiency and support long-run economic growth.

30. **Sustained fiscal consolidation will be key to continued improvements in macroeconomic performance.** Continued fiscal consolidation is a condition for containing public debt growth and maintaining the sustainability of the public finances. It is also key to further bolster investor confidence and help raise private investment to support long-run economic growth and employment. Fiscal adjustment will also help lower external sector imbalances and buttress international reserves.

31. **Monetary and exchange rate policy will be crucial to strengthen the external sector**. The central bank is committed to ensuring that growth of monetary aggregates remains moderate to support fiscal efforts to bolster the external position and help meet the program's

monetary and international reserve targets. The ongoing implementation of the recapitalization of the BCH is necessary to strengthen the operational framework of monetary policy. Increased exchange rate flexibility would also be important to bolster the balance of payments position, protect competitiveness, and ease the costs of fiscal adjustment. A more flexible exchange rate arrangement should also be part of the authorities' strategy to strengthen the monetary framework over the medium term.

32. **The authorities program also seeks to address the main financial sector risks**. Bank financial soundness indicators remain generally strong. Dollarization has been rising but remains moderate. Currency mismatches on the side of borrowers are, however, significant and constitute the main source of risk in the banking system. The authorities' measures to discourage foreign currency borrowing by undhedged agents by making lending conditions to them more stringent should help lower this risk.

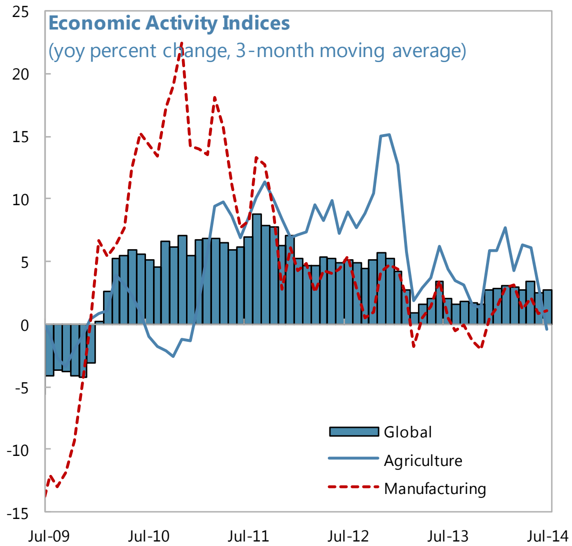
33. **Fiscal consolidation needs to accommodate the need to protect social spending and public investment.** Honduras remains one of the poorest countries in the region and needs to continue to press ahead with efforts to lower the poverty rate. The authorities' economic program seeks to protect key social programs and free up resource for anti-poverty spending. The government's plans to reform and widen the safety net are also welcome in this respect. However, it is important to ensure that they are fiscally sustainable. In this regard, it is essential that the social protection bill recently submitted to congress is amended to limit its costs, safeguard the fiscal program's targets, and make the reform sustainable over time. Changing the composition of expenditure away from current outlays is also necessary to protect public investment and support long-run growth.

34. **The program is subject to several risks.** Program risks derived mainly from possible slippages in the implementation of measures to reduce the wage bill and strengthen the electricity sector, and from less favorable external conditions. The latter could hurt domestic growth, affecting revenue collections and the fiscal targets. The authorities are committed to adopting necessary measures if any of these risks materialize, and to ensuring that the fiscal costs from the social protection reform fit into the program's targets and are consistent with intertemporal sustainability.

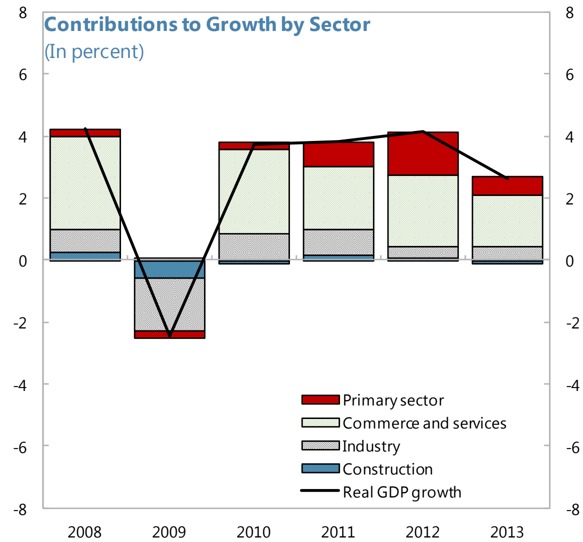
35. **Given the strength of the authorities' economic program, staff supports their request for SBA/SCF arrangements for SDR129.5 million**.

Figure 1. Honduras: Recent Developments

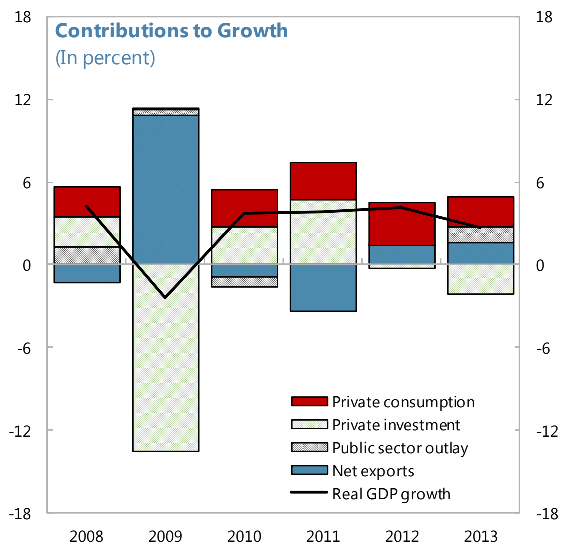
Economic activity has started to pick up in 2014….



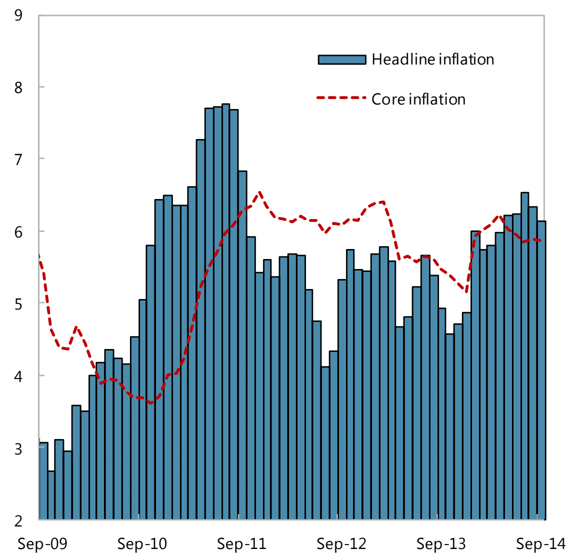
…after softening last year, driven by shocks to agriculture and weaker growth in services…



…and lower private consumption.



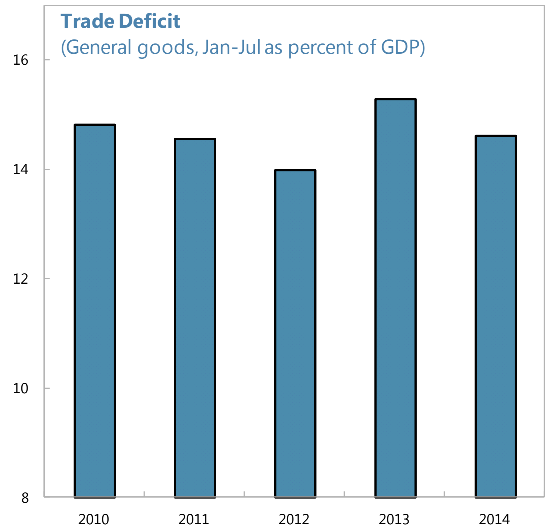
Inflation has risen in 2014, mainly as a result of the December 2013 tax measures.



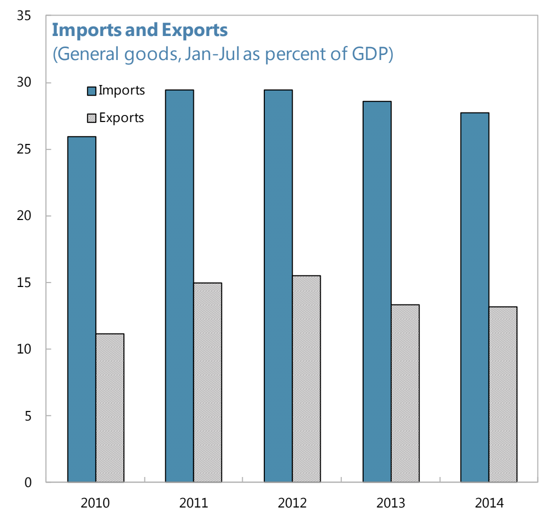
Sources: Central Bank of Honduras, Ministry of Finance, and Fund staff estimates and projections.

Figure 2. Honduras: External Sector Developments

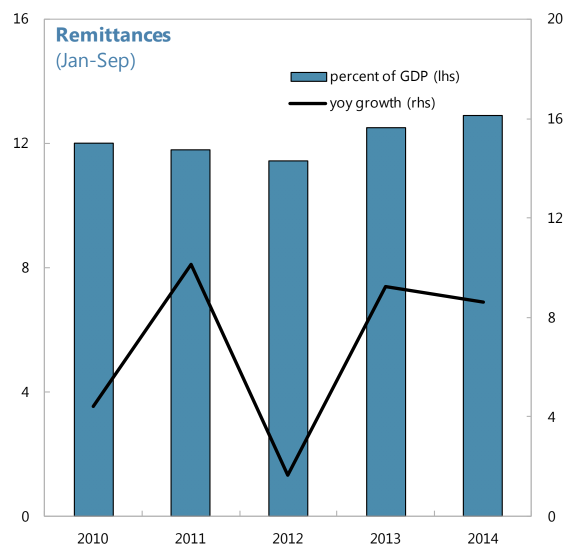
The trade balance improved in the first months of 2014…



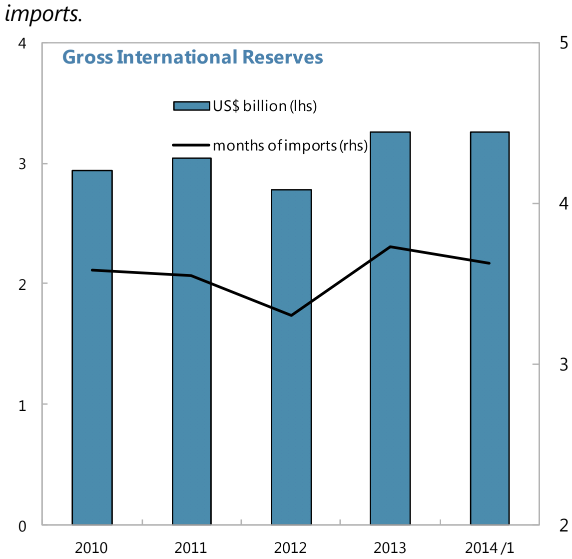
…driven by a decline in imports.



Remittances continued to grow strongly in 2014, but remain below pre-crisis levels.



Gross international reserves have increased so far in 2014 and reserve coverage remains above 3.5 months of imports.

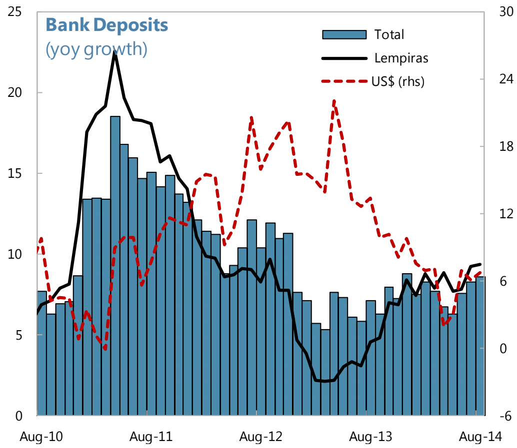


Sources: Central Bank of Honduras and Fund staff estimates and projections.

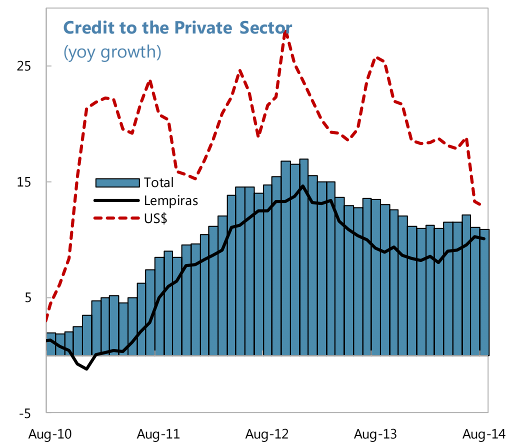
1/ 2014 Data as of October 6.

Figure 3. Honduras: Monetary Developments

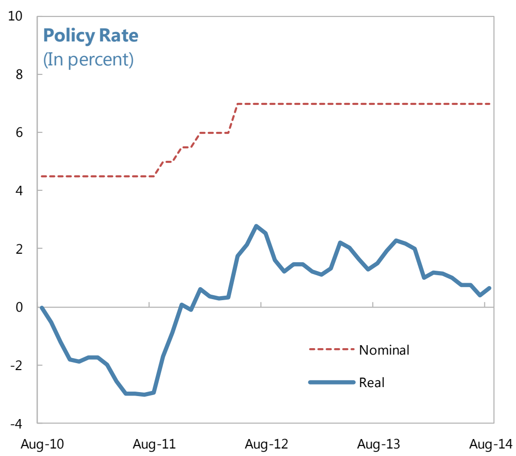
Deposits growth has picked up in recent months...



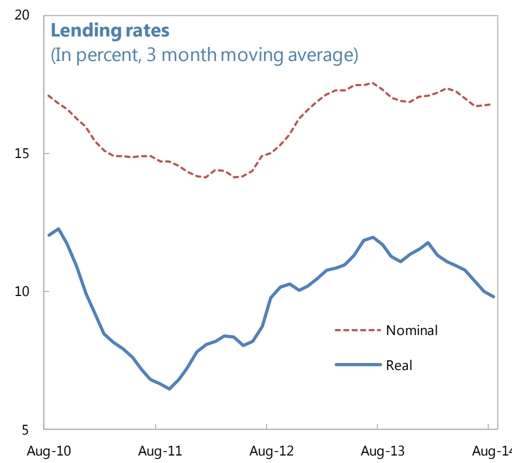
...while growth of credit to the private sector has remained broadly stable.



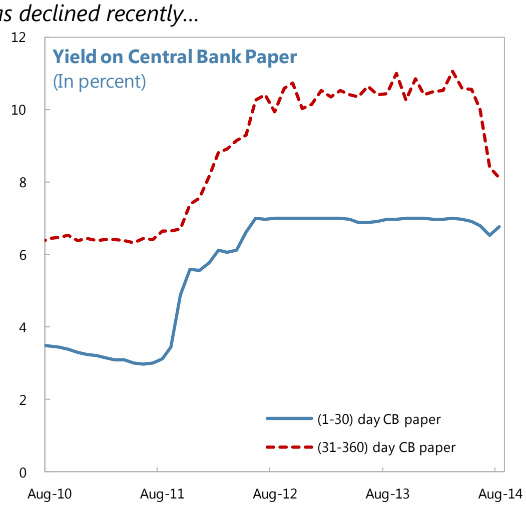
The policy rate has remained unchanged...



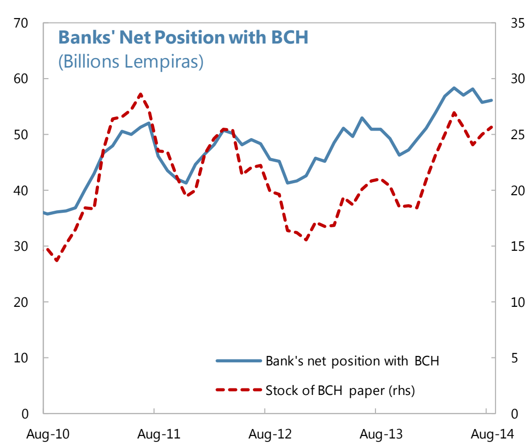
...and nominal lending rates have stayed broadly stable.



Although yield on central bank paper for longer maturities has declined recently...



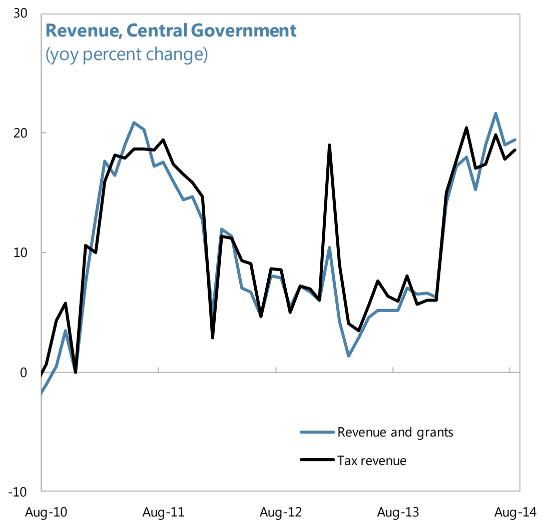
...the central bank has continued to mop up liquidity.



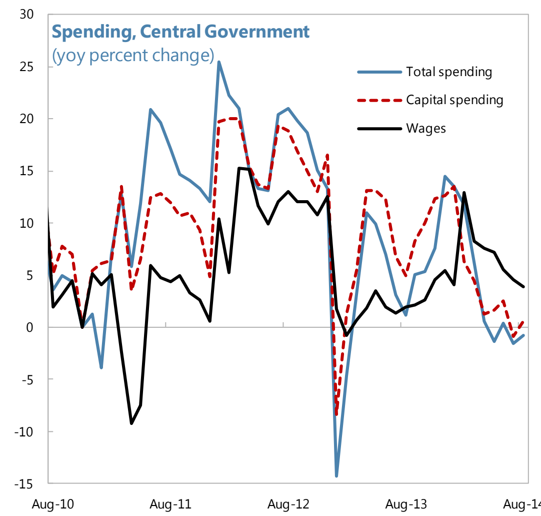
Sources: Central Bank of Honduras and Fund staff estimates and projections.

Figure 4. Honduras: Fiscal Developments

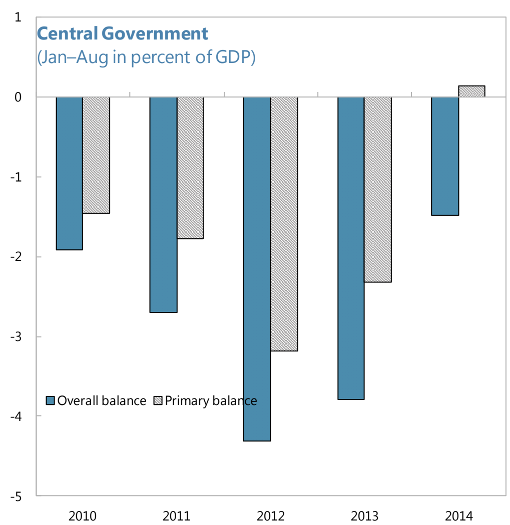
Higher revenues from the December 2013 measures....



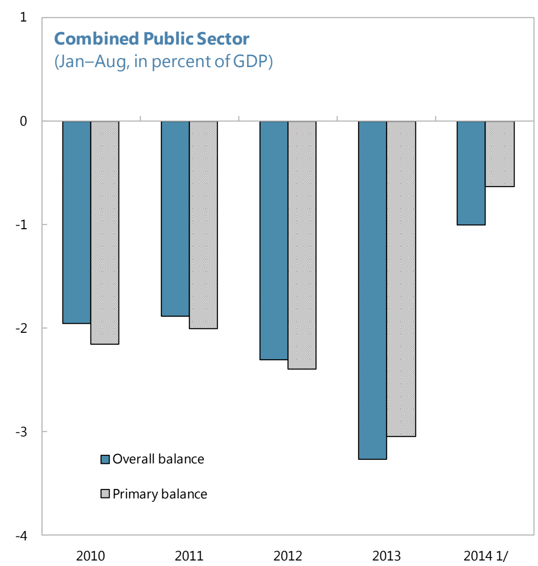
...and tighter control on spending....



...led to significant deficit reduction by the central government...



...and the combined public sector through August.



Sources: Ministry of Finance and Fund staff estimates and projections.

Table 1. Honduras: Selected Economic Indicators

I. Social Indicators

Population (2013)	8.1 million	Life expectancy at birth in years (2011)	73
Per capita income in U.S. dollars (PPP, 2012)	4,194	Adult literacy (ages 15 and above, 2010)	84.8 percent
Rank in UNDP Development Index (2012)	120 of 186	Percent of pop. below poverty line (2011)	61.9
Unemployment rate (2012)	3.6	Gini index (2010)	57
Underemployment rate (2012)	54.1	Oil imports (2013)	US$2.1 billion
Net FDI (as percent of GDP, 2013)	5.0	Main exports: coffee, bananas, palm oil, and maquila.	

II. Economic Indicators

				Prel.	Projections	
	2010	2011	2012	2013	2014	2015
	(Annual percentage change, unless otherwise indicated)					
National income and prices						
GDP at constant prices	3.7	3.8	4.1	2.6	3.0	3.0
GDP deflator	4.7	7.8	3.6	1.5	5.3	5.7
Consumer prices (eop)	6.5	5.6	5.4	4.9	6.5	5.8
Consumer prices (average)	4.7	6.8	5.2	5.2	6.2	5.6
Money and credit						
Private sector credit	3.5	9.6	16.9	11.2	9.9	10.5
Broad money	9.4	12.7	6.6	8.4	10.2	10.6
Lending rate (eop, in percent) 1/	15.1	14.2	16.7	16.9	16.9	...
Deposit rate (eop, in percent) 1/	8.0	7.4	11.4	11.0	9.9	...
	(In percent of GDP, unless otherwise indicated)					
Investment and saving						
Gross domestic investment	**21.6**	**24.4**	**24.4**	**25.6**	**25.6**	**25.3**
Private sector	18.2	21.1	21.4	21.9	22.3	22.9
Public sector	3.3	3.4	3.0	3.6	3.3	2.4
Gross national savings	**17.2**	**16.5**	**15.8**	**16.0**	**17.7**	**18.2**
Private sector	16.6	15.4	16.4	18.7	18.7	18.0
Public sector	0.6	1.1	-0.5	-2.7	-1.0	0.2
Balance of payments						
External current account balance	-4.3	-8.0	-8.5	-9.5	-7.8	-7.1
Exports, f.o.b. (annual percentage change)	29.8	27.3	4.8	-6.6	4.7	3.9
Imports, f.o.b. (annual percentage change)	20.8	24.9	2.2	-3.7	3.2	3.4
GIR (In months of imports) 2/	3.6	3.6	3.3	3.7	3.7	3.8
Net International Reserves (millions of dollars)	2,082	2,032	1,665	2,211	2,271	2,411
Terms of Trade (annual percent change)	-7.3	1.5	-1.1	-2.5	2.8	1.7
Real effective exchange rate (eop, depreciation -) 1/	4.3	1.8	-1.7	0.4	1.2	...
Combined public sector						
Primary balance	-3.4	-3.0	-4.3	-7.1	-5.2	-2.1
Overall balance	-2.8	-2.8	-4.2	-7.6	-5.9	-3.2
Public sector debt	**29.8**	**32.1**	**34.4**	**45.1**	**47.8**	**49.4**

Sources: Central Bank of Honduras, Ministry of Finance, and Fund staff estimates and projections.

1/ 2014 data as of August.

2/ Based on following year's imports of goods and services, excluding maquila.

Table 2. Honduras: Operations of the Central Government

(In percent of GDP)

		Prel.	Proposed Program					
	2012	2013	2014	2015	2016	2017	2018	2019
Total revenue and grants	**16.7**	**17.0**	**18.8**	**18.4**	**18.5**	**18.7**	**18.7**	**18.6**
Current revenue	15.7	16.3	17.9	17.6	17.9	18.1	18.2	18.2
Tax revenue	14.8	15.1	16.8	16.5	16.8	17.0	17.1	17.1
Nontax revenue	1.0	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Capital revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	1.0	0.8	0.9	0.8	0.6	0.5	0.4	0.4
Total expenditure	**22.7**	**24.9**	**24.3**	**22.4**	**21.9**	**21.5**	**21.2**	**21.1**
Current expenditure	18.3	19.8	19.3	18.7	18.3	18.0	17.4	17.4
Wages and salaries	9.6	9.7	9.3	8.8	8.5	8.2	8.0	8.0
Goods and services	2.7	3.0	2.5	2.3	2.2	2.4	2.2	2.2
Transfers	4.3	4.9	4.8	4.6	4.4	4.1	3.9	3.9
Interest payments	1.7	2.3	2.6	3.0	3.2	3.4	3.3	3.3
External	0.3	0.5	0.9	1.0	1.1	1.2	1.2	1.2
Domestic	1.3	1.7	1.7	2.0	2.1	2.2	2.1	2.1
Other current expenditure	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	4.2	5.2	4.8	3.7	3.6	3.5	3.8	3.7
Fixed capital formation	1.6	2.5	1.7	1.1	1.2	1.1	1.4	1.3
Transfers	2.7	2.7	3.1	2.6	2.4	2.4	2.4	2.4
Net lending	0.1	-0.1	0.2	0.0	0.0	0.0	0.0	0.0
Overall balance	**-6.0**	**-7.9**	**-5.5**	**-4.0**	**-3.4**	**-2.9**	**-2.6**	**-2.4**
Financing	**6.0**	**7.9**	**4.3**	**2.6**	**2.4**	**2.6**	**2.6**	**2.4**
External financing	**2.1**	**8.4**	**1.5**	**1.4**	**0.7**	**0.8**	**1.1**	**0.7**
Disbursements	2.4	3.2	2.0	2.0	1.3	1.6	2.0	2.0
Amortization	-0.4	-0.3	-0.6	-0.7	-0.6	-0.8	-0.9	-1.3
Bond issues	0.0	5.4	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing 1/	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0
Domestic financing	**4.2**	**-0.1**	**3.4**	**1.7**	**2.2**	**2.2**	**1.9**	**2.1**
Financial system	0.7	-1.2	2.2	0.6	0.6	0.5	0.5	0.5
Central bank	-0.2	-1.5	1.7	0.0	0.0	0.0	0.0	0.0
Rest of the financial system	0.9	0.3	0.5	0.6	0.6	0.5	0.5	0.5
Bonds outside the financial system	1.0	0.7	1.1	3.1	0.9	0.9	0.8	1.1
Floating debt/arrears 2/	2.6	0.4	0.0	-2.2	0.0	0.0	0.0	0.0
PPPs	0.0	0.0	0.1	0.2	0.7	0.8	0.6	0.5
Adjustment for HIPC/MDRI debt relief 3/	-0.5	-0.4	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4
Statistical discrepancy	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Financing Gap	**0.0**	**0.0**	**1.1**	**1.4**	**0.9**	**0.3**	**0.0**	**0.0**
Official budget support	...	...	1.1	0.5	0.4	0.3	0.0	0.0
Eurobonds	...	...	0.0	0.9	0.5	0.0	0.0	0.0
Memorandum items								
Primary balance	-4.3	-5.6	-2.9	-1.0	-0.1	0.5	0.8	0.9
Gross total debt	37.8	46.5	49.0	50.9	52.9	53.5	53.5	53.6
Excluding BCH recapitalization	...	...	48.2	49.6	51.0	51.1	50.9	50.6
Arrears 2/	2.2	2.6	2.4	0.0	0.0	0.0	0.0	0.0
Nominal GDP (in billions of lempiras)	361.3	376.3	408.2	444.3	480.1	520.6	565.1	613.4

Sources: Honduran authorities, Fund staff estimates and projections.

1/ Includes debt forgiveness, accumulation, rescheduling, payment and/or forgiveness of arrears.

2/ Wage and suppliers arrears and other unsettled payments.

3/ Offsets the HIPC/MDRI debt relief accounted as grants.

Table 3. Honduras: Operations of the Combined Public Sector[1/]

(In percent of GDP)

	2012	Prel. 2013	Proposed Program 2014	2015	2016	2017	2018	2019
Total revenue and grants	**22.5**	**22.9**	**24.5**	**24.6**	**25.1**	**25.5**	**25.6**	**25.7**
Current revenue	21.3	21.7	23.2	23.6	24.4	24.8	25.0	25.2
Tax revenue	15.3	15.6	17.3	17.0	17.3	17.5	17.6	17.6
Nontax revenue	5.0	5.5	5.1	5.0	5.0	5.0	5.0	5.0
Interest earnings 2/	1.4	1.5	1.7	1.7	1.7	1.8	1.8	1.8
Operating balance of public enterprises	-0.3	-1.0	-0.8	-0.1	0.4	0.5	0.7	0.8
Capital revenue	0.2	0.4	0.2	0.2	0.2	0.2	0.2	0.2
Grants	1.0	0.8	1.1	0.8	0.6	0.5	0.4	0.4
Total expenditure	**26.7**	**30.4**	**30.4**	**27.8**	**27.3**	**27.3**	**27.1**	**27.0**
Current expenditure	21.9	24.4	24.2	23.3	22.7	22.7	22.2	22.2
Wages and salaries	11.9	12.8	12.4	11.8	11.4	11.1	10.9	10.9
Goods and services	4.0	4.4	4.1	3.8	3.7	3.9	3.7	3.7
Transfers	3.1	3.5	3.8	3.5	3.3	3.3	3.3	3.3
Operating losses of the central bank	0.5	0.5	0.5	0.4	0.4	0.3	0.3	0.3
Interest payments	1.3	2.0	2.4	2.8	3.0	3.1	3.0	2.9
External	0.4	0.5	0.9	1.0	1.1	1.2	1.2	1.2
Domestic	0.9	1.5	1.4	1.8	1.9	1.9	1.8	1.7
Other	1.2	1.2	1.0	1.0	1.0	1.0	1.0	1.0
Capital expenditure	5.5	6.4	6.2	4.5	4.6	4.6	4.8	4.8
Fixed capital formation	3.7	5.1	4.8	3.5	3.7	3.7	3.9	3.9
Transfers	1.8	1.2	1.4	1.0	0.9	0.9	0.9	0.9
Net lending	-0.7	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	**-4.2**	**-7.6**	**-5.9**	**-3.2**	**-2.2**	**-1.8**	**-1.4**	**-1.2**
Financing	**4.8**	**8.0**	**5.3**	**2.3**	**1.7**	**1.9**	**1.9**	**1.7**
External financing	**2.4**	**8.4**	**1.9**	**1.8**	**1.0**	**1.0**	**1.0**	**0.7**
Disbursements	2.8	3.2	2.5	2.5	1.7	2.0	2.2	2.0
Amortization	-0.4	-0.3	-0.6	-0.7	-0.7	-1.0	-1.2	-1.4
Bond Issues	0.0	5.4	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing 3/	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Domestic financing	**2.4**	**-0.4**	**3.4**	**0.5**	**0.7**	**0.9**	**0.9**	**1.0**
Financial system	0.7	-0.3	3.3	0.4	-0.1	0.1	0.2	0.3
Central bank	0.7	-1.0	2.2	0.4	0.4	0.3	0.3	0.3
Rest of the financial system	0.0	0.7	1.1	0.0	-0.5	-0.3	-0.1	0.0
Bonds outside the financial system	-0.1	0.0	0.0	2.6	0.0	0.0	0.0	0.0
Floating debt/arrears 4/	1.7	-0.1	0.0	-2.6	0.0	0.0	0.0	0.0
PPPs	0.0	0.0	0.5	0.3	0.8	0.9	0.7	0.7
Other	0.0	0.0	-0.4	-0.2	0.0	0.0	0.0	0.0
Adjustment for HIPC/MDRI debt relief 5/	-0.5	-0.4	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4
Statistical discrepancy	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Extraordinary financing	**0.0**	**0.0**	**1.1**	**1.4**	**0.9**	**0.3**	**0.0**	**0.0**
Official budget support	…	…	1.1	0.5	0.4	0.3	0.0	0.0
Eurobonds	…	…	0.0	0.9	0.5	0.0	0.0	0.0
Memorandum items:								
Primary balance 6/	-4.3	-7.1	-5.2	-2.1	-0.9	-0.6	-0.3	-0.1
Overall balance electrcity company (ENEE)	-1.0	-1.8	-1.3	-0.3	-0.3	-0.3	0.0	0.2
Consolidated total debt	34.4	45.1	47.8	49.4	50.5	50.8	50.5	49.9
Nominal GDP (in billions of lempiras)	361.3	376.3	408.2	444.3	480.1	520.6	565.1	613.4

Sources: Honduran authorities and Fund staff estimates and projections.

1/ Includes central government, social security institutions, public enterprises, local governments, and decentralized agencies.

2/ Interest earned on public pension funds personal and housing loans to their affiliates.

3/ Includes debt forgiveness, accumulation, rescheduling, payment and/or forgiveness of arrears.

4/ Wage and suppliers arrears and other unsettled payments.

5/ Offsets the HIPC/MDRI debt relief accounted as grants.

T4 6/ Primary deficit calculation takes into account interest earnings.

Table 4. Honduras: Summary Accounts of the Central Bank and Financial System

(In millions of Lempiras; end-December)

	2010	2011	2012	2013	Projections 2014	Projections 2015
			I. Central Bank			
Net International Reserves 1/	**51,561**	**53,919**	**51,500**	**62,945**	**67,442**	**74,828**
(In millions of US$)	2,719	2,821	2,571	3,056	3,137	3,315
Net International Reserves (in millions of US$) 2/	2,082	2,032	1,665	2,211	2,271	2,411
Net Domestic Assets	**-31,628**	**-32,561**	**-29,351**	**-39,344**	**-41,526**	**-46,393**
Credit to the public sector (net)	8,050	12,567	12,729	7,237	14,337	14,337
Other depository institutions (net)	-39,946	-44,592	-42,618	-49,112	-57,780	-65,604
Other financial institutions	6,171	6,853	6,268	6,917	7,222	9,037
Nonfinancial private sector	-119	-593	-275	-212	-301	-303
Medium and long-term net foreign assets	980	1,008	1,304	2,181	2,279	3,793
Other items net	-6,763	-7,804	-6,759	-6,356	-7,282	-7,653
Currency issue	**19,933**	**21,358**	**22,149**	**23,600**	**25,916**	**28,434**
			II. Other Depository Institutions			
Net Foreign Assets	**1,189**	**1,129**	**-5,453**	**-10,277**	**-16,658**	**-16,764**
(In millions of US$)	62	59	-272	-497	-775	-743
Foreign assets (in million of US$)	555	597	472	490	455	475
Net Domestic Assets	**135,378**	**152,924**	**171,234**	**190,820**	**215,721**	**237,018**
Credit to the monetary authorities (net)	45,194	49,751	48,341	55,650	64,960	73,482
Credit to other financial institutions (net)	-19,063	-21,135	-23,448	-26,045	-30,278	-34,042
Credit to the combined public sector (net)	-1,725	1,232	1,947	1,089	5,684	5,737
Central government	-5,230	-3,534	-3,705	-8,618	-9,397	-9,379
Other nonfinancial public sector	741	716	1,227	5,640	11,014	11,031
Local governments	2,764	4,050	4,425	4,067	4,067	4,085
Credit to the private sector	143,460	157,263	183,916	204,443	224,732	248,322
Local currency	108,577	117,057	134,149	145,428	158,755	174,808
Foreign currency	34,883	40,205	49,768	59,015	65,977	73,514
Other items net	-32,487	-34,187	-39,522	-44,316	-49,377	-56,480
Liabilities	**136,567**	**154,053**	**165,781**	**180,544**	**199,063**	**220,254**
Of which: Deposits in domestic currency	98,341	112,123	117,378	127,211	141,470	156,545
Of which: Deposits in foreign currency	37,107	41,173	47,565	52,224	56,390	62,399
			III. Financial System			
Net Foreign Assets	**50,783**	**53,144**	**44,063**	**51,347**	**49,463**	**56,743**
(In millions of US$)	2,669	2,780	2,200	2,484	2,301	2,514
Net Domestic Assets	**100,814**	**117,636**	**137,968**	**145,958**	**168,007**	**183,707**
Credit to the nonfinancial combined public sector	6,324	13,799	14,676	8,326	20,021	20,074
Credit to the private sector	143,460	157,263	183,916	204,443	224,732	248,322
Local currency	108,577	117,057	134,149	145,428	158,755	174,808
Foreign currency	34,883	40,205	49,768	59,015	65,977	73,514
Other assets net	-5,077	-6,572	-7,088	-7,369	-9,200	-7,196
Other items net 3/	-43,894	-46,853	-53,536	-59,441	-67,546	-77,492
Broad Money (M4)	**151,597**	**170,780**	**182,031**	**197,305**	**217,470**	**240,449**
			(Rate of growth 12 months)			
Currency issue	12.6	7.1	3.7	6.6	9.8	9.7
Currency in circulation	13.2	10.3	1.4	3.9	9.8	9.7
Broad money	9.4	12.7	6.6	8.4	10.2	10.6
Broad money (constant exchange rate)	9.4	12.5	5.3	7.5	9.1	9.2
Credit to the private sector	3.5	9.6	16.9	11.2	9.9	10.5
Credit to the private sector (constant exchange rate)	3.5	9.5	15.5	10.2	8.7	8.9
M1	15.4	10.3	-6.9	4.5	11.4	10.6

Sources: Central Bank of Honduras and Fund staff estimates.

1/ Includes allocation of SDR 104.8 million in August, 2009.

2/ Excluding domestic liabilities in foreign currency and deposits of Hondutel.

3/ Includes the revaluation account reflecting changes in the value of assets due to exchange rate fluctuations.

Table 5. Honduras: Balance of Payments

(In millions of U.S. dollars; unless otherwise indicated)

		Prel.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019
Current account balance	**-1,581**	**-1,764**	**-1,521**	**-1,429**	**-1,408**	**-1,366**	**-1,334**	**-1,290**
Trade balance	-3,012	-3,147	-3,124	-3,191	-3,252	-3,327	-3,484	-3,619
Exports	8,359	7,806	8,176	8,497	8,797	9,154	9,529	9,890
Of which: maquila	3,939	3,889	3,990	4,112	4,255	4,423	4,598	4,780
Imports	-11,371	-10,953	-11,301	-11,688	-12,049	-12,482	-13,013	-13,509
Of which: maquila	-2,748	-2,560	-2,607	-2,747	-2,850	-2,970	-3,100	-3,220
Of which: Petroleum products	-2,059	-2,061	-2,043	-2,028	-2,060	-2,097	-2,151	-2,212
Services	-591	-659	-690	-699	-703	-708	-712	-716
Income (net)	-1,266	-1,353	-1,295	-1,295	-1,343	-1,401	-1,460	-1,505
Of which: payments on direct investments	-1,192	-1,208	-1,058	-1,031	-1,048	-1,083	-1,125	-1,161
Current transfers (net)	3,288	3,395	3,589	3,757	3,890	4,070	4,321	4,549
Of which: remittances	2,892	3,121	3,325	3,488	3,637	3,818	4,051	4,270
Capital account	**101**	**133**	**136**	**121**	**125**	**129**	**133**	**137**
Financial account	**1,426**	**2,501**	**1,227**	**1,158**	**1,214**	**1,363**	**1,390**	**1,325**
Direct investment (net)	851	992	969	1,005	1,009	1,043	1,064	1,101
Other private capital flows (net)	129	17	-94	-190	15	121	120	86
Public sector borrowing (net)	446	1,493	352	343	191	199	205	139
Of which: Eurobond	0	1,000	0	0	0	0	0	0
Of which: Disbursements	513	600	487	498	355	420	476	467
Of which: Amortization	-76	-70	-121	-141	-150	-206	-255	-312
Errors and omissions	-237	-391	0	0	0	0	0	0
Overall balance	**-291**	**479**	**-158**	**-150**	**-69**	**126**	**188**	**173**
Net international reserves (- increase)	**367**	**-546**	**-60**	**-140**	**-124**	**-191**	**-188**	**-173**
Financing gap	**0**	**0**	**218**	**290**	**193**	**65**	**0**	**0**
Official budget support	**0**	**0**	**218**	**104**	**86**	**65**	**0**	**0**
Eurobond	**0**	**0**	**0**	**186**	**106**	**0**	**0**	**0**
Residual gap	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Memorandum items:								
Current account (in percent of GDP)	-8.5	-9.5	-7.8	-7.1	-6.8	-6.4	-6.0	-5.6
Non oil current account (in percent of GDP)	2.6	1.6	2.7	3.0	3.1	3.4	3.7	4.0
Terms of trade (percent change)	-1.1	-2.5	2.8	1.7	-0.1	0.0	-0.2	-0.2
Exports of goods (percent change)	4.8	-6.6	4.7	3.9	3.5	4.1	4.1	3.8
Of which: volume growth (percent change)	10.9	-2.4	2.3	3.1	3.9	4.0	4.0	4.0
Imports of goods (percent change)	2.2	-3.7	3.2	3.4	3.1	3.6	4.3	3.8
Of which: volume growth (percent change)	7.0	-1.8	3.6	4.3	3.4	3.5	3.9	3.9
Gross reserves (end of period)	2,778	3,255	3,329	3,507	3,660	3,877	4,094	4,296
In months of next year imports (excluding maquila)	3.3	3.7	3.7	3.8	3.8	3.9	4.0	4.1
Total external debt to GDP ratio (in percent)	26.2	35.9	37.8	39.9	40.9	41.1	40.9	40.4
External public debt to GDP ratio (in percent)	19.7	28.1	29.7	31.8	32.9	33.1	33.0	32.6
External public sector debt service (in percent of nonmaquila exports)	3.0	2.8	7.3	7.9	8.5	9.8	10.7	11.6
Nominal GDP (millions of U.S. dollars)	18,514	18,487	19,452	20,164	20,752	21,431	22,155	22,904

Sources: Central Bank of Honduras and Fund staff estimates.

Table 6. Honduras: External Financing Needs and Sources

(In millions of U.S. dollars)

			Prel.	Proj.			
	2011	2012	2013	2014	2015	2016	2017
Current account deficit	1,409	1,581	1,764	1,521	1,429	1,408	1,366
Debt amortizations	333	266	342	344	358	360	410
Subtotal (requirements)	1,741	1,847	2,106	1,865	1,787	1,768	1,776
Capital account flows (net)	166	101	133	136	121	125	129
Foreign direct investment (net)	1,012	851	992	969	1,005	1,009	1,043
Pulic sector borrowing (project related)	554	513	600	487	498	355	420
Eurobond	0	0	1,000	0	0	0	0
Other capital flows (net) 1/	-41	14	-72	115	13	211	310
Change in reserves (+ decrease)	50	367	-546	-60	-140	-124	-191
Subtotal (sources)	1,741	1,847	2,106	1,647	1,497	1,575	1,711
Financing gap	0	0	0	218	290	193	65
World Bank	…	…	…	55	25	0	0
IADB	…	…	…	130	65	65	65
IMF	…	…	…	0	0	0	0
EU	…	…	…	33	14	21	0
Eurobond	…	…	…	0	186	106	0

Sources: Central Bank of Honduras and Fund staff estimates and projections.

1/ Includes errors and omissions.

Table 7. Honduras: Medium-Term Macroeconomic Framework

(In percent of GDP. unless otherwise specified)

	Prel.		Proj.					
	2012	2013	2014	2015	2016	2017	2018	2019
Growth and prices (in percent)								
Real GDP growth	4.1	2.6	3.0	3.0	3.3	3.5	3.7	3.7
GDP deflator	3.6	1.5	5.3	5.7	4.6	4.8	4.7	4.7
CPI inflation (eop)	5.4	4.9	6.5	5.8	5.4	5.4	5.4	5.4
Investment and saving								
Gross domestic investment	**24.4**	**25.6**	**25.6**	**25.3**	**25.5**	**25.7**	**25.9**	**26.0**
Private sector	21.4	21.9	22.3	22.9	23.1	23.3	23.5	23.5
Public sector	3.0	3.6	3.3	2.4	2.4	2.4	2.4	2.5
Gross national savings	**15.8**	**16.0**	**17.7**	**18.2**	**18.7**	**19.3**	**19.9**	**20.3**
Private sector	16.4	18.7	18.7	18.0	17.2	17.4	17.2	17.6
Public sector	-0.5	-2.7	-1.0	0.2	1.5	1.9	2.7	2.8
Balance of payments								
External current account	-8.5	-9.5	-7.8	-7.1	-6.8	-6.4	-6.0	-5.6
Non oil current account	2.6	1.6	2.7	3.0	3.1	3.4	3.7	4.0
Gross international reserves (millions of dollars)	2,778	3,255	3,329	3,507	3,660	3,877	4,094	4,296
(in months of non maquila imports) 1/	3.3	3.7	3.7	3.8	3.8	3.9	4.0	4.1
Terms of Trade (annual percent change)	-1.1	-2.5	2.8	1.7	-0.1	0.0	-0.2	-0.2
External debt	**26.2**	**35.9**	**37.8**	**39.9**	**40.9**	**41.1**	**40.9**	**40.4**
Combined public sector								
Revenue	22.5	22.9	24.5	24.6	25.1	25.5	25.6	25.7
Of which: Noninterest revenue and grants	21.1	21.3	22.8	22.9	23.4	23.7	23.8	23.9
Expenditure	26.7	30.4	30.4	27.8	27.3	27.3	27.1	27.0
Primary balance	**-4.3**	**-7.1**	**-5.2**	**-2.1**	**-0.9**	**-0.6**	**-0.3**	**-0.1**
Overall balance	**-4.2**	**-7.6**	**-5.9**	**-3.2**	**-2.2**	**-1.8**	**-1.4**	**-1.2**
Central government								
Revenue	16.7	17.0	18.8	18.4	18.5	18.7	18.7	18.6
Expenditure	22.7	24.9	24.3	22.4	21.9	21.5	21.2	21.1
Of which: Noninterest expenditure	21.0	22.7	21.7	19.5	18.6	18.2	17.9	17.7
Primary balance	**-4.3**	**-5.6**	**-2.9**	**-1.0**	**-0.1**	**0.5**	**0.8**	**0.9**
Overall balance	**-6.0**	**-7.9**	**-5.5**	**-4.0**	**-3.4**	**-2.9**	**-2.6**	**-2.4**
Consolidated public sector debt 2/								
Total	**34.4**	**45.1**	**47.8**	**49.4**	**50.5**	**50.8**	**50.5**	**49.9**
Domestic debt	14.7	17.1	18.1	17.6	17.7	17.7	17.4	17.3
External debt	19.7	28.1	29.7	31.8	32.9	33.1	33.0	32.6
Memo items:								
Nominal GDP (in billions of lempiras)	361	376	408	444	480	521	565	613

Sources: Central Bank of Honduras, Ministry of Finance, and Fund staff estimates and projections.

1/ Refers to the following year's imports of nonmaquila goods and non-factor services.

2/ Debt series revised based on comprehensive data provided by the authorities in September 2012.

Table 8. Honduras: External Vulnerability Indicators

	2010	2011	2012	Prel. 2013	Proj. 2014	Proj. 2015
Exports of goods and services, annual percent change	25.4	24.3	4.6	-6.1	4.7	4.1
Imports of goods and services, annual percent change	20.9	24.8	3.5	-2.9	3.4	3.5
Terms of trade (deterioration -)	-7.3	1.5	-1.1	-2.5	2.8	1.7
Real effective exchage rate (eop, depreciation -) 1/	4.3	1.8	-1.7	0.4	1.2	…
Current account balance (percent of GDP)	-4.3	-8.0	-8.5	-9.5	-7.8	-7.1
Capital and financial account (percent of GDP)	9.8	7.4	8.2	14.2	7.0	6.3
External public debt (percent of GDP)	18.0	18.1	19.7	28.1	29.7	31.8
External public debt (in percent of exports of goods and services)	39.1	35.6	38.7	58.7	62.4	66.7
Debt service on external public debt (in percent of non maquila exports)	3.9	4.4	3.0	2.8	7.3	7.9
Gross official reserves						
in millions of U.S. dollars	2,921	3,043	2,778	3,255	3,329	3,507
in percent of short-term external debt	963	1,211	1,055	1,022	956	984
in months of next year's non maquila imports	3.6	3.6	3.3	3.7	3.7	3.8
Net international reserves						
in millions of U.S. dollars	2,082	2,032	1,665	2,211	2,271	2,411
in percent of short-term external debt	686	809	633	694	652	677
in months of next year's non maquila imports	2.5	2.4	2.0	2.5	2.5	2.6

Sources: Central Bank of Honduras and Fund staff estimates and projections.

1/ 2014 data is for August.

Table 9. Honduras: Structure and Performance of the Banking Sector

(In percent, unless otherwise indicated)

	2009	2010	2011	2012	Prel. 2013	2014 3/
Total assets (in millions of Lempiras) 1/	**220,277**	**236,665**	**270,981**	**302,662**	**341,614**	**372,119**
(In percent of GDP)	80	79	81	84	91	95
Number of banks	**17**	**17**	**17**	**17**	**17**	**17**
Domestic	8	8	7	7	7	7
Foreign	9	9	10	10	10	10
Bank concentration						
Number of banks accounting for at least						
25 percent of total assets	2	2	2	2	2	2
75 percent of total assets	6	6	6	6	6	6
Bank rating (CAMEL)						
Number of banks (Category IV and V)	1	0	0	0	0	0
Share of total assets	2	0	0	0	0	0
Capital adequacy						
Regulatory capital to risk-weighted assets	14.3	14.9	14.9	14.7	14.5	14.8
Capital (net worth) to assets	9.3	9.2	9.1	9.3	9.1	9.3
Asset quality and composition						
Nonperforming loans(NPLs) to total loans 2/	4.7	3.7	2.9	3.3	3.4	4.0
NPLs net of provisions to capital 2/	4.2	-4.4	-6.5	-4.6	-5.2	-0.7
Restructured loans to regulatory capital	9.0	19.8	26.6	24.7	25.3	22.8
Non earning assets net of provisions						
to regulatory capital	47.2	47.9	46.9	45.0	44.1	50.7
Provisions to total loans	4.1	4.3	3.9	4.0	4.2	4.2
Provisions to NPLs 2/	86.2	118.9	135.0	121.8	123.7	102.7
Sectoral distribution of loans to total loans:						
Commerce	11.6	12.7	13.0	14.4	14.3	14.5
Construction and real estate	33.5	34.2	32.9	30.8	28.9	27.9
Agriculture and related sectors	0.0	0.0	0.0	4.4	4.7	4.7
Industry	15.4	13.6	12.3	11.7	11.9	11.3
Consumption	15.7	16.5	18.3	20.5	21.9	20.6
Other	0.0	0.0	0.0	18.2	18.0	20.7
Profitability						
Return on assets (ROA)	1.2	1.3	1.3	1.5	1.4	1.4
Return on equity (ROE)	12.6	12.5	13.2	15.9	14.5	13.6
Interest margin to total income	48.1	48.2	48.9	52.1	47.5	51.9
Personnel expenses to administrative expenses	39.6	39.6	39.6	39.4	41.8	42.0
Liquidity						
Liquid assets to total assets	21.1	24.4	24.3	21.4	25.0	25.0
Liquid assets to total short-term liabilities	52.2	58.2	58.8	56.2	69.7	74.4
Dollarization						
Deposits in foreign currency in percent of total	30.0	29.5	29.1	30.6	30.6	31.1
Credit in foreign currency in percent of total	25.1	28.3	30.1	31.2	33.5	33.9

Source: National Commission of Banking and Insurance.

1/ Includes contingent assets.

2/ As of 2012 NPLs include delinquency of restructured loans.

3/ 2014 data as of August.

Table 10. Honduras: Millennium Development Goals

	1990	1995	2000	2005	2010	2011	2012
Goal 1: Eradicate extreme poverty and hunger							
Employment to population ratio, 15+, total (%)	56.8	58.9	63.4	58.7	60.2	60.3	..
Employment to population ratio, ages 15-24, total (%)	48.5	50.9	54.2	47.1	46.4	46.3	..
Poverty gap at $1.25 a day (PPP) (%)	22.4	10.9	8.1	13.3	9.4	..	..
Malnutrition prevalence, weight for age (% of children under 5)	15.8	16.1	12.5	8.6	..	..	..
Prevalence of undernourishment (% of population)	21.4	18.6	16.3	14.2	10.0	9.6	..
Goal 2: Achieve universal primary education							
Primary completion rate, total (% of relevant age group)	64.5	..	..	81.8	98.5	101.4	..
School enrollment, primary (% net)	88.8	..	88.8	91.8	95.8	97.3	..
Goal 3: Promote gender equality and empower women							
Proportion of seats held by women in national parliaments (%)	10.2	..	9.4	23.4	18.0	19.5	19.5
Ratio of girls to boys in primary and secondary education (%)	104.4	..	..	105.6	107.2	106.9	..
Goal 4: Reduce child mortality							
Immunization, measles (% of children ages 12-23 months)	90.0	89.0	98.0	96.0	99.0	99.0	..
Mortality rate, infant (per 1,000 live births)	42.9	35.6	28.8	23.4	18.9	18.2	..
Mortality rate, under-5 (per 1,000 live births)	55.0	44.4	35.0	27.9	22.2	21.4	..
Goal 5: Improve maternal health							
Births attended by skilled health staff (% of total)	46.9	54.9	55.7	66.9	..	..	..
Contraceptive prevalence (% of women ages 15-49)	46.7	50.0	61.8	65.2	..	..	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	220.0	180.0	160.0	130.0	100.0	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases							
Incidence of tuberculosis (per 100,000 people)	125.0	125.0	116.0	89.0	51.0	43.0	..
Prevalence of HIV, total (% of population ages 15-49)	..	..	..	..	..	..	..
Tuberculosis case detection rate (%, all forms)	60.0	71.0	89.0	55.0	74.0	96.0	..
Goal 7: Ensure environment sustainability							
CO2 emissions (metric tons per capita)	0.5	0.7	0.8	1.1	1.0	..	..
Forest area (% of land area)	72.7	..	57.1	51.8	46.4	45.3	..
Improved sanitation facilities (% of population with access)	48.8	56.8	64.5	72.1	79.2	80.6	..
Improved water source (% of population with access)	72.8	76.9	80.8	84.7	88.2	88.9	..
Terrestrial protected areas (% of total land area)	13.6	15.0	18.2	18.2	18.2	..	..
Goal 8: Develop a global partnership for development							
Internet users (per 100 people)	0.0	0.0	1.2	6.5	11.1	15.9	18.1
Mobile cellular subscriptions (per 100 people)	0.0	0.0	2.5	18.6	125.1	104.0	93.1

Source: Millenium Development Goals, World Bank.

Table 11. Honduras: Prior Actions and Structural Benchmarks 2014–2015

Measure	Target Date
Prior actions	
Present to congress a 2015 budget bill consistent with the central government and combined public sector deficits targeted under the program	Met
Submit to congress a bill to strengthen the framework for public-private partnerships (PPPs)	Met
Reinstate the automatic mechanism for the adjustment of fuels prices	5 days before Board discussion of program
Structural benchmarks	
Adjust average electricity tariffs by 2.5 percent during 2015 to reflect past cost increases; further adjust tariffs to incorporate current changes in costs (see MEFP, Appendix I).	Continuous
Approval of legislation to strengthen the PPP framework	December 2014
Repeal legislation allowing the issuance of government guarantees for debt contracted by private companies involved in PPP projects	December 2014
Conduct a census of public employees, with the aim of identifying and cancelling redundant positions during 2015	December 2014
Take actions sufficient to achieve savings in ENEE's wage bill as indicated in paragraph 11 of the MEFP.	March 2015
Submit to congress legislation to reform the Social Security Institute (IHSS) to strengthen its actuarial position and improve its governance	March 2015
In consultation with staff, prepare a plan to address the financial difficulties of HONDUTEL	March 2015
Approval of the law reforming the IHSS	June 2015
Complete an audit of public sector arrears, with a view to clearing them	June 2015
Present a program for developing a medium-term fiscal framework with a clear fiscal anchor and fiscal policy targets	June 2015
Present to congress a 2016 budget bill consistent with the program targets for central government and CPS deficits	September 2015
Strengthen the Large Taxpayer Unit with adequate staff levels	September 2015
Present a plan for a gradual removal of foreign exchange surrender requirements	December 2015

Table 12. Honduras: Performance Criteria 1/

(Cumulative flows; millions of Lempiras, unless specified)

	2014		2015	
	Prel.	PC	PC	PC
	End-Jun.	End-Dec.	End-Jun.	End-Dec.
QUANTITATIVE PERFORMANCE CRITERIA				
Fiscal targets 2/				
Overall balance of the combined public sector (floor)	-2,642	-23,931	-5,256	-14,283
Overall balance of the central government (floor)	-4,365	-22,252	-6,870	-17,873
Overall balance of ENEE (floor) 3/	-2,155	-5,521	-1,491	-3,353
Public debt targets 4/				
Contracting and guaranteeing of new non-concessional loans (continuous ceiling, in million US$)	…	600	600	600
Accumulation of new arrears by ENEE (continuous ceiling)	…	0	0	0
Accumulation of new external arrears (continuous ceiling, in million US$)	0	0	0	0
Monetary targets				
Net international reserves of the Central Bank (floor, in million US$)	2,362	2,271	2,390	2,411
Stock of net domestic assets of the central bank (ceiling) 5/	-28,900	-22,017	-27,001	-22,454
Indicative targets 2/				
Wage bill of the central government (ceiling)	17,945	38,049	18,850	39,248
Social spending (floor)	2,496	7,078	2,834	7,333
Operating revenue-to-spending ratio of ENEE (floor)	…	0.85	0.97	0.97

1/ Definitions as specified in the Technical Memorandum of Understanding.
2/ Cumulative starting in January of the correspondent year.
3/ Excluding government transfers.
4/ Cumulative starting in December 2014. Targets on non-concessional debt and external arrears are for the combined public sector.
5/ Using the program exchange rate of L21.1066 = 1US$.

Table 13. Honduras: Disbursements, Purchases, and Timing of Reviews under the SCF/SBA Arrangements (Proposed Schedule)

Date of Availability	Conditions	Amount (millions of SDRs)			Percent of quota		
		Total	SCF	SBA	Total	SCF	SBA
December 3, 2014	Board approval of the arrangement	38.8500	6.4750	32.3750	30.00	5.00	25.00
April 15, 2015	Observance of end-December 2014 performance criteria and continuous performance criteria and completion of first review	6.4750	3.2375	3.2375	5.00	2.50	2.50
October 15, 2015	Observance of end-June 2015 performance criteria and continuous performance criteria and completion of second review	6.4750	3.2375	3.2375	5.00	2.50	2.50
April 15, 2016	Observance of end-December 2015 performance criteria and continuous performance criteria and completion of third review	25.9000	19.4250	6.4750	20.00	15.00	5.00
October 15, 2016	Observance of end-June 2016 performance criteria and continuous performance criteria and completion of fourth review	25.9000	19.4250	6.4750	20.00	15.00	5.00
April 15, 2017	Observance of end-December 2016 performance criteria and continuous performance criteria and completion of fifth review	12.9500	0.0000	12.9500	10.00		10.00
October 15, 2017	Observance of end-June 2017 performance criteria and continuous performance criteria and completion of sixth review	12.9500	0.0000	12.9500	10.00		10.00
	Total	129.5000	51.8000	77.7000	100.00	40.00	60.00

Honduras' quota is SDR 129.5 million.

Table 14. Honduras: Indicators of Fund Credit

(As of September 30, 2014; in units indicated)

			Projections					
	2012	2013	2014	2015	2016	2017	2018	2019
Existing Fund credit								
Stock, in millions of SDRs 1/	12.2	8.1	4.1	1.0	0.0	0.0	0.0	0.0
Obligations, in millions of SDRs	4.1	4.1	4.1	3.1	1.0	0.0	0.0	0.0
Proposed SCF								
Stock, in millions of SDRs 1/	0.0	0.0	6.5	13.0	51.8	51.8	51.1	48.6
Disbursements, in millions of SDRs	0.0	0.0	6.5	6.5	38.9	0.0	0.0	0.0
Obligations, in millions of SDRs 2/	0.0	0.0	0.0	0.1	0.2	0.3	1.0	2.8
Principal, in millions of SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.7	2.5
Interest and charges, in millions of SDRs	0.0	0.0	0.0	0.1	0.2	0.3	0.3	0.3
Proposed SBA								
Stock, in millions of SDRs 1/	0.0	0.0	32.4	38.9	51.8	77.7	60.7	39.7
Disbursements, in millions of SDRs	0.0	0.0	32.4	6.5	13.0	25.9	0.0	0.0
Obligations, in millions of SDRs 3/	0.0	0.0	0.0	0.3	0.5	0.6	17.8	21.6
Principal, in millions of SDRs	0.0	0.0	0.0	0.0	0.0	0.0	17.0	21.0
Interest and charges, in millions of SDRs	0.0	0.0	0.0	0.3	0.5	0.6	0.8	0.6
Stock of existing and prospective Fund credit 1/								
In millions of SDRs	12.2	8.1	42.9	52.8	103.6	129.5	111.8	88.2
In percent of quota	9.4	6.3	33.1	40.8	80.0	100.0	86.3	68.1
In percent of exports of goods and services	0.2	0.1	0.7	0.8	1.6	2.0	1.6	1.3
In percent of external debt	0.4	0.2	0.9	1.0	1.9	2.2	1.9	1.5
In percent of gross reserves	0.7	0.4	2.0	2.4	4.5	5.2	4.3	3.3
Obligations to the Fund from existing arrangements and prospective Fund arrangements								
In millions of SDRs	4.1	4.1	4.1	3.4	1.6	0.9	18.8	24.4
In percent of quota	3.1	3.1	3.1	2.7	1.3	0.7	14.5	18.8
In percent of exports of goods and services	0.1	0.1	0.1	0.1	0.0	0.0	0.3	0.3
In percent of external debt	0.1	0.1	0.1	0.1	0.0	0.0	0.3	0.4
In percent of gross reserves	0.2	0.2	0.2	0.2	0.1	0.0	0.7	0.9

1/ End of period.
2/ Expected repayment schedule SCF, assuming full drawings and interest a 0.50 percent interest rate. The Honduran authorities have the intention to treat the arrangement as precautionary.
3/ Expected repayment schedule SBA, assuming full drawings and a rate of charge of 1.08 percent. The Honduran authorities have expressed their intention to treat the arrangement as precautionary, since balance of payment pressures have not materialized.

Appendix I. Honduras: Debt Sustainability Analysis

Under the policies envisaged by the proposed program, the debt sustainability analysis (DSA) shows improved public debt sustainability prospects compared to the previous DSA. However, given risks to the macroeconomic and fiscal outlook, Honduras' risk of external debt distress is assessed to remain moderate. External public debt indicators, except for one, are expected to remain below their indicative thresholds. Against this background, an improved rating of low risk of debt distress could be considered in a future DSA provided that the program's fiscal consolidation and growth targets are achieved.

A. Background

Honduras' public debt ratios continued to increase in 2013, reflecting weak fiscal policies. The fiscal position deteriorated in recent years, with the overall deficit of the combined public sector (CPS) rising to 7½ percent of GDP in 2013, from 2.8 percent in 2011.[1] By end 2013, the public debt ratio reached 45 percent of GDP. While the share of commercial external debt rose in 2013, following the placement of US$1 billion (5.4 percent of GDP) in global bonds,[2] about 80 percent of public external debt is to official creditors. A substantial portion of external public debt has been contracted on concessional terms, with a grant element averaging about 20 percent in 2013 (Table A2).

Public debt is mostly with foreign creditors. While the share of domestic debt has risen in recent years, over 60 percent of total public debt is accounted for by external creditors. The main external lenders to Honduras are the Inter-American Development Bank (IADB), the Central American Bank for Economic Integration, and the World Bank. Debt to these institutions carries long maturities, although given current lending and discount rates, only the IADB continues to provide concessional loans (i.e., with a grant element of at least 35 percent) to Honduras. Domestic public debt is mainly to commercial banks, has a shorter—though rising— maturity (about 3 years), and carries a higher real interest rate (Tables A1 and A2).

B. Underlying Assumptions

Economic growth. The baseline scenario assumes that growth in Honduras will rise to 3 percent in 2014–15 and strengthen further in subsequent years, before stabilizing at about 3¾ percent—broadly in line with its estimated potential. This reflects an improvement from the previous DSA, where growth was expected to remain at about 3 percent in the medium term. However, growth is

[1] The combined public sector includes the central government, local governments, decentralized agencies, social security institutions, the central bank, and public enterprises. The DSA baseline includes costs from PPP-related liabilities.

[2] The US$1 billion bond was placed in two tranches. The first tranche (US$0.5 billion, 11 years, 7.5 percent interest rate) was placed in March 2013; and the second tranche (US$0.5 billion, 7 years, at 8.75 percent) was placed in December 2013.

still projected to remain below the historical average (4 percent) throughout the DSA period. The acceleration of growth over the medium term is predicated on more favorable external conditions (notably better terms of trade and a growth pick up in the US) and the recovery of the coffee sector from leaf-rust disease, as well as improved confidence and higher private investment from stronger economic policy management. These factors are expected to offset the dampening effect of fiscal consolidation on growth, which in Honduras is expected to be modest given the high degree of openness of the economy.

Fiscal policy. The baseline scenario incorporates a cumulative fiscal adjustment of about 6½ percent of GDP during the program period (2014–17), with the primary deficit of the CPS declining to 1¾ percent of GDP and ½ percent of GDP by 2017, respectively (a significant improvement from the previous DSA, where the overall balance was expected to reach about 4¼ percent of GDP in 2017). The overall CPS deficit continues to decline slowly over the medium term as debt and interest payments start to fall, stabilizing at about 1 percent of GDP over the longer term (consistent with a primary deficit of ¼ percent of GDP).[3] The fiscal adjustment features a combination of higher tax revenues (about 2 percent of GDP) and lower expenditure (about 3 percent of GDP), mostly at the central government level. It also reflects a substantial improvement in the finances of the state-owned electricity company (ENEE)—whose deficit (1.8 percent of GDP in 2013) is projected to be eliminated by 2018. This improvement comes from higher tariffs, reduction of losses, and wage bill savings.

Public sector financing. Financing for the public sector is assumed to come mainly from external sources, especially multilateral lenders. It is, however, assumed that the financing mix changes toward less concessional sources compared to recent years (Table A2), including within multilateral institutions. The baseline scenario assumes the placement of two additional global bonds in 2015–16, totaling about US$300 million (1.4 percent of GDP), to help meet government financing needs. These bonds are assumed to carry an interest rate of 7 percent (significantly above current yields in the secondary market, which have hovered around 6 percent in recent weeks) and 10-year maturity. All global bonds are assumed to be refinanced through the issuance of new, similar bonds. Other financing needs are met through official, mostly multilateral, financing. The DSA includes existing domestic arrears in the stock of public debt, and assumes that arrears are paid down with domestic bonds bearing market rates in 2015.

External sector. The external current account deficit is projected to decline from 9½ percent in 2013 to 6.4 percent by 2017, and stabilize at about 5¼ percent of GDP over the longer term. The previous DSA projected a weaker external position— with the current account deficit stabilizing at about 6½ percent of GDP over the medium term—reflecting mainly a significantly smaller fiscal consolidation effort. The improvement in the current account during the program period reflects more favorable external conditions (including continued recovery of worker remittances), lower

[3] The primary deficit differs from that reported in Table A1. The latter reflects the primary deficit calculation in the DSA framework, which does not take into account interest revenue.

income payments, and a stronger macroeconomic policy mix (fiscal consolidation and a weaker real exchange rate). As in the previous DSA, the current account deficit continues to be financed through foreign direct investment and, to a lesser extent, public sector borrowing, with very small private sector flows. This allows international reserves to increase to about 4 months of imports by 2017 and settle at close to 4½ months of imports over the longer term.

C. Public and External Debt Sustainability Analysis

Public debt ratios are expected to peak in 2017, and start to decline subsequently (Table A1)**.** Public debt is projected to peak at about 51 percent of GDP in 2017 (up from 45 percent of GDP in 2013) and start falling slowly as fiscal consolidation proceeds and interest payments decline, reaching 45 percent of GDP by 2024. This represents a significant improvement from the previous DSA, which projected a public debt-to-GDP ratio of 67 percent by 2024. In present value terms, the public-debt ratio is expected to peak at 46 percent of GDP and fall to about 40 percent of GDP in the early 2020s. The public debt dynamics remains somewhat vulnerable to both policy-related and exogenous shocks, especially to those related to economic growth and fiscal policy (Table A3).

The evolution of external debt ratios is projected to follow a similar pattern (Table A2). External debt ratios are projected to peak at 41 percent of GDP in 2017, from about 36 percent of GDP in 2013. The share of external debt in total public debt rises slowly to about two-thirds by the mid-2020s and stabilizes at that level. The ratios for the PV of public debt and public debt service remain below their indicative thresholds in the baseline scenario throughout the projection period.[4,5] (Table A4). No alternative scenario leads to breaching the thresholds for the PV of debt. The threshold for the ratio of debt service to revenue is exceeded in two separate years (2020 and 2025) under the most extreme shock, with the spikes reflecting the amortization of global bonds. The ratio of debt service to exports remains well below its threshold under all scenarios.

A customized scenario with several negative shocks shows that external public debt indicators remain below their indicative thresholds, except for the debt service to revenue ratio. The scenario aims at capturing key risks and vulnerabilities in Honduras. It includes negative shocks to GDP growth, which could arise from weaker-trading partner growth ; harder external financing conditions that could be associated with negative developments in international financial markets; a weaker fiscal position from possible slippages in the implementation of adjustment measures; and the assumption of PPP-related contingent liabilities by the government.[6] In this scenario, external

[4] Debt threshold for Honduras are based on the average ratio in the Country Policy and Institutional Assessment (CPIA) for 2011-13, which implies a medium policy performance rating.

[5] Remittances are included in the external DSA (Honduras meets the criteria for its inclusion). In the last three years, they were around 16 percent of GDP—still below pre-global crisis levels but expected to continue to recover over the next few years—and close to 40 percent of exports of goods and services.

[6] In the customized scenario, (i) real GDP growth is 2.5 percent from 2014 to 2017, and rises 0.2 percentage points per year to reach 3.3 percent in 2021, staying at this level for the remainder of the DSA period; (ii) financing conditions from external capital markets deteriorate permanently, with the rate of interest on Eurobonds rising to 8.5 percent, starting in 2015; (iii) the overall deficit of the CPS increases by 2 percent of GDP in 2015 compared to the

(continued)

public debt rises initially but remains below the indicative threshold and starts to decline around the mid-2020s. The ratio of debt service to exports also remains below its indicative threshold. The threshold for the ratio of debt service to revenue is exceeded once (in 2020, owing to the global bond repayment, as mentioned above) and approaches the threshold on two subsequent dates.

D. Conclusion

Public and external debt indicators have strengthened compared to previous DSA, but the risk of debt distress remains moderate. The improvement in debt indicator reflects the stronger macroeconomic policies that would underpin the Fund-supported program, which would translate into substantially lower fiscal and current account deficits. It is also aided by somewhat higher economic growth compared to the previous DSA. However, given risks to the macroeconomic and fiscal outlook, Honduras' risk of external debt distress is assessed to remain moderate. External public debt indicators are expected to stay below their indicative thresholds (except for the ratio of debt service to revenue), provided that the program's fiscal consolidation and growth targets are achieved. In that context, a rating of low risk of debt distress could be considered in a future DSA.

baseline (this increase fades out partially at a constant rate of 15 percent during the DSA period, e.g., compared to the baseline, the deficit is higher by 1.7, 1.0 and 0.5 percent of GDP respectively in 2016, 2019 and 2024; and (iv) contingent liabilities (estimated by the authorities at about 2 percent of GDP) related to existing PPP projects are assumed to materialize over the next three years and result in an increase in public external debt.

Table A1. Honduras: Public Sector Debt Sustainability Framework, Baseline Scenario, 2011–2034

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2011	2012	2013			2014	2015	2016	2017	2018	2019	2014-19 Average	2024	2034	2020-34 Average
Public sector debt 1/	32.1	34.4	45.1			47.8	49.4	50.5	50.8	50.5	49.9		45.1	36.1	
of which: foreign-currency denominated	18.1	19.7	28.1			29.7	31.8	32.9	33.1	33.0	32.6		30.0	23.4	
Change in public sector debt	2.3	2.3	10.8			2.6	1.6	1.1	0.3	-0.3	-0.6		-0.8	-0.7	
Identified debt-creating flows	-0.3	2.7	6.8			3.4	0.8	0.0	-0.6	-1.0	-1.2		-1.6	-1.0	
Primary deficit 2/	1.7	3.0	5.7	2.3	1.6	3.5	0.5	-0.8	-1.2	-1.5	-1.7	-0.2	-1.5	-1.0	-1.3
Revenue and grants	23.1	22.5	22.9			24.5	24.5	25.0	25.2	25.2	25.2		25.2	25.2	
of which: grants	1.1	1.0	0.8			1.1	0.8	0.6	0.5	0.4	0.4		0.4	0.4	
Primary (noninterest) expenditure	24.9	25.5	28.6			28.0	25.0	24.1	23.9	23.7	23.5		23.8	24.3	
Automatic debt dynamics	-2.1	-0.3	1.1			-0.1	0.3	0.8	0.6	0.5	0.5		-0.2	-0.1	
Contribution from interest rate/growth differential	-1.2	-0.8	0.5			-0.2	0.0	0.1	-0.1	-0.3	-0.3		-0.3	-0.2	
of which: contribution from average real interest rate	-0.1	0.4	1.4			1.1	1.3	1.7	1.6	1.5	1.5		1.3	1.2	
of which: contribution from real GDP growth	-1.1	-1.3	-0.9			-1.3	-1.4	-1.6	-1.7	-1.8	-1.8		-1.6	-1.3	
Contribution from real exchange rate depreciation	-0.8	0.5	0.6			0.1	0.4	0.7	0.7	0.8	0.8		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	2.6	-0.4	4.0			-0.8	0.8	1.1	0.9	0.7	0.7		0.8	0.3	
Other Sustainability Indicators															
PV of public sector debt	...	...	39.9			42.6	44.2	45.4	45.6	45.2	44.6		40.8	32.4	
of which: foreign-currency denominated	...	...	22.8			24.5	26.7	27.7	27.9	27.8	27.3		25.7	19.7	
of which: external	...	...	22.8			24.5	26.7	27.7	27.9	27.8	27.3		25.7	19.7	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 3/	5.7	6.8	10.1			9.3	7.4	5.2	3.0	3.0	2.8		2.9	2.6	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	174.4			174.0	180.6	181.6	181.0	179.2	176.7		161.8	128	
PV of public sector debt-to-revenue ratio (in percent)	...	...	180.5			181.9	186.6	186.0	184.8	182.3	179.8		164.6	131	
of which: external 4/	...	...	103.2			104.7	112.5	113.6	113.2	112.0	110.1		103.6	79.4	
Debt service-to-revenue and grants ratio (in percent) 5/	17.1	17.0	19.2			23.7	28.3	24.0	16.9	17.8	17.9		17.4	14.3	
Debt service-to-revenue ratio (in percent) 5/	17.9	17.8	19.9			24.7	29.2	24.6	17.3	18.1	18.2		17.7	14.5	
Primary deficit that stabilizes the debt-to-GDP ratio	-0.5	0.7	-5.1			0.9	-1.2	-2.0	-1.5	-1.2	-1.1		-0.7	-0.2	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	3.8	4.1	2.6	4.1	2.7	3.0	3.0	3.3	3.5	3.7	3.7	3.4	3.7	3.7	3.7
Average real interest rate on total debt (in percent)	-3.6	0.5	4.2			0.4	0.7	1.9	1.7	1.6	1.6	1.3	1.7	1.9	1.9
Average nominal interest rate on forex debt (in percent)	1.7	1.8	2.0	1.7	0.2	3.6	3.6	3.7	3.8	3.8	3.8	3.7	3.8	4.1	4.0
Average real interest rate on domestic debt (in percent)	-0.5	3.3	9.0	1.4	3.9	3.6	4.9	6.7	6.2	5.9	5.8	5.5	5.6	5.5	5.6
Real exchange rate depreciation (in percent, + indicates depreciation)	-4.9	3.0	3.2	-2.1	3.4	0.4	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	7.8	3.6	1.5	5.9	2.1	5.3	5.7	4.6	4.8	4.7	4.7	5.0	4.2	4.2	4.2
Growth of real primary spending (deflated by GDP deflator, in percent)	-1.1	6.7	15.1	5.4	6.8	0.9	-8.1	-0.1	2.7	2.6	3.0	0.2	4.1	3.7	3.9
Grant element of new external borrowing (in percent)	...	...	...	...	...	13.0	8.5	7.5	13.6	14.0	16.2	12.2	6.5	8.1	...

Sources: National authorities and Fund staff estimates and projections.

1/ Combined public sector.

2/ Primary deficit does not take into account interest earnings.

3/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

4/ Revenues excluding grants.

5/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table A2. Honduras: External Debt Sustainability Framework, Baseline Scenario, 2011–2034 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical 8/	Standard 8/	Projections									
				Average	Deviation							2014-2019			2020-2034
	2011	2012	2013			2014	2015	2016	2017	2018	2019	Average	2024	2034	Average
External debt (nominal) 1/	**23.8**	**26.2**	**35.9**			**37.8**	**39.9**	**40.9**	**41.1**	**40.9**	**40.4**		**37.6**	**30.7**	
of which: public and publicly guaranteed (PPG)	18.1	19.7	28.1			29.7	31.8	32.9	33.1	33.0	32.6		30.0	23.4	
Change in external debt	-0.2	2.4	9.7			1.9	2.1	1.0	0.2	-0.2	-0.5		-0.8	-0.6	
Identified net debt-creating flows	-0.4	2.8	4.2			1.8	1.0	0.6	0.1	-0.2	-0.6		-0.8	-0.8	
Non-interest current account deficit	**7.5**	**8.0**	**8.8**	**6.8**	**3.7**	**6.6**	**5.7**	**5.3**	**4.9**	**4.5**	**4.1**		**3.9**	**3.9**	3.9
Deficit in balance of goods and services	20.2	19.5	20.6			19.6	19.3	19.1	18.8	18.9	18.9		18.9	18.9	
Exports	51.0	50.9	47.8			47.6	47.8	48.1	48.5	48.9	49.2		49.2	49.2	
Imports	71.2	70.3	68.4			67.2	67.1	67.2	67.3	67.8	68.1		68.1	68.1	
Net current transfers (negative = inflow)	-17.8	-17.8	-18.4	-19.0	2.4	-18.4	-18.6	-18.7	-19.0	-19.5	-19.9		-20.1	-20.0	-20.1
of which: official	-1.3	-1.2	-0.8			-0.8	-1.0	-0.9	-0.9	-0.9	-0.9		-0.9	-0.9	
Other current account flows (negative = net inflow)	5.0	6.3	6.6			5.4	5.1	5.0	5.0	5.1	5.1		5.0	5.0	
Net FDI (negative = inflow)	**-5.7**	**-4.6**	**-5.4**	**-5.9**	**1.2**	**-5.0**	**-5.0**	**-4.9**	**-4.9**	**-4.8**	**-4.8**		**-4.8**	**-4.8**	-4.8
Endogenous debt dynamics 2/	**-2.1**	**-0.6**	**0.7**			**0.2**	**0.2**	**0.2**	**0.1**	**0.1**	**0.1**		**0.1**	**0.1**	
Contribution from nominal interest rate	0.5	0.5	0.7			1.2	1.3	1.4	1.5	1.5	1.5		1.4	1.2	
Contribution from real GDP growth	-0.8	-0.9	-0.7			-1.0	-1.1	-1.3	-1.4	-1.5	-1.5		-1.3	-1.1	
Contribution from price and exchange rate changes	-1.8	-0.2	0.7			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**0.1**	**-0.4**	**5.5**			**0.1**	**1.1**	**0.3**	**0.1**	**0.1**	**0.2**		**0.1**	**0.2**	
of which: exceptional financing	0.0	0.0	-0.1			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	30.7			32.7	34.7	35.7	35.8	35.6	35.1		33.3	27.0	
In percent of exports	...	...	64.1			68.6	72.6	74.2	73.8	72.9	71.4		67.7	54.9	
PV of PPG external debt	**...**	**...**	**22.8**			**24.5**	**26.7**	**27.7**	**27.9**	**27.8**	**27.3**		**25.7**	**19.7**	
In percent of exports	**...**	**...**	**47.7**			**51.5**	**55.8**	**57.6**	**57.5**	**56.8**	**55.5**		**52.3**	**40.1**	
In percent of government revenues	**...**	**...**	**103.2**			**104.7**	**112.5**	**113.6**	**113.2**	**112.0**	**110.1**		**103.6**	**79.4**	
Debt service-to-exports ratio (in percent)	**8.3**	**15.8**	**16.9**			**15.9**	**16.8**	**16.9**	**17.4**	**17.5**	**17.7**		**17.9**	**16.3**	
PPG debt service-to-exports ratio (in percent)	**1.9**	**1.4**	**1.6**			**3.3**	**3.6**	**3.9**	**4.6**	**4.9**	**5.3**		**6.0**	**4.9**	
PPG debt service-to-revenue ratio (in percent)	**4.5**	**3.4**	**3.5**			**6.7**	**7.3**	**7.6**	**9.0**	**9.7**	**10.4**		**11.9**	**9.7**	
Total gross financing need (Billions of U.S. dollars)	1.4	2.4	2.4			2.1	2.1	2.1	2.2	2.2	2.2		2.6	4.1	
Non-interest current account deficit that stabilizes debt ratio	7.7	5.6	-0.9			4.7	3.7	4.4	4.7	4.7	4.6		4.6	4.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	3.8	4.1	2.6	4.1	2.7	3.0	3.0	3.3	3.5	3.7	3.7	3.4	3.7	3.7	3.7
GDP deflator in US dollar terms (change in percent)	8.1	0.7	-2.7	4.3	3.6	2.2	0.6	-0.4	-0.2	-0.3	-0.3	0.3	1.4	1.6	1.2
Effective interest rate (percent) 5/	2.3	2.3	2.7	2.4	0.3	3.7	3.7	3.7	3.8	3.8	3.8	3.8	3.9	4.0	3.9
Growth of exports of G&S (US dollar terms, in percent)	24.3	4.6	-6.1	8.2	13.5	4.7	4.1	3.6	4.1	4.2	3.9	4.1	5.1	5.4	4.9
Growth of imports of G&S (US dollar terms, in percent)	24.8	3.5	-2.9	7.8	18.9	3.4	3.5	3.1	3.5	4.1	3.8	3.6	5.1	5.4	4.9
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	13.0	8.5	7.5	13.6	14.0	16.2	12.2	6.5	8.1	8.2
Government revenues (excluding grants, in percent of GDP)	22.0	21.5	22.1			23.4	23.7	24.4	24.7	24.8	24.8		24.8	24.8	24.8
Aid flows (in Billions of US dollars) 6/	0.4	0.4	0.4			0.3	0.3	0.2	0.2	0.1	0.2		0.2	0.3	
of which: Grants	0.2	0.2	0.1			0.2	0.2	0.1	0.1	0.1	0.1		0.1	0.2	
of which: Concessional loans	0.3	0.2	0.2			0.1	0.2	0.1	0.1	0.1	0.1		0.1	0.1	
Grant-equivalent financing (in percent of GDP) 7/	...	...	...			1.5	1.1	0.8	0.8	0.7	0.8		0.6	0.6	0.6
Grant-equivalent financing (in percent of external financing) 7/	...	...	...			33.5	23.9	25.0	29.7	28.2	30.7		19.7	23.5	22.2
Memorandum items:															
Nominal GDP (Billions of US dollars)	17.6	18.5	18.5			19.5	20.2	20.8	21.4	22.2	22.9		27.9	47.1	
Nominal dollar GDP growth	12.2	4.9	-0.1			5.2	3.7	2.9	3.3	3.4	3.4	3.6	5.1	5.4	4.9
PV of PPG external debt (in Billions of US dollars)			4.2			4.7	5.2	5.6	5.8	6.0	6.1		7.1	9.2	
(PVt-PVt-1)/GDPt-1 (in percent)						2.7	3.0	1.8	1.1	0.8	0.4	1.6	0.7	0.5	0.7
Gross workers' remittances (Billions of US dollars)	2.8	2.9	3.1			3.3	3.5	3.6	3.8	4.1	4.3		5.3	8.9	
PV of PPG external debt (in percent of GDP + remittances)	...	...	19.5			20.9	22.7	23.6	23.7	23.5	23.0		21.6	16.6	
PV of PPG external debt (in percent of exports + remittances)	...	...	35.3			37.9	41.0	42.2	42.1	41.3	40.3		37.7	28.9	
Debt service of PPG external debt (in percent of exports + remittan	...	...	1.2			2.4	2.6	2.8	3.3	3.6	3.8		4.3	3.5	

Sources: National authorities and Fund staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Defined as grants, concessional loans, and debt relief.

7/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

8/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table A3. Honduras: Sensitivity Analysis for Key Indicators of Public Debt 2014–34

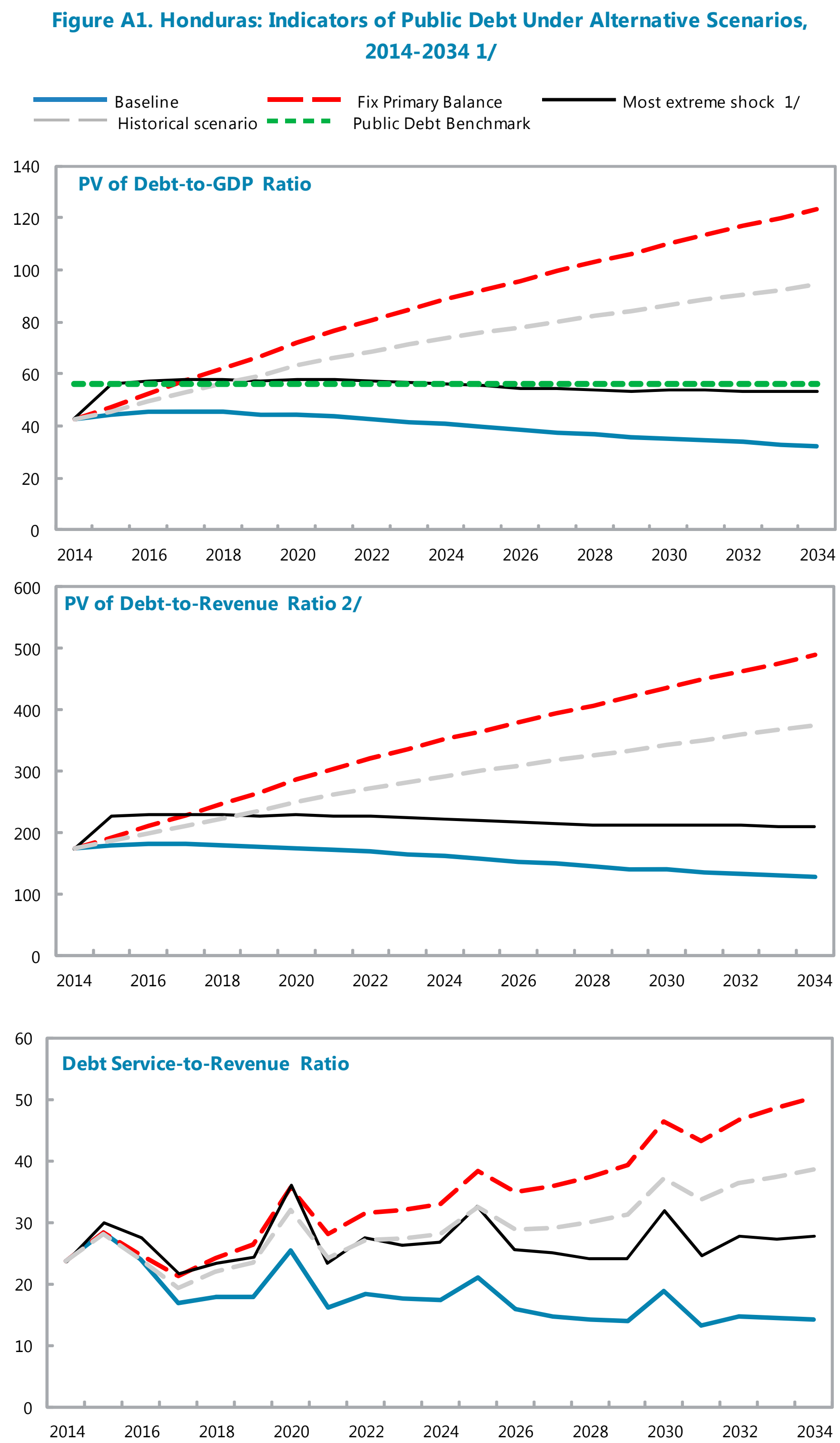
	Projections							
	2014	2015	2016	2017	2018	2019	2024	2034
PV of Debt-to-GDP Ratio								
Baseline	43	44	45	46	45	45	41	32
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	43	46	49	53	56	59	74	94
A2. Primary balance is unchanged from 2014	43	47	53	58	62	67	89	123
A3. Permanently lower GDP growth 1/	43	45	46	47	48	48	51	67
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	43	45	48	49	50	50	50	49
B2. Primary balance is at historical average minus one standard deviations in 2015-201	43	48	53	54	54	53	50	41
B3. Combination of B1-B2 using one half standard deviation shocks	43	47	52	53	53	52	50	43
B4. One-time 30 percent real depreciation in 2015	43	56	57	58	58	57	56	53
B5. 10 percent of GDP increase in other debt-creating flows in 2015	43	54	55	56	56	55	52	43
PV of Debt-to-Revenue Ratio 2/								
Baseline	174	181	182	181	179	177	162	128
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	174	186	198	210	223	236	293	374
A2. Primary balance is unchanged from 2014	174	193	211	229	247	266	352	489
A3. Permanently lower GDP growth 1/	174	182	185	188	189	191	203	264
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	174	185	192	195	197	198	199	195
B2. Primary balance is at historical average minus one standard deviations in 2015-201	174	194	214	214	212	210	197	162
B3. Combination of B1-B2 using one half standard deviation shocks	174	192	209	210	209	207	197	168
B4. One-time 30 percent real depreciation in 2015	174	228	229	229	228	228	223	211
B5. 10 percent of GDP increase in other debt-creating flows in 2015	174	221	222	221	220	218	205	169
Debt Service-to-Revenue Ratio 2/								
Baseline	24	28	24	17	18	18	17	14
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	24	28	24	19	22	23	28	39
A2. Primary balance is unchanged from 2014	24	28	25	21	24	26	33	50
A3. Permanently lower GDP growth 1/	24	28	24	17	19	19	21	27
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-20	24	29	25	18	20	20	21	21
B2. Primary balance is at historical average minus one standard deviations in 2015-201	24	28	25	22	24	21	19	18
B3. Combination of B1-B2 using one half standard deviation shocks	24	28	25	21	23	20	20	19
B4. One-time 30 percent real depreciation in 2015	24	30	28	22	23	24	27	28
B5. 10 percent of GDP increase in other debt-creating flows in 2015	24	28	26	28	20	22	20	19

Sources: National authorities and Fund staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Figure A1. Honduras: Indicators of Public Debt Under Alternative Scenarios, 2014–34 1/



Sources: National authorities and Fund staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2024.
2/ Revenues are defined inclusive of grants.

Table A4. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34

(In percent)

	Projections							
	2014	2015	2016	2017	2018	2019	**2024**	2034
PV of debt-to-GDP+remittances ratio								
Baseline	21	23	24	24	23	23	**22**	17
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	21	22	22	22	22	22	**24**	26
A2. New public sector loans on less favorable terms in 2014-2034 2	21	23	24	25	25	25	**26**	26
A3. Customized scenario /7	21	24	26	28	29	29	**31**	25
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	21	22	24	24	24	23	**22**	17
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	21	26	33	34	34	33	**32**	21
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	21	22	23	23	23	22	**21**	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	21	24	27	27	27	26	**25**	18
B5. Combination of B1-B4 using one-half standard deviation shocks	21	23	25	25	25	24	**23**	17
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	21	30	31	31	31	30	**28**	22
PV of debt-to-exports+remittances ratio								
Baseline	38	41	42	42	41	40	**38**	29
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	38	40	40	40	40	40	**45**	50
A2. New public sector loans on less favorable terms in 2014-2034 2	38	41	43	44	44	44	**46**	46
A3. Customized scenario /7	38	43	47	49	51	51	**54**	43
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	38	40	41	41	40	39	**37**	29
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	38	50	68	68	67	66	**64**	41
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	38	40	41	41	40	39	**37**	29
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	38	45	50	48	47	46	**44**	31
B5. Combination of B1-B4 using one-half standard deviation shocks	38	43	48	48	47	46	**44**	32
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	38	40	41	41	40	39	**37**	29
PV of debt-to-revenue ratio								
Baseline	105	112	114	113	112	110	**104**	79
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	105	108	106	104	103	102	**110**	116
A2. New public sector loans on less favorable terms in 2014-2034 2	105	113	117	119	120	120	**127**	126
A3. Customized scenario /7	105	118	127	134	138	141	**152**	121
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	105	111	115	114	113	111	**106**	81
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	105	127	161	161	160	159	**155**	100
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	105	110	109	109	108	106	**101**	77
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	105	119	129	129	128	126	**122**	86
B5. Combination of B1-B4 using one-half standard deviation shocks	105	113	118	118	117	115	**111**	80
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	105	156	158	157	156	153	**146**	112

Table A4. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34 (continued)

(In percent)

	Projections							
	2014	2015	2016	2017	2018	2019	**2024**	2034
Debt service-to-exports+remittances ratio								
Baseline	2	3	3	3	4	4	**4**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	2	3	3	3	3	3	**4**	4
A2. New public sector loans on less favorable terms in 2014-2034 2	2	3	3	3	3	3	**4**	5
A3. Customized scenario /7	2	3	3	4	4	4	**5**	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	2	3	3	3	4	4	**4**	4
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	2	3	4	5	5	5	**6**	6
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	2	3	3	3	4	4	**4**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	2	3	3	4	4	4	**5**	4
B5. Combination of B1-B4 using one-half standard deviation shocks	2	3	3	4	4	4	**5**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	2	3	3	3	4	4	**4**	4
Debt service-to-revenue ratio								
Baseline	7	7	8	9	10	10	**12**	10
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	7	7	7	8	8	9	**9**	10
A2. New public sector loans on less favorable terms in 2014-2034 2	7	7	7	8	8	9	**12**	13
A3. Customized scenario /7	7	7	8	10	11	12	**15**	15
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	7	7	8	9	10	11	**12**	10
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	7	7	8	11	12	13	**15**	14
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	7	7	7	9	10	10	**12**	10
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	7	7	8	10	11	11	**13**	11
B5. Combination of B1-B4 using one-half standard deviation shocks	7	7	8	9	10	11	**12**	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	7	10	11	13	14	15	**17**	14
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	3	3	3	3	3	3	**3**	3

Sources: National authorities and Fund staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

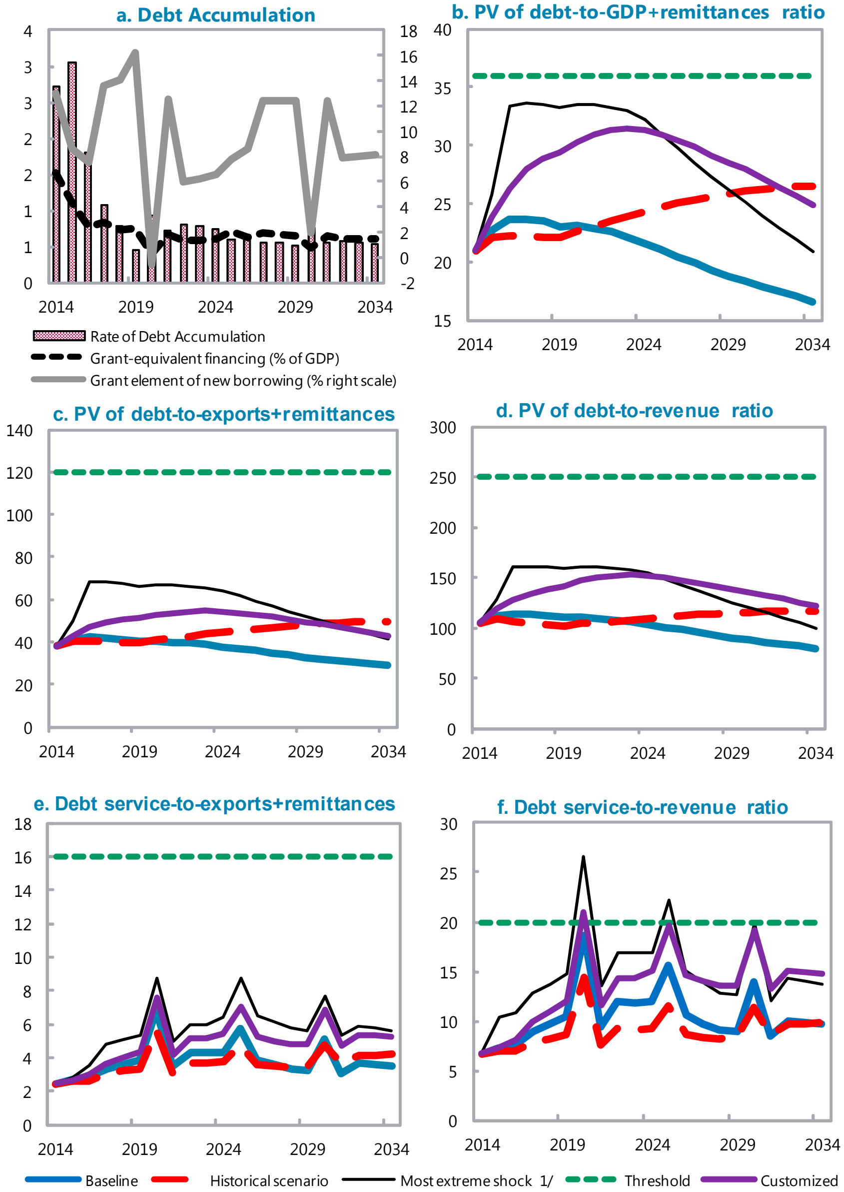
4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

7/ In the customized scenario, (i) real GDP growth is 2.5 percent from 2014 to 2017, and rises 0.2 percentage points per year to reach 3.3 percent in 2021, staying at this level for the remainder of the DSA period; (ii) financing conditions from external capital markets deteriorate permanently, with the rate of interest on Eurobonds rising to 8.5 percent, starting in 2015; (iii) the overall deficit of the CPS increases by 2 percent of GDP in 2015 compared to the baseline (this increase fades out partially at a constant rate of 15 percent during the DSA period, e.g., compared to the baseline, the deficit is higher by 1.7, 1.0 and 0.5 percent of GDP respectively in 2016, 2019 and 2024; and (iv) contingent liabilities (estimated at about 2 percent of GDP) related to existing PPP projects are assumed to fully materialize over the next three years and result in an increase in public external debt.

Figure A2. Honduras: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2014–34 1/



Sources: Country authorities and Fund staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2024. In figure b. it corresponds to a Exports shock; in c. to a Exports shock; in d. to a Exports shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

2/ For the customized scenario see footnote 7/ in table A4.

Appendix II. Letter of Intent

November 19, 2014

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde,

1. Macroeconomic conditions in Honduras weakened in 2013. Economic growth declined to 2.6 percent in 2013 from 4.1 percent in 2012, owing to a drop in coffee production due to leaf-rust disease, less favorable external conditions, and lower private investment from increased uncertainty related to last year's presidential elections. At the same time, the public finances continued to weaken, reflecting higher spending and rising losses by the state-owned electricity company. In the external sector, the current account deficit rose, although international reserves increased due to the placement of sovereign global bonds for US$1 billion.

2. The government that took office in January 2014 is implementing measures to strengthen the public finances and advance structural reforms. A broad set of fiscal measures, aimed mainly at increasing revenue, was approved in December 2013. In addition, we have decided to reduce current spending and transfers, and lower electricity subsidies through better targeting. On the structural side, legislation to reform the electricity sector and pension funds has been enacted, while measures to strengthen tax administration and improve discipline in the budget process have also been adopted. The government has also decided to strengthen the social safety net through increased transfers to low-income groups.

3. The main objective of our 2014–17 economic program is to preserve macroeconomic stability while improving the conditions for sustainable and inclusive economic growth. The main elements of the program include strong fiscal consolidation; structural reforms to strengthen the macroeconomic policy framework and promote economic growth; and measures to strengthen the social safety net. We believe that the policies set forth in the attached Memorandum of Economic and Financial Policies (MEFP) are adequate to achieve the objectives of our program, but we will take any further measures that may become appropriate for this purpose. Honduras will consult with the Fund on the adoption of these measures, and in advance of any revision to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation..

4. In support of our program, we are requesting a 36-month SBA arrangement and a 24-month arrangement under the SCF in the amount of SDR129.5 million (equivalent to 100 percent of Honduras' IMF quota, or about US$200 million at current exchange rates). The SCF/SBA arrangements, which we intend to treat as precautionary, will signal our commitment to implement sound economic policies, allow us to catalyze external financial assistance, and bolster investor confidence.

5. Program implementation will be monitored through semi-annual reviews, with the first one scheduled to be completed by April 2015. The quantitative performance criteria and structural benchmarks under the program are set out in tables 1 and 2 of the attached MEFP. We will provide Fund staff with all information required to monitor program performance and complete program reviews.

6. Consistent with the commitment to keep the public informed, we authorize the IMF to publish this Letter of Intent, its attachments and the related staff report, as well as all future program documents.

Sincerely yours,

/s/	/s/
Marlon Tábora Muñoz	Wilfredo Rafael Cerrato Rodriguez
President, Central Bank of Honduras	Minister of Finance

Attachments

Attachment I. Memorandum of Economic and Financial Policies for 2014–17

Background and Program Objectives

1. Honduras faces significant challenges. Honduras is one of the poorest countries in the region, with a poverty rate of about 60 percent. It also continues to face a difficult, though improving, security situation, with high levels of crime. Amid these long-standing challenges, upon taking office in January 2014, the government of President Hernandez inherited a difficult macroeconomic situation. Economic growth decelerated significantly to 2.6 percent in 2013, driven mainly by exogenous external and domestic factors, including political uncertainty related to last year's presidential elections. The fiscal accounts continued to weaken, with the combined public sector (CPS) deficit rising to 7.6 percent of GDP in 2013, from 2.8 percent of GDP in 2011. This deterioration was driven by higher primary spending and interest payments, as well as by a substantial increase in the deficit of the state-owned electricity company (ENEE). The relaxation of fiscal policy has led to a rapid increase in public debt and to cash-flow pressures. In addition, combined with a real appreciation of the exchange rate and less favorable terms of trade, it has led to a sizeable increase in the external current account deficit and limited reserve coverage.

2. **The government has taken decisive measures to address these challenges.** To support fiscal consolidation, a substantive set of fiscal measures focused on raising revenue (including an increase in the VAT rate from 12 to 15 percent, higher fuel taxes and a reduction in electricity subsidy through better targeting) was approved in December 2013. In addition, the government is implementing measures to restrain spending, including a wage freeze in 2014–15, while protecting the social safety net. At the same time, legislation has been enacted to enable the implementation of key structural reforms, including in the electricity and pension sectors, which would support both fiscal consolidation and long-run growth.

3. **The main objective of our economic program is to preserve macroeconomic stability while improving conditions for sustainable inclusive growth.** Our strategy includes strong fiscal consolidation, aimed at eliminating cash-flow pressures and stabilizing public debt by 2017–18. The improvement in the public finances will also help bolster the external sector position. Our structural reform agenda seek to support fiscal consolidation efforts while strengthening the macroeconomic policy framework and boosting growth. With these objectives in mind, our program includes (i) a substantial increase in tax revenue following the December 2013 tax reform; (ii) strong measures to reduce spending; (iii) significant strengthening of ENEE's financial position; (iv) structural reforms in several key areas (e.g., electricity sector, tax administration, pension funds); and (v) measures to strengthen the social safety net and protect low-income groups.

Recent Economic Development and Outlook

4. **Macroeconomic and fiscal conditions have started to improve.** Economic growth picked up to 2.6 percent through August (up from 2.1 percent in the same period last year). The recovery is being driven by improved investor confidence and more favorable external conditions, factors that have offset the dampening effects of ongoing fiscal consolidation. Annual inflation rose to 6.3 percent in October, up from 4.6 percent a year earlier, mainly due to one-off factors (the December 2013 fiscal measures and a recent spike in food prices due to the effect of a drought). On the fiscal side, the CPS overall deficit declined to 1 percent of GDP through August, about 3.3 percentage points lower than in the same period last year. This improvement was explained by the December 2013 fiscal measures and lower primary spending. The external position has also improved, with a lower current account deficit—reflecting slow import growth and increased remittances—and higher international reserves.

5. **Macroeconomic performance should continue to strengthen during the program period.** We project growth to rise to 3 percent in 2014–15, supported by more favorable external conditions, the dissipation of political uncertainty related to last year's elections, and a recovering coffee sector—factors that would continue to offset the dampening effects of fiscal consolidation. The latter are expected to be relatively modest, given the high degree of openness of the Honduran economy. With sound macroeconomic policies and structural reforms, confidence should continue to strengthen leading to higher private investment. In this context, we expect growth to continue picking up, reaching 3.7 percent by 2018. While we project inflation to rise to 6½ in 2014—reflecting mainly to the one-off effects mentioned above—it should come down next year and stabilize in the 5–6 percent range over the medium term. Our economic program is also expected to lead to a significant reduction in the external current account deficit and a sizeable increase in the level of international reserves.

Fiscal Policy

6. **The program aims at restoring fiscal discipline and putting public debt on a sustainable path.** The fiscal strategy seeks to stabilize public debt ratios by 2017-18 and reduce them thereafter. To achieve this, the program will target a reduction of the CPS overall deficit to 1.8 percent of GDP by 2017. Of this adjustment about 2 percent of GDP will take place in 2014 on the back of measures already in place. The remaining consolidation effort will result from further reducing central government spending, improving the financial situation of ENEE, and higher revenue through tax administration measures.

7. **For 2014 and 2015, we are targeting a CPS deficit of 5.9 and 3.2 percent of GDP, respectively.** A significant portion of this year's consolidation is driven by the increase in revenue from the December 2013 measures. On the spending side, the wage bill and goods and services will bear most of the adjustment. In September, we submitted to congress a draft budget consistent with the program's fiscal targets for 2015 (prior action). This budget will maintain nominal wages

constant, prioritize and optimize capital spending and reduce expenditure in goods and services. After the tax measures of December 2013, we do not anticipate the need to raise tax rates during the remainder of the program period, but we will step up our reform program to improve tax administration. The 2015 budget law will also aim at standardizing benefits for public employees, and this standardization will continue during the remainder of the program until we can address the problem in a more permanent manner through a comprehensive reform of public employment and compensation.

A. Revenue

8. We expect tax revenue to rise by close to 2 percent of GDP during 2014–17. Of this increase, around 1¾ points would come from the measures approved in December 2013, with the remainder stemming from improvements in tax administration. Our program to strengthen tax administration covers the following areas:

- **Large Taxpayer Unit (LTU).** We will strengthen the LTU by hiring new qualified personnel (structural benchmark, September 2015). We also plan to ensure a more efficient use of our resources and better control of the most important taxpayers. To this effect, we will assess the benefits of reducing the number of taxpayers classified as large, and based on this evaluation we will decide whether to reduce the number of such taxpayers. We will significantly increase the coverage of risk-based audits for large taxpayers in the next fiscal year relative to 2014.

- **Tax intelligence and risk analysis unit**. To streamline operations in this unit, we will standardize information and introduce an adequate technology platform (data warehouse).

- **Customs**. Operational management within customs need to be improved to facilitate controls, information sharing, and speed up processes. We aim to establish a business process mapping to define activities and responsibilities, and within this context, a customs manual will be elaborated. In addition, based on the findings of previous IMF technical assistance, we will revisit our procedures to control fuel imports with the goal to have a new system in place by March 2015.

B. Spending

9. **Expenditure reduction plays a key role in our fiscal program.** We are implementing measures to reduce the wage bill, expenditure on goods and services as well as to prioritize and optimize capital outlays, while protecting the social safety net. More specifically, the spending plan includes the following:

- **Wage bill**. Nominal wage rates for 2014–15 will remain at the same level of 2013. However, the wage bill of the CPS will still decline to 12.4 and 11.8 percent of GDP in 2014 and 2015, respectively, from about 12.8 percent of GDP in 2013. For 2016–17, we plan to limit wage increases for all central government employees (including in the health and education sectors) to 5 percent, broadly in line with inflation. Our program also includes a reduction in public sector payroll derived from several initiatives: (i) we have started a program to improve payroll controls by conducting audits in public institutions, aimed at identifying and removing irregular workers. The first step, already underway, is to conduct a comprehensive census to pave the way for the audits. We expect to have the results for the first group of six institutions by December 2014, and for the rest of the institutions by March 2015; (ii) we will eliminate all current non-critical open positions; and (iii) we will close all positions where employees decide to leave the public sector, with the exception of those positions deemed as critical. In addition, in order to gain more control over the payroll, we have issued a resolution to include, for payment purposes, all public employees in the system for financial administration (SIAFI) by June 2015. Finally, we will start a pilot program to reduce public employment by using severance payments. The 2015 budget includes a provision to this end. We view the significant reduction in the wage bill that will result from these measures as key to creating fiscal space under our program to protect social programs and strengthen the social safety net in order to support our poverty reduction efforts (see paragraphs 12-13).

- **Goods and services**. We will reduce spending in goods and services by about ½ percent of GDP throughout the program. To help achieve this, we will impose stricter spending controls to ensure that ceilings set in SIAFI for each institution are met.

- **Capital spending.** We anticipate capital spending to decline from its peak of 5.1 percent of GDP in 2013 to 3.7 percent of GDP in 2017. The adjustment is expected to materialize mainly in 2015. To rationalize capital spending, we are planning to conduct a full review of our investment program to prioritize projects. We will seek to protect those investments that yield the highest contribution to growth.

- **Transfers.** Transfers to decentralized institutions (local governments and the national university) will remain stable in nominal terms at their 2013 level.

10. **Strengthening spending control.** We will create a committee, headed by the chief of the Economic Cabinet and the Finance Minister, to assess spending developments in all institutions of the CPS. The 2014–15 budget laws empower this committee to enforce spending ceilings.

11. **ENEE needs urgent measures to restore its financial sustainability.** The overall deficit of ENEE reached 1.8 percent of GDP in 2013, owing to low tariffs, high technical and non-technical losses, and operational inefficiencies. We plan to use a set of tools to address ENEE's multidimensional problem.

- Under the current institutional set up, tariffs in Honduras are adjusted on a monthly basis to incorporate variations in fuel costs. We recently adjusted tariff by revising the tariff formula to reflect fuel cost increases in the first half of 2014 while also taking into account the fuel price changes that have taken place in recent months. We have also adjusted tariffs to reflect other cost increases during recent years in order to help meet the economic program's fiscal targets, including regarding the operational margin of ENEE. The average tariff will be further adjusted by the new sector regulator (see paragraph 22) by 2.5 percent in 2015. Appendix I provides more details on how the 2015 tariff adjustment will be carried out. Under the new electricity law, the new regulator will also be charged with adjusting tariffs quarterly to reflect current changes in costs.

- In addition, we will reduce technical and non-technical losses by at least 7 percentage points during 2015–17 and lower ENEE's wage bill (net of severance payments) by about ¼ percent of GDP in 2015 by reducing the company's workforce. These wage bill savings will be maintained at least through 2017. Our program provisions for the cost of severance payments (estimated at about 0.2 percent of GDP) associated with the latter measure. The aim of this set of measures is to eliminate ENEE's deficit by 2018.

- We also plan to allow private participation in distribution and transmission by giving these segments in concession under long-term contracts and public-private partnership (PPP) arrangements as conditions allow it over the next few years. This should raise efficiency in the sector, helping promote economic growth, and further reduce technical and non-technical losses.

C. Social Safety Net

12. **We plan to maintain recent levels of social spending to continue supporting our efforts to reduce poverty.** Social spending has been rising in recent years, supported to a large extent by external donors**.** We are aware that social conditions for the most vulnerable need to continue improving. Our program envisages locking in recent increases in social spending by maintaining overall expenditure under our main social programs at 1.6 percent of GDP during 2014–15 while shifting funding toward domestic, revenue sources. An important fraction of this spending will focus on raising living standards for low-income groups by improving their housing (improvements in roofs, floors, and cooking systems to reduce air contamination inside in dwellings) under our new Vida Mejor program. This program is aimed at helping 400,000 families in extreme poverty and is part of a broader government plan that sets development goals for improved governance, human development, and security. We also plan to maintain the electricity subsidy for those consuming less than 75KW per month. In addition, with a view to improving the effectiveness of social spending, we will conduct a review of our current social programs (by June 2015) to ensure that these are properly targeted.

13. **We also plan to reform our pension and healthcare systems to expand coverage in both areas to further bolster our poverty reduction efforts**. Draft legislation providing for this reform was submitted to congress in September. Given our country's fiscal situation, we will ensure that the proposed draft legislation will be amended to minimize its cost, and to be fully consistent with our program fiscal targets and sustainable on an intertemporal basis. In addition, the reform will be implemented gradually. With assistance from the World Bank and the Inter-American

Development Bank (IADB), we will also strengthen the design of the reform to make the new pension and healthcare systems more effective while keeping their costs within the budget.

D. Financing

14. **The program will be financed mainly from external sources.** MDBs have already committed about US$480 million (2.5 percent of GDP) for 2014 and are expected to disburse about US$780 million (3.8 percent of GDP) during 2015–16. In addition, these institutions and the European Union have agreed to disburse about US$220 million in budget support (1.1 percent of GDP) in 2014 upon approval of the IMF program. For 2015–16, we anticipate that financing conditions for Honduras will improve on the basis of our strong fiscal consolidation efforts. Thus, we are planning to tap global markets to meet remaining financing needs. ENEE is planning to borrow US$250 million from local banks in 2014 to finance its deficit. With the program fully financed, we are confident that we will not need to withdraw resources from the IMF.

15. **A loan from the Central American Bank for Economic Integration (CABEI) will be used for liability management.** Our goal is to replace high-interest, short-maturity domestic debt with cheaper and longer-maturity external debt while diversifying the portfolio of pension funds. To this end, we have contracted a US$300 million loan with CABEI to repay government bonds held by pension funds. The loan has a 20-year repayment period and carries a variable interest rate. Under the loan agreement, pension funds will create a trust fund to invest in CABEI loans and invest in projects financed by CABEI. We will ensure that pension funds upgrade their investment policies and governance in line with best international practices to safeguard pension fund resources while achieving adequate returns. We will not contract further loans with CABEI for these purposes during the program period.

16. **Domestic arrears.** Domestic arrears by the public sector were estimated at about 3 percent of GDP by end 2013. These arrears are mainly with suppliers of goods and services, pension funds, and other public entities, and private generators of electricity. We are planning to conduct a full review to assess the validity of these claims (structural benchmark, June 2015) and then clear validated arrears with domestic bonds. The public sector does not have external arrears.

Monetary, Exchange Rate, and Financial Sector Policies

17. **Our monetary policy will aim to keep inflation in check and maintain an adequate level of international reserves.** The central bank (BCH) will seek to keep annual inflation at 5–6 percent. However, for 2014–15 we anticipate a spike in inflation owing to temporary factors (tax measures, higher energy costs, and food price increases due to a drought). The central bank's monetary program is consistent with a prudent expansion of bank credit to the private sector to support the growth objectives of the government. We will control the growth of net domestic credit through active placements of central bank bills, and will not extend new credit to the central government. We will not provide financing to Banhprovi beyond that envisaged under the trust fund approved in 2013. At the same time, we will adopt all necessary measures to ensure that monetary targets are

met. We will also keep the monetary policy rate (TPM) at a positive level in real terms. Monetary conditions will be monitored closely to adjust liquidity as needed to keep inflation under control and the meet program's international reserve targets. Our monetary program envisages that net international reserves will increase by US$60 million in 2014 and by US$140 million in 2015. This will maintain reserve coverage at about 3¾ months of imports. The program also sets a ceiling on net domestic assets of the central bank.

18. **We will continue to improve the operational framework for conducting monetary policy.** The BCH will continue moving in this direction, including by (i) moving toward a system of liquidity forecasting and liquidity management on a daily basis; (ii) improving market-based repo operations for liquidity management, (iii) increasing the signaling content of the TPM; and (iv) phasing out banks' use of government bonds to meet a portion of reserve requirements during the program period. In addition, we plan to adopt international financial reporting standards for the central bank. We envisage continued technical assistance from the IMF to strengthen the central bank's institutional capacity and move forward with these reforms.

19. **Our exchange rate policy will be consistent with the objective of safeguarding competitiveness and strengthening the external position.** We will allow for higher exchange rate flexibility to support the external position and competitiveness, as well as to reduce the dampening effect of fiscal adjustment on economic activity. We will prepare and implement a plan for the gradual removal of foreign exchange surrender requirements (structural benchmark, December 2015). This will help foster the future development of an interbank foreign exchange market and more exchange rate flexibility over the medium term. We will issue the regulations needed to ensure a proper functioning and development of the foreign exchange market.

20. **Recapitalization of the central bank.** To enhance the central bank's ability to pursue effective monetary policy, we will immediately begin implementing the BCH recapitalization program approved by congress in May 2014. The recapitalization will be carried out through non-marketable bonds bearing a positive interest rate in real terms.

21. **We are fully committed to further improving the regulatory framework and supervisory practices in the financial system**. In particular, we plan to: (i) resume publication of the Financial Stability Report; (ii) increase efforts to discourage foreign-currency borrowing by unhedged agents, for which the Superintendency of Banks will adopt additional measures by setting loan-to-value and debt service-to-income ratios that are more stringent for such borrowers. (iii) strengthen the capacity for risk-based supervision; (iv) strengthen the risk-based supervision framework for saving and loans cooperatives; and (v) enact an AML/CFT Law in line with the 2012 FATF standard.

Structural Reforms

22. **Electricity sector.** We have begun to adopt measures to overhaul the electricity sector. A new electricity sector law was enacted in July to promote a more efficient, open and transparent electricity sector. The law also allows for greater private sector participation in transmission, distribution and public lightening through PPP initiatives. Private sector companies already participate in electricity generation. We anticipate that the full implementation of the law could take about 2 years due to the complexity of the process. With support from World Bank, the IADB and bilateral donors, we have started the implementation of the new law, and will issue the key regulations by December 2014. A first step in this process is to create an independent and stronger regulatory entity (CREE) that inter alia will be charged with regulating the operation of the new electricity market, and setting tariffs, access mechanisms and use of the electricity systems, in a more efficient and transparent way, and based on technical criteria. CREE will become fully functional by March 2015.

23. **Telecommunications company (HONDUTEL).** HONDUTEL's financial situation has deteriorated in recent years owing to poor management and increasing competition. We acknowledge that the company faces significant challenges to compete in a high-tech market that is constantly evolving. We plan to restore the financial sustainability of HONDUTEL through its restructuring and private sector participation. In consultation with Fund staff, we will prepare a plan to restore its financial viability by March 2015 (structural benchmark), and implement it during the program period (starting in 2015).

24. **Strengthening fiscal responsibility.** We strongly believe that our fiscal institutional framework should be strengthened, including by establishing an institutional mechanism to lock in the deficit reduction from the implementation of our program. Such mechanism could be developed under the framework of a fiscal responsibility law (FRL), building on the successful experience of some Latin American countries. As a first step in this direction, we will develop a medium-term fiscal framework with a clear fiscal anchor and fiscal policy targets by June 2015 (structural benchmark). This new fiscal framework will be used on the preparation of the 2016 budget. We will then decide on the appropriate timing for the adoption of an FRL.

25. **Fuel prices.** In July, we agreed with fuel suppliers to stabilize retail fuel prices for several months. However, we note that this could distort consumer expectations, creating pressures to demand a permanent subsidy. To prevent this, we will reinstate the automatic mechanism to adjust domestic fuel prices in line with international prices and exchange rate variations (prior action).

26. **Strengthening the framework for PPPs.** We believe that PPPs are important to address infrastructure gaps and support economic growth. However, to limit fiscal costs and risks arising from PPPs and protect the public finances, we will submit to congress legislation to strengthen the framework for PPPs (prior action). This legislation is expected to be approved by December 2014 (structural benchmark). In the meantime, we will refrain from approving new PPP projects. In the new framework, the ministry of finance will have a leading role in project evaluation and approval,

including the power to stop projects that may jeopardize fiscal sustainability. The legislation will thus limit the role of COALIANZA to the promotion and facilitation of PPPs, with the technical and financial assessment of projects also transferred to the ministry of finance. In addition, we are planning to enhance the government's capacity to assess and quantify PPP-related risks by creating a special unit at the ministry of finance. We will also finance COALIANZA directly from the budget and not from fees charged to users. To further limit PPP-related risks, we will repeal legislation that allows issuing government guarantees for debt contracted by private companies involved in PPP projects (structural benchmark, December 2014).

27. **Pension funds and social security institute (IHSS).** We are committed to continue to reform our public pension funds. To this end, we have adopted a parametric reform of the public employees' fund, aimed at reducing its actuarial deficit and strengthening its governance. Building on the experience of our successful pension reform so far we will also reform the IHSS. The preparatory work for this reform is ongoing and we anticipate having the corresponding legislation approved by congress June 2015 (structural benchmark).

Safeguards Assessment

28. **We will request the IMF to update the safeguards assessments of the BCH.** The update will be completed before the first program review. We intend to implement the recommendations that arise from the assessment.

Program Monitoring

29. **Program monitoring.** The program will be subject to semi-annual reviews, and will be monitored through performance criteria, indicative targets, and structural benchmarks, as set out in tables 1 and 2. The first review is expected to be conducted in April 2015 the second review in October 2015, and the third review in April 2016. To facilitate program monitoring, we are committed to provide detailed information as specified in the technical memorandum of understanding (TMU). Relevant definitions and reporting procedures are further specified in the accompanying TMU.

30. **Program Monitoring Committee (PMC).** The PMC—comprising the chief of the economic cabinet, the minister and vice minister of finance, the director of DEI, the president of the CNBS, the chief economist of the Central Bank, the director of *Unidad de Planeamiento y Evaluacion de Gestion* and the treasury director at the ministry of finance—will meet at least once a month to review implementation of the Fund-supported program and consistency of all relevant policy initiatives with the program's objectives. The IMF resident representative will attend the meetings as an observer. The central bank will prepare minutes of the meetings and send them to the IMF resident representative no later than 5 business days after each meeting.

Table 1. Honduras: Performance Criteria 1/

(Cumulative flows; millions of Lempiras, unless specified)

	2014		2015	
	Prel.	PC	PC	PC
	End-Jun.	End-Dec.	End-Jun.	End-Dec.
QUANTITATIVE PERFORMANCE CRITERIA				
Fiscal targets 2/				
Overall balance of the combined public sector (floor)	-2,642	-23,931	-5,256	-14,283
Overall balance of the central government (floor)	-4,365	-22,252	-6,870	-17,873
Overall balance of ENEE (floor) 3/	-2,155	-5,521	-1,491	-3,353
Public debt targets 4/				
Contracting and guaranteeing of new non-concessional loans (continuous ceiling, in million US$)	…	600	600	600
Accumulation of new arrears by ENEE (continuous ceiling)	…	0	0	0
Accumulation of new external arrears (continuous ceiling, in million US$)	0	0	0	0
Monetary targets				
Net international reserves of the Central Bank (floor, in million US$)	2,362	2,271	2,390	2,411
Stock of net domestic assets of the central bank (ceiling) 5/	-28,900	-22,017	-27,001	-22,454
Indicative targets 2/				
Wage bill of the central government (ceiling)	17,945	38,049	18,850	39,248
Social spending (floor)	2,496	7,078	2,834	7,333
Operating revenue-to-spending ratio of ENEE (floor)	…	0.85	0.97	0.97

1/ Definitions as specified in the Technical Memorandum of Understanding.
2/ Cumulative starting in January of the correspondent year.
3/ Excluding government transfers.
4/ Cumulative starting in December 2014. Targets on non-concessional debt and external arrears are for the combined public sector.
5/ Using the program exchange rate of L21.1066 = 1US$.

Table 2. Honduras: Prior Actions and Structural Benchmarks 2014–2015

Measure	Target Date
Prior actions	
Present to congress a 2015 budget bill consistent with the central government and combined public sector deficits targeted under the program	Met
Submit to congress a bill to strengthen the framework for public-private partnerships (PPPs)	Met
Reinstate the automatic mechanism for the adjustment of fuels prices	5 days before Board discussion of program
Structural benchmarks	
Adjust the average electricity tariff by 2.5 percent during 2015 to reflect past cost increases; further adjust tariffs to incorporate current changes in costs (see Appendix I).	Continuous
Approval of legislation to strengthen the PPP framework	December 2014
Repeal legislation allowing the issuance of government guarantees for debt contracted by private companies involved in PPP projects	December 2014
Conduct a census of public employees, with the aim of identifying and cancelling redundant positions during 2015	December 2014
Take actions sufficient to achieve savings in ENEE's wage bill as indicated in paragraph 11.	March 2015
Submit to congress legislation to reform the Social Security Institute (IHSS) to strengthen its actuarial position and improve its governance	March 2015
In consultation with staff, prepare a plan to address the financial difficulties of HONDUTEL	March 2015
Approval of the law reforming the IHSS	June 2015
Complete an audit of public sector arrears, with a view to clearing them	June 2015
Present a program for developing a medium-term fiscal framework with a clear fiscal anchor and fiscal policy targets	June 2015
Present to congress a 2016 budget bill consistent with the program targets for central government and CPS deficits	September 2015
Strengthen the Large Taxpayer Unit with adequate staff levels	September 2015
Present a plan for a gradual removal of foreign exchange surrender requirements	December 2015

Appendix I. Main Policies and Structural Reform Program

E. Public Finances

Budget

- Present to congress a 2015 budget bill consistent with the central government and combined public sector (CPS) deficits targeted under the program (prior action).

- Present to congress 2016–17 budget bills consistent with the central government and CPS deficit targeted under the program (for 2016 budget bill, structural benchmark, September 2015).

- Ensure that the social protection bill will be amended to keep its costs within the budget and bring it for discussion in congress only when it has been made consistent with the program's fiscal targets.

Tax administration

- Strengthen the Large Taxpayer Unit with adequate staff levels (structural benchmark, September 2015); assess reducing the number of taxpayers classified as "large".

- Increase the coverage of risk-based full scope audits for large taxpayers relative to current levels (December 2015).

- Strengthen the tax intelligence and risk analysis units by standardizing information and introducing an adequate technology platform (data warehouse) (structural benchmark, December 2015).

Customs administration

- Establish a business process mapping (BPM) defining activities and responsibilities (March 2015).

- Develop a customs manual based on the BPM (June 2015).

- Strengthen the post clearance and risk management departments (September 2015).

- Strengthen control processes for fuels imports, bulk cargo and exports (March 2015).

Expenditure measures

- Conduct a census of public employees (structural benchmark, December 2014), with the aim of identifying and cancelling redundant positions during 2015.

- Limit recruiting to levels consistent with budget ceilings (2015–17).

- Maintain central government wages constant in nominal terms in 2014-15, and limit annual increases in employee compensation to a maximum of 5 percent for all central government workers in 2016–17.

- Keep transfers to local government and other public entities stable in nominal terms (2014–17).

- Adopt a mechanism to strengthen expenditure controls, including by bringing central government employees into SIAFI, and improve treasury liquidity management (March 2015).

- Assess bringing employees from decentralized institutions into SIAFI (June 2015) with the aim of implementing this initiative during the remainder of the program period.

Arrears

- Complete an audit of public sector arrears, with a view to clearing them (structural benchmark, June 2015).

Fiscal framework

- Submit to congress legislation to strengthen the legal framework for public-private partnerships (PPPs) and stop the approval of new PPP projects until this reform is approved (prior action).

- Approval of the above-mentioned bill (structural benchmark, December 2014).

- Repeal legislation allowing the issuance of government guarantees for debt contracted by private companies involved in PPP projects (structural benchmark, December 2014).

- Present a program for establishing of a medium-term fiscal framework (MTFF) with a clear fiscal anchor and targets (June 2015).

- Assess the appropriateness of adopting fiscal responsibility legislation based on the MTFF (December 2015).

- Start implementing the MTFF in budget preparations (September 2015).

Electricity Sector and HONDUTEL

- Adjust the average electricity tariff by 2.5 percent in July 2015 to reflect adjustment lags from past increases in costs; further adjust tariffs quarterly to reflect current changes in costs.[1]

- Adopt measures sufficient to reduce ENEE's wage bill (net of severance payments) by about ¼ percent of GDP.

- Issue key implementing regulations for the new general electricity sector law (December 2014).[2]

- Establish a fully functional Regulatory Committee for Electrical Energy (CREE) (March 2015).

- In consultation with staff, prepare a plan to address the financial difficulties of HONDUTEL (March 2015).

- Start implementation of the plan to address HONDUTEL's financial difficulties (September 2015).

- Conduct audits of the financial statements of ENEE and HONDUTEL through an internationally-recognized firm (September 2015).

Pension funds

- Submit to congress legislation to reform the Social Security Institute (IHSS) to strengthen its actuarial position and improve its governance (structural benchmark, March 2015).

- Approval of the law reforming the IHSS (structural benchmark, June 2015).

- Approve the implementing regulations for the law reforming the public employees' pension fund (INJUPEMP) (December 2014).

- Strengthen regulations governing investments by pension funds (June 2015).

[1] The 2.5 percent increase will be calculated over the average tariff in place in December (that is, 3.70 lempiras per KWH), and will exclude other adjustments for current changes in costs applied during 2015. Specifically, the increase in 2015 derived from the 2.5 percent adjustment will be about 0.09 lempiras per KWH.

[2] These comprise (i) the general regulations to the law; (ii) CREE's internal regulations; (iii) regulations governing the electricity sector operator; and (iv) regulations for the price regime and system access and use.

F. Financial Sector

- Adopt additional measures aimed at reducing currency mismatches by unhedged borrowers by setting loan-to-value and debt service-to-income ratios that are more stringent for such borrowers (March 2015).
- Resume publication of Financial Stability Report (March 2015).
- Enact AML/CFT legislation in line with the 2012 FATF standard (June 2015).

G. Monetary Sector

Exchange rate policy

- Allow for higher exchange rate flexibility within the current exchange rate regime (November 2014).
- Present a plan for a gradual removal of foreign exchange surrender requirements (structural benchmark, December 2015).
- Lift in steps surrender requirements to the BCH and allow interbank foreign exchange transactions (precise timing to be defined after presentation of plan).
- Elaborate regulations needed to ensure a proper functioning and development of the foreign exchange market by (precise timing to be defined after presentation of plan to remove FX surrender requirements).

Monetary policy and framework

- Cease central bank financing to Banhprovi beyond the level envisaged under the trust fund approved in 2013 (2014–2017) and reform legislation to prohibit central bank financing to it (December 2015).
- Abstain from central bank lending to the public sector (continuous).
- Gradually modernize the operational framework of monetary policy, including for adjusting the policy interest rate with a view to achieving the inflation and international reserves targets (2014–2017).
- Adopt international financial reporting standards for the central bank (Precise timing to be defined after the completion of the safeguards assessment).
- Implement the program to recapitalize the central bank (2014–17).

H. Social Policies

- Complete a review of the "*Bono 10 mil*" and "*Vida Mejor*" social programs to ensure that they are adequately targeted to low-income families (June 2015).

Attachment II. Technical Memorandum of Understanding

1. This memorandum sets out technical understandings between the Honduran authorities and the Fund staff for monitoring of the economic program agreed for the period November 2014–November 2017. It defines the concepts used to assess observance of quantitative performance criteria, structural benchmarks, and indicative targets specified in Tables 1 and 2 of the Memorandum of Economic and Financial Policies (MEFP). It also specifies the frequency of the data to be provided to the Fund to monitor the developments under the program.

I. Program Assumptions

2. For program monitoring purposes, unless otherwise indicated, U.S. dollar denominated components of the balance sheet of the Central Bank of Honduras will be valued at the exchange rate of L21.1066/US$ exchange rate at end-August 2014. Amounts denominated in other currencies will be converted for program purposes into U.S. dollar amounts using the cross-rates as of end-August 2014 published on the IMF website http://www.imf.org, including US$/EUR = 1.3188, JPY/US$ = 103.71, CHF/US$ = 0.9145, CAD/US$ = 1.0858, SDR/US$ = 0.6586.

J. Fiscal Targets

3. **The deficit of the combined public sector (CPS)** will be measured from the financing side (i.e., "below the line"), and will correspond to the net borrowing of the CPS, from both external and domestic sources, excluding payment of arrears accumulated until December 2013. The CPS comprises the nonfinancial public sector (NFPS) and the operating result (quasi-fiscal balance) of the central bank. The NFPS covers the central government, local governments and decentralized agencies, the social security institute (IHSS), the public pension funds (INJUPEMP, INPREMA, IPM), and the public enterprises. For the purposes of the program, the public enterprises will comprise the State Electricity Company (ENEE), the State Telecommunications Company (HONDUTEL), the State Water and Sewerage Company (SANAA), and the State Ports Company (ENP).

4. **The deficit of the central government** also will be measured from the financing side, excluding payment of arrears accumulated until December 2013. The central government includes the executive, judicial, and legislative branches, and the so-called decentralized agencies (desconcentradas) (Table B).

5. **The current primary expenditure of the central government** is defined as total current expenditure less interest payments.

6. **The central government wage bill** is defined as all central government wages and salaries, including severance payments, plus employer social security and pension contributions; other remunerations (such as bonus payments and in-kind compensations) are also included in the definition.

7. **Social spending** is defined as the programs and projects of social content that are financed with domestic resources, debt relief, grants and loans. (See Table C).

8. **The deficit of ENEE** will be also measured from the financing side. For program purposes, it will be defined excluding transfers from the central government to the company.

9. **The operating margin of ENEE** will be defined as the ratio of operating revenue to operating expenditure. Operating revenue will be defined as total current revenue minus transfers from the central government. Operating expenditure will be defined as total expenditure excluding interest payments and capital spending.

10. **The operating balance of the public enterprises** is defined as the difference between the operating revenue (excluding interest earnings and transfers) and the operating expenditure (excluding interest payments and transfers) of the enterprises.

11. **Net domestic financing of the CPS** will be measured as the operating result of the central bank and the change (relative to end-December 2013) in the stocks of: (1) outstanding indebtedness of the NFPS (direct bank credit plus bank holdings of public sector bonds less deposits) to the domestic financial system (central bank, commercial banks, and other financial institutions); (2) outstanding public sector bonds held outside the financial system; (3) repatriation of deposits held abroad; and (4) outstanding suppliers' credit and floating debt (un-cashed and undelivered checks, and unpaid invoices and orders) of the central government, and unpaid orders of the rest of the NFPS. For the purposes of the program, domestic financial system is defined as comprising all depositary institutions, according to the Monetary and Financial Statistics Manual (MFSM) definition.

12. **Discrepancies.** The authorities will undertake periodic reconciliations to minimize discrepancies between above-the-line and below-the-line financing data. As needed, such reconciliations must be carried out prior to completion of the program reviews.

13. **Adjustor.** If tax revenues were to exceed those projected under the program for 2014 and 2015, at least 50 percent of the excess revenue will be saved and the residual will be allocated as counterpart to social and/or capital projects (Paragraph 7, Table C).

K. Monetary Targets

14. **Net International Reserves (NIR) of the central bank (program definition).** For program purposes, the NIR of the central bank will be measured as gross international reserves that are readily available minus (i) short-term reserve liabilities (including purchases and credits from the Fund), as described in the international reserves table prepared by the central bank according to the MFSM; (ii) foreign assets that are counterpart of foreign currency deposits of financial institutions at the central bank and of any other liability of the central bank with residents that is payable in foreign currency; (iii) any conversion of short-term reserve liabilities; and (iv) the transfer to the central bank of foreign currency deposits held abroad by HONDUTEL, INJUPEMP, and IHSS, which amounted to US$98 million at end-August 2014. Readily available reserves also exclude those assets that are

pledged or otherwise encumbered, including but not limited to reserve assets used as collateral or guarantee for a third-party external liability. NIR will be valued at program accounting exchange rates.

15. **Net domestic assets (NDA) of the central bank** will be measured as the difference between currency issue and NIR, both measured on the basis of end-of-period data.

16. **Adjustor**. Starting in 2014, the target floor on NIR will be adjusted downwards (the target ceiling on net domestic assets of the central bank will be adjusted upwards) by up to US$100 million for the shortfall of programmed external disbursements to the budget (including from sovereign bond placements). In case of an excess during the program period, the target floor on NIR will be adjusted upwards (the target ceiling on domestic assets of the central bank will be adjusted downwards) by the full such amount. The external disbursements contemplated in the program are to be received from the World Bank, IADB, and the European Union totaling US$473 million between 2014 and 2017.

L. External Targets

17. **External debt.** For program purposes, the definition of debt is the one set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to External Debt (Executive Board's Decision No. 6230-(79/140), as amended by Decision No 14416-(09/91, effective December 1, 2009). This definition applies also to commitments contracted or guaranteed for which value has not been received, and to private debt for which official guarantees have been extended and which, therefore, constitute a contingent liability of the public sector. Excluded from this definition are normal import-related credits, defined as liabilities that arise from the direct extension, during the normal course of trading, of credit from a supplier to a purchaser—that is, when payment of goods and services is made at a time that differs from the time when ownership of the underlying goods or services changes. Normal import credit arrangements covered by this exclusion are self-liquidating; they contain pre-specified limits on the amounts involved and the times at which payments must be made; they do not involve the issuance of securities. For the purpose of the program, external debt is defined on the basis of residency.

18. **Debt definition**. The definition of debt set forth in No. 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements reads as follows:

(a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the

obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in point (a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt give rise to new debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

19. **Definition of public debt**. For the purpose of the program, public sector debt is defined as the debt of the combined public sector excluding the debt of local governments.

20. For purpose of the program, the guarantee of a debt arises from any explicit legal obligation of the general government or any other agency acting on behalf of the general government to service such a debt in the event of nonpayment by the recipient (involving payments in cash or in kind), or from any implicit legal or contractual obligation to finance partially or in full any shortfall incurred by the debtor.

21. **Concessionality** will be calculated using a unified discount rate of 5 percent and taking into account all details of the loan agreement, including maturity, grace period, payment schedule, upfront commission, and management fees. The grant element of loans can be calculated using the concessionality calculator available at the IMF web site http://www.imf.org.[10] For program purposes, a debt is **concessional** if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rate used for this purpose is 5 percent.

22. **Borrowing on nonconcessional terms**. For the purposes of the program, this continuous ceiling applies to the contracting or guaranteeing of nonconcessional external debt by the CPS or any other agencies on its behalf.[11] Debt denominated in currencies other than the U.S. dollar shall be converted to the U.S. dollars using program assumptions on bilateral exchange rates. The

[10] Currently available at http://www.imf.org/external/np/pdr/conc/calculator/default.aspx.

[11] This includes short-term external debt (with an original maturity of up to and including one year) and non-concessional medium- and long-term debt with original maturities of more than one year.

continuous ceiling applies not only to debt as defined above, but also to commitments contracted or guaranteed for which value has not been received. This ceiling will be adjusted downwards by the amount of programmed disbursements that change into concessional resources.

23. **Exclusions**. Excluded from the non-concessional external debt continuous ceiling are: (i) debts classified as international reserve liabilities of the Central Bank, (ii) debts to restructure, refinance, or prepay existing debts, (iii) use of Fund resources (iv) short-term import financing (with a maturity of less than one year), and (v) central bank instruments placed in the domestic market held by nonresidents.

24. **Stock of external debt arrears**. For the purpose of the program's continuous ceiling, external debt service arrears are defined as overdue debt service arising in respect of obligations incurred directly or guaranteed by the public sector, except on debt subject to rescheduling or restructuring, as indicated by the respective creditors. The CPS will accumulate no external debt arrears during the program period.

M. Energy Sector

25. **Arrears of ENEE** are defined as overdue payments of ENEE to private and public entities. During the program period, no new arrears to the private sector will be accumulated, excluding technical delays stemming from the payment process. Technical delays are defined as the maximum period allowed for the payment of suppliers' and/or contractors' invoices to ENEE without incurring arrears, in line with the law on public contracts (Decree 74-2001). This period extends up to 45 days, starting from submission of appropriate documents for payment.

N. Monitoring and Reporting Requirements

26. **The information required to monitor the compliance with quantitative and structural benchmarks** specified in the MEFP will be supplied to the Fund at least monthly (electronically, to the extent possible) and within 45 days of the end of the previous month (unless otherwise noted) according to the sources detailed in the next paragraph.

27. **The ceilings on the deficit of the central government and of the CPS** will be monitored below-the-line on the basis of the monthly reports *Financiamiento de la Administración Central* and *Financiamiento del Sector Público Combinado*, respectively, prepared by the central bank, which contain:

- **Net external financing** of the central government and the NFPS, respectively, with detailed information on disbursements, amortizations, exceptional financing, zero coupon bonds, and accumulation of arrears. This information will be prepared by the central bank and reconciled with the Ministry of Finance.

- **Net domestic financing** of the central government and the NFPS, respectively, with detailed information on: (1) net domestic financing from the central bank and the rest of the financial system to the central government and the NFPS, as contained in the *Balance diario*; (2) net placement of bonds (including stabilization bonds) by the central government and the NFPS outside the financial system, as reported by the central bank with data from the Public Credit Directorate of the Ministry of Finance; (3) change in foreign currency deposits held abroad by the central government and the NFPS; and (4) change in the outstanding stock of suppliers' credit and floating debt of the central government, as reported by the Treasury, and the rest of the NFPS as reported by the central bank. To monitor the net domestic financing to the CPS, the central bank will provide the Fund with detailed data on a cash basis on the operating revenue and expenditure of the central bank.

28. **The ceilings on the wage bill of the central government** will be monitored monthly on the basis of the Ministry of Finance report: *Sueldos y salarios de la administracion central*.

29. To complement the monitoring of fiscal performance, a breakdown of tax revenue by type of tax will also be provided monthly.

30. **Social spending (Table C)** will be monitored quarterly on the basis of financial reports provided by the Ministry of Finance.

31. **The overall balance of ENEE** and its nonaccumulation of arrears will be monitored monthly on the basis of financial reports provided by the Ministry of Finance.

32. **The floor on NIR and the ceiling on NDA of the central bank** will be monitored on the basis of information produced by the central bank, in accordance with the new presentation of the MFSM. This information will be provided within two weeks of the end of the previous month.

33. **The ceilings on the contracting of nonconcessional external debt and on the nonaccumulation of external payments arrears** will be monitored with information provided by the Ministry of Finance. The accounting of non-reschedulable external debt-service arrears by creditor (if any), with detailed explanations, will be transmitted by the Ministry of Finance on a monthly basis within four weeks of the end of each month. Moreover, a loan-by loan accounting of all new loans contracted or guaranteed by the public sector, including detailed information on the amounts, currencies, and terms and conditions, as well as relevant supporting materials, will be transmitted by the central bank on a quarterly basis within four weeks of the end of each quarter.

34. **Implementation of structural measures in the program** will be monitored monthly based on information provided by the central bank, the Ministry of Finance, and the Banking and Securities Commission.

Table A. Data to be Reported to the IMF

Item	Periodicity
I. Fiscal Data	
Net external financing: detailed information on disbursements, amortizations, exceptional financing, zero coupon bond, and accumulation of arrears.	Monthly, within 45 days of the end of each month.
Net domestic financing of the central government and the NFPS: detailed information on (1) net domestic financing from the central bank and the rest of the financial system to the central government and the NFPS, (2) net placement of bonds by the central government and the NFPS outside the financial system, (3) change in foreign currency deposits held abroad by the central government and the NFPS; and (4) change in the outstanding stock of suppliers' credit and floating debt of the central government, as reported by the Treasury, and the rest of the NFPS as reported by the central bank.	Monthly, within 45 days of the end of each month.
Monitoring of net domestic financing to the central government will require that the central bank provide the Fund with detailed data on a cash basis on the operating revenue and expenditure of the central bank.	Monthly, within 45 days of the end of each month.
Monitoring of net domestic financing to the CPS will require that the central bank provide the Fund with detailed data on a cash basis on the operating revenue and expenditure of the central bank.	Monthly, within 45 days of the end of each month.
Overall balance of ENEE and arrears (if any, with detailed explanations)	Monthly, within 45 days of the end of each month.
Wage bill of the central government.	Monthly, within 45 days of the end of each month.
Breakdown of tax revenue by type of tax	Monthly, within 45 days of the end of each month.
Social spending	Quarterly, within 45 days of the end of each quarter.

Detailed information on: Revenues and expenditures of the central government. Revenues and expenditures of the NFPS, including the operating balance of public enterprises. Revenues and expenditures of ENEE.	 Monthly, within 45 days of the end of each month. Quarterly, within 45 days of the end of each month. Monthly, within 45 days of the end of each month.
II. Monetary Data	
Detailed information on the Central Bank balance sheet, including Net International Reserves and Net Domestic Assets.	Monthly, within 2 weeks of the end of each month.
Detailed information on domestic liabilities of the central bank payable in foreign currency, including change in foreign currency deposits of public enterprises in the central bank.	Monthly, within 2 weeks of the end of each month.
III. External Debt	
Loan-by loan accounting of all new loans contracted or guaranteed by the public sector, including detailed information on the amounts, currencies, and terms and conditions, as well as relevant supporting materials	Quarterly, within four weeks of the end of each quarter.
The accounting of arrears on external debt-service by creditor (if any), with detailed explanations.	Monthly, within four weeks of the end of each month.
IV. Additional Data	
Balance of Payments statistics	Quarterly, within three months of the end of each quarter.

Table B. Decentralized Agencies of the Public Sector

Programa de Asignación Familiar
Fondo Hondureño de Inversión Social
Instituto de la Propiedad
Programa Nac. de Prevención Rehabilitación y Reinsercion Soc
Instituto Nacional de la Juventud
Instituto Nacional de Conservación y Desarrollo Forestal
Instituto de Acceso a la Información Pública
Instituto Hondureño de Geología y Minas
Comisión Permanente de Contingencias
Cuerpo de Bomberos de Honduras
Empresa Nacional de Artes Gráficas
Instituto Nacional Penitenciario
Centro Nacional de Educación para el Trabajo
Ente Regulador de Servicios de Agua Potable y Saneamiento
Dirección Investigación y Evaluación de la Carrera Policial
Comisión Nacional de Telecomunicaciones
Comisión Administradora Zona Libre Turística Islas de la Bahia
Dirección Ejecutiva de Ingresos
Dirección de la Marina Mercante
Fondo Víal
Direccion de Ciencia y Tecnología Agropecuaria
Dirección Nacional de Desarrollo Rural Sostenible
Fondo Nacional de Desarrollo Rural Sostenible
Programa Nacional de Desarrollo Rural y Urbano Sostenible
Comisión Nacional de Energía
Centro de la Cultura Garinagu de Honduras
Procuraduría del Ambiente y Recursos Naturales

Table C. Main Social Programs

Description
***Bono Diez Mil* and *Vida Mejor* Programs**
Bono Diez Mil
Vida Mejor
Other social investment expenditures and programs
Honduran Social Investment Fund (FHIS)
Community Education Program (PROHECO)
Family allowances program (PRAF)
Healthy schools program (Free school meals)
Free tuition
Social work scholarships
Transportation education bond
Social aid to persons
Patronatos Aldeas y Caserios, NGOs
Academic excellence scholarships
Various scholarships
Other scholarships and programs

INTERNATIONAL MONETARY FUND

HONDURAS

November 20, 2014

REQUEST FOR A STAND-BY ARRANGEMENT AND AN ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY—INFORMATIONAL ANNEX

Prepared By The Western Hemisphere Department

CONTENTS

FUND RELATIONS

(As of September 30, 2014)

Membership Status: Joined: December 27, 1945

General Resources Account:	**SDR Million**	**% Quota**
Quota	129.50	100.00
Fund holdings of currency (Exchange Rate)	120.87	93.34
Reserve Tranche Position	8.63	6.66

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	123.85	100.00
Holdings	89.18	72.01

Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
ECF Arrangements	5.09	3.93

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-By	10/01/2010	3/31/2012	64.75	0.00
SCF	10/01/2010	3/31/2012	64.75	0.00
Stand-By	04/07/2008	03/30/2009	38.85	0.00
ECF[1]	02/27/2004	02/26/2007	71.20	40.68
ECF[1]	03/26/1999	12/31/2002	156.75	108.30

Projected Payments to Fund
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2014	2015	2016	2017	2018
Principal	1.02	3.05	1.02		
Charges/Interest	0.00	0.02	0.01	0.01	0.01
Total	**1.02**	**3.07**	**1.03**	**0.01**	**0.01**

[1] Formerly PRGF.

Implementation of Enhanced HIPC Initiative: Enhanced Framework

Commitment of HIPC Assistance	
Decision point date	June 30, 2000[2]
Assistance committed (NPV terms)	End-1999
Total assistance (US$ million)	556.00
Of which: IMF assistance (US$ million)	30.30
Completion point date	April 2005

Disbursement of IMF Assistance (SDR million)

Amount disbursed	22.66
Interim assistance	8.80
Completion point balance	13.86
Additional disbursement of interest income	3.70
Total Disbursements	**26.36**

Implementation of MDRI Assistance

Total Debt Relieve (SDR million)[3]	107.46
Of which: MDRI	98.24
HIPC	9.21

Debt Relief by Facility (SDR million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
January 2006	N/A	107.46	107.46

Exchange Rate Arrangement. Honduras' de jure exchange arrangement is a crawling band, and the de facto exchange rate regime is a crawl-like arrangement. The exchange rate of the lempira is determined by foreign exchange auctions of the Central Bank of Honduras (BCH). The BCH maintains an operational band requiring all bid prices for the purchase of foreign exchange to be within a range of 7 percent above or below the base price, with such prices subject to the requirement that bids in auctions not exceed 1 percent of the average base price from auctions during the preceding seven business days. The base price is revised weekly according to a procedure established by the BCH board of directors for this purpose, which includes the following variables: (1) the differential between the domestic inflation rate and the estimated inflation rates of

[2] World Bank Board, July 6, 2000.

[3] The Multilateral Debt Relief Initiative (MDRI) provides 100 percent debt relief to eligible member countries that are qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Honduras's main trading partners, (2) changes in the exchange rates of these countries' currencies vis-à-vis the U.S. dollar, and (3) the performance of official reserve assets. In July 2011, the BCH reactivated the crawling band system that had been in operation until mid-2005. As a result, following a long period of stability, the lempira was allowed to crawl once again in July 2011 and thereafter has followed a slow depreciating trend against the U.S. dollar.

Honduras has accepted the obligations under Article VIII, Section 2, 3, and 4 of the Articles of Agreement, and maintains a system that is free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation. The last Article IV consultation with Honduras was concluded on June 9, 2014.

FSAP participation and ROSCs. Fiscal ROSC conducted on February 26–March 2, 2001 (IMF Country Report No. 02/16) and updated (IMF Country Report No. 05/256). Data ROSC data conducted on July 8–24, 2003 (IMF Country Report No. 05/230). FSAP conducted on October 14–19, 2002 and January 20–February 4, 2003. FSAP Update conducted on September 24 to October 9, 2007.

Safeguards Assessments. The latest safeguards assessment for the Banco Central de Honduras was completed on March 4, 2011. The assessment concluded that the main risk to central bank autonomy—lending to government that exceed limits in the BCH law—was being addressed by program commitments but should ultimately be resolved through changes in legislation. Other key recommendations included securing capacity building for IFRS implementation, strengthening the external audit framework, and modernizing the internal audit function.

Technical Assistance. Honduras has received substantial technical assistance. The table below details assistance provided since November 2012.

Department	Purpose	Time of Delivery
MCM	Central Bank Accounting	Nov 2012
MCM	Bank Supervision & Regulations	Nov 2012
MCM	Bank Supervision and Regulations	Feb 2013
MCM	Monetary and Foreign Exchange Policy	Apr 2013
MCM	Bank Supervision and Regulation	Apr 2013
MCM	Bank Supervision and Regulation	May 2013
MCM	CAPTAC-DR: Building of a Model of Inflation Forecasts	Nov 2013
MCM	Bank Supervision and Regulations	Nov 2013
MCM	CAPTAC-DR: Hedging Derivatives	Dec 2013
MCM	CAPTAC-DR: Building a Model for Structural Liquidity Forecasts	May 2014
MCM	CAPTAC-DR: Treasury Management	Jul 2014
MCM	CAPTAC-DR: Bank Supervision and Regulation	Jul 2014
MCM	CAPTAC-DR: Treasury Management	Oct 2014
FAD	Public Financial Management	Nov 2012
FAD	MTEF Implementation	Nov 2012
FAD	Budget Execution and Cash Planning	Jan 2013
FAD	Customs Administration	Jan 2013
FAD	Tax Administration	Mar 2013
FAD	Customs Administration	Apr 2013
FAD	Public Financial Management	Aug 2013
FAD	Tax Administration	Aug 2013
FAD	Budget Execution and Arrears Control	Sept 2013
FAD	Managing Fiscal Risks	Sep 2013
FAD	Customs Administration	Nov 2013
FAD	Tax Administration	Dec 2013
FAD	Financial Programming and Analyzing Fiscal Risks	Feb 2014
FAD	Public Financial Management	Feb 2014
FAD	Strengthening the Medium-term Expenditure Framework	Feb 2014
FAD	Customs Administration	Apr 2014
FAD	Tax Administration	Apr 2014
FAD	Modernization of Revenue Administration	Jul 2014
FAD	Tax Administration	Oct 2014
STA	Balance of Payments	Nov 2012
STA	CAPTAC: Export/Import Price Index and PPI	Feb 2013
STA	Migration to GFSM 2001	Feb 2013
STA	CAPTAC: National Accounts 2008 SNA	Mar 2013

STA	CAPTAC: Balance of Payments Statistics and IIP	May 2013
STA	CAPTAC: National Accounts-Construction Data Sources	Jul 2013
STA	CAPTAC: Balance of Payments	Nov 2013
STA	CAPTAC: Producer Price Index	Dec 2013
STA	CAPTAC: National Accounts-Statistics and Construction Data Sources	Mar 2014
STA	CAPTAC: Coordinated FDI and Portfolio Surveys	Mar 2014
STA	External Debt Statistics	Jun 2014
STA	Balance of Payments and IIP Statistics	Jul 2014

RELATIONS WITH THE WORLD BANK GROUP

(As of October 21, 2014)

The World Bank Group's Board discussed the current joint IDA/IFC Country Partnership Strategy for the Republic of Honduras for FY2012–FY2014 on December 6, 2011. The CPS provides the strategic identifies the key areas in which Bank Group support can best assist Honduras in achieving sustainable development and poverty reduction for the period. The CPS was designed to continue supporting the Honduras Country Vision and National Plan adopted in 2010. The strategic objectives of the CPS are to: (i) improve citizen security; (ii) expand opportunities and reduce vulnerabilities (social, economic, and climate); and (iii) enhance good governance. On May 8, 2013 the World Bank Group's Board considered the Progress Report, assessing implementation of the CPS at mid-term. While the CPS remained relevant, the WBG extended the CPS by 12 months to allow more time to achieve CPS outcomes and work with the incoming administration on the next partnership strategy. IDA 16 resources have been focused on poverty reduction, including delivering services in poor communities and strengthening the Government's social protection program; improving public sector performance and improving citizen security. In line with their regional strategy, the IFC program continued its focus on the financial sector, infrastructure, agribusiness, public private partnerships, investment climate and competitiveness. The investment lending program has materialized largely as expected, and reflects strong continuity with the existing portfolio. Portfolio implementation has improved, including a notable increase in disbursement rates.

Under the current strategy, the Bank's activities help Honduras adopt a balanced and comprehensive approach to reducing violence, combining the traditional focus on control and punishment with a new emphasis on prevention contributing to the achievement of improvements in citizen security and to strengthening evidence-based decision-making at both national and local levels. A large number of CPS outcomes and targets are clustered under the Expand opportunities and reduce vulnerabilities strategic objective. Fiscal consolidation was achieved during the first year of the CPS, a better investment climate (especially transport/logistics for trade), strengthened education quality and social protection and better disaster risk management. The results sought with respect to reducing the fiscal burden of the state-owned Electricity Company (ENEE) have not been achieved at this time though progress has been made in laying the policy and institutional groundwork for future improvements. Planned outcomes with respect to education quality improvement have been largely achieved and targets aimed at improving coverage and governance of Honduras´ National Conditioned Cash Transfer Social Protection Program (*Bono Vida Mejor*, formerly *Bono 10,000*) have been achieved. Ongoing activities are supporting public sector financial management practices, increased participation of Small Micro Entrepreneurs increase access to agriculture markets, land titling, and improved logistics in transport.

The ongoing program is supported with IDA lending in the order of SDR 109.5 million approximately US$171 million over FY12-14 (which coincides with the IDA 16 cycle). Complementary, IFC has committed US$638.9 million to support private sector-led growth, out of which US$535.7million is IFC's own account and the remaining US$103.3million mobilized from other lenders. IFC financing has contributed to foster access to finance for approximately 30,000 micro, small and medium enterprises (MSMEs) and expanded or improved access to electricity for approximately 140,000 people. Furthermore, IFC has 10 advisory service programs for private sector and the Government in amount of US$3.1million aimed at building capacity of financial intermediaries, supporting development of PPPs, improving investment climate conditions in Honduras and training small and medium business to become more productive and sustainable.

IFC is actively supporting the electricity sector through the financing of renewable energy projects and also advising one of the local trustees commissioned by the GoH in the preparation of the PPP for distribution of electricity.

A. Projects

The Bank active portfolio is made of 10 projects totaling close to 390mUS$ of which 243 million disbursed. The portfolio is rather mature, and by early 2016 the Bank expects to have 5 projects only disbursing.

Honduras Rural Competitive Project (COMRURAL). The Project Development Objective of COMRURAL is to contribute to increased productivity and competitiveness among organized rural small-scale producers through their participation in productive alliances.

Honduras Water and Sanitation Sector Modernization Project (PROMOSAS). The PDO of PROMOSAS is to support the Recipient to improve: (a) the sustainability, efficiency, and reliability of its WSS services in Eligible Municipalities; (b) the performance of its national WSS sector institutions in the exercise of their respective roles in accordance with the WSS Sector Framework Law; and (c) its capacity to respond promptly and effectively to an Eligible Emergency.

Power Sector Efficiency Enhancement Project (PROMEF). The PDO is to improve ENEE's operational and financial performance, thus contributing to the sustainability of the power sector in Honduras.

Second Land Administration Project. Provide improved, decentralized land administration services, including better access to and more accurate information on property records and transactions.

Roads Rehabilitation and Improvement. Improve the quality of road network and of road management in support of the government's growth and competitiveness goals through: (i) Improved governance and enhanced road management capacity in INSEP (former SOPTRAVI) and the Road Fund; (ii) Improvement in selected road corridors; and (iii) Extension in the scope of the maintenance of the unpaved road network; and (iv) improvement of the Recipient capacity to respond promptly and effectively to an eligible emergency

Improving Public Sector Performance. To strengthen the management of public finances and to establish a more efficient, effective and transparent public procurement system through: (i) upgrading the public financial management system; (ii) upgrading the e-procurement platform; (iii) enhancing the internal control systems over personnel expenditures; and (iv) building capacity of the Central Administration.

Social Protection. To: (a) improve the institutional capacity of Recipient's institutions to manage the Conditional Cash Transfer (CCT) Program, by strengthening transparent mechanisms and instruments for targeting Program beneficiaries, monitoring compliance with Program co-responsibilities, and making payments to Program beneficiaries; (b) provide income support to Eligible Beneficiaries; (c) increase the use of preventive health services and school attendance in grades 1 to 6 among Program beneficiaries in rural areas; and (d) improve the Recipient's capacity to respond promptly and effectively to an Eligible Emergency.

Safer Municipalities. Support Honduras (i) to improve the capacities of national and local actors in violence prevention, (ii) to ensure urban municipalities are addressing crime and violence risk factors, and (iii) to respond promptly and effectively to an eligible emergency.

Disaster Risk Management. Support Honduras to: (a) continue strengthening its capacity for integrated disaster risk management at the municipal and national level; and (b) improve its capacity to respond promptly and effectively to an eligible emergency.

Rural Infrastructure. The objectives of the Project are: (a) to improve the access, quality and sustainability of infrastructure services (roads, water, sanitation and electricity) for the rural poor in the Recipient's territory; (b) to develop capacities and an enabling environment within the Recipient for locally-driven infrastructure service provision and planning; and (c) to improve the Recipient's capacity to respond promptly and effectively to an Eligible Emergency.

B. Non-Lending Activities

Economic and Sector Work. Honduras benefits from a comprehensive series of completed, ongoing and planned analytical and advisory activities to support the CPS' pillars. Recently completed economic and sector work includes: a "Honduras Public Expenditure Review: Towards Restoring Fiscal Consolidation" (2013); a poverty and inequality report titled "*Centroamérica en el Nuevo Milenio: Seis Historias Diferentes de Pobreza y Desigualdad*" (2013) with a chapter on Honduras; a series of Policy and Sectoral Notes titled "Towards Fiscal Stability and Sustainable Development for a Better Life" (2014); a "Honduras Gender Assessment" (2014); and a "Debt Management and Performance Assessment" (2014)

C. Financial Relations

Project	Loan	Approved Amount (USD Eq)	Percent Disbursed	Approval Date	Sign Date	Undisbursed Balance (USD Eq)	Disbursed Outstanding Balance (USD Eq)	Closing Date
HONDURAS ROAD REHABILITATION AND IMPROVEMENT II (Additional Financing)	IDA 45830	25,000,000.00	81.18%	21-May-09	2-Aug-10	3,819,237.03	16,469,551.17	31-Dec-14
HONDURAS ROAD REHABILITATION AND IMPROVEMENT II	IDA 44660	48,600,000.00	97.03%	17-Jun-08	13-Oct-08	1,305,104.08	42,658,887.92	31-Dec-14
Power Sector Efficiency Enhancement Project (PROMEF)	IDA 45360	30,000,000.00	77.80%	22-Jan-09	27-Feb-09	6,158,639.96	21,586,203.64	30-Jun-15
Honduras Rural Competitiveness Project	IDA 44650	30,000,000.00	74.73%	17-Jun-08	17-Sep-08	5,254,657.94	15,539,122.06	30-Nov-15
Improving Public Sector Performance	IDA 50200	18,200,000.00	15.01%	6-Dec-11	7-Dec-11	14,769,592.03	2,608,066.97	31-Dec-15
Social Protection (Additional Financing)	IDA 52940	12,300,000.00	10.69%	8-Aug-13	26-Aug-13	10,877,431.31	1,301,782.69	31-Dec-15
Social Protection	IDA 47740	40,000,000.00	93.17%	29-Jun-10	2-Aug-10	2,686,511.74	36,673,143.26	31-Dec-15
HN Rural Infrastructure Project (Additional Financing)	IDA 52890	20,000,000.00	9.75%	19-Jun-13	12-Jul-13	17,828,732.08	1,925,358.92	30-Jun-16
HN Rural Infrastructure Project	IDA 40990	47,000,000.00	100.00%	7-Jul-05	16-Nov-05	0.00	47,528,640.00	30-Jun-16
HN Water and Sanitation Sector Modernization Project (Additional Financing)	IDA 52700	10,000,000.00	9.71%	19-Jun-13	12-Jul-13	8,984,940.32	966,368.68	31-Dec-16
HN Water and Sanitation Sector Modernization Project	IDA 43350	30,000,000.00	98.79%	21-Jun-07	16-Nov-07	356,397.83	29,051,948.17	31-Dec-16
Second Land Administration Project	IDA 46410	32,800,000.00	75.74%	30-Jun-11	23-Aug-11	7,386,327.99	23,061,707.01	30-Jan-17

HN Safer Municipalities	IDA 51920	15,000,000.00	7.30%	13-Dec-12	18-Dec-12	13,493,402.22	1,062,243.78	31-Aug-18
Disaster Risk Management Project	IDA 51900	30,000,000.00	10.85%	13-Dec-12	18-Dec-12	22,401,778.38	2,725,805.60	30-Apr-19

Period	Disb. Amt. US dollars	Repay Amt. US dollars	Net Amt. US dollars	Charges US dollars	Fees US dollars
Jan 2004 - Dec 2004	124,993,399.88	26,631,377.19	98,362,022.69	13,384,750.51	891,813.61
Jan 2005 - Dec 2005	151,277,671.07	81,949,113.22	69,328,557.85	12,269,288.49	1,497,989.24
Jan 2006 - Dec 2006	57,559,309.34	7,670,153.72	49,889,155.62	6,125,782.48	544,575.44
Jan 2007 - Dec 2007	45,593,696.79	0.00	45,593,696.79	2,659,538.45	483,934.13
Jan 2008 - Dec 2008	51,133,214.53	0.00	51,133,214.53	0.00	3,336,665.56
Jan 2009 - Dec 2009	49,366,580.43	0.00	49,366,580.43	0.00	2,988,997.79
Jan 2010 - Dec 2010	108,874,081.26	206,291.01	108,667,790.25	0.00	4,115,824.21
Jan 2011 - Dec 2011	134,874,013.63	2,216,075.80	132,657,937.83	0.00	4,668,739.38
Jan 2012 - Dec 2012	79,525,717.39	2,925,066.67	76,600,650.72	648,194.77	5,343,130.05
Jan 2013 - Dec 2013	90,226,017.05	3,428,128.16	86,797,888.89	1,072,187.71	6,185,978.29
Jan 2014 - Oct 2014	32,462,389.28	4,079,209.61	28,383,179.67	1,106,545.82	5,142,924.02
Report Total	**925,886,090.65**	**129,105,415.38**	**796,780,675.27**	**37,266,288.23**	**35,200,571.72**

STATISTICAL ISSUES

(As of October 2014)

Assessment of Data Adequacy for Surveillance

General: Data provision is broadly adequate for surveillance, although it has some shortcomings. Data on the banking system, the public finances, trade, and external debt broadly satisfy minimum criteria required for surveillance and program monitoring purposes. However, timely and comprehensive data on public enterprises' financial operations, widening the coverage of financial institutions, improving estimate of arrears and floating debt of public entities, enhancing reporting of government guarantees and fiscal contingent liabilities, and a consistent and reliable method to estimates of private capital flows would strengthen surveillance work.

National accounts: The Central Bank of Honduras (BCH) compiles the national accounts estimates following the *System of National Accounts 1993* (*1993 SNA*), rev. 4. The base year is 2000. The BCH has published quarterly GDP data that are fully consistent with the new annual series. The BCH developed a special account to measure the tourism sector with more detail and is in the process of updating the input-output matrix with 2014 data (expected to be published during the second semester). The BCH is working in adopting the national account framework 2008 SNA, supported by TA from an independent consultant and CAPTAC.

Price statistics: The BCH prepares and publishes (since April 2000) the consumer price index (CPI), with reference period December 1999 = 100. The selection of products included in the CPI basket and corresponding weights are based on the National Survey on Household Income and Expenditure of 1998–1999. The BCH also revised the producer price index by expanding its coverage and updating its base and classification, in the framework of the revision of the national accounts; preliminary estimations of this index were made and the release of this index is expected soon. However, this index excludes goods for processing activities (maquila), and includes trade and transport margins, making it difficult to use it in the compilation of national accounts at constant prices.

Government finance statistics: The Ministry of Finance (SEFIN) compiles and disseminates government finance statistics (GFS) covering central administration, central government, general government, and nonfinancial public sectors. The above-the-line data of these sectors are reported to WHD, along with below-the-line data for central administration and nonfinancial public sector, which are provided by the BCH. Issue related to the recording of debt relief hinders the quality of below-the-line data. Currently, the SEFIN and the BCH are participating in the GFS harmonization project for Central America, Panama, and Dominican Republic. Under this project, country participants will elaborate and publish comparable GFS across countries to permit a comparative analysis of fiscal developments and facilitate the regional policy dialogue. The components of the projects are: (i) compilation and dissemination of GFS sub-annual and annual using the GFSM 2001 framework, and (ii) preparation of a detailed migration plan for gradual adoption of the full GFSM 2001 framework. A mechanism to collect data systematically of arrears and floating debt of public entities, particularly public enterprises are needed.

Monetary statistics: Monetary and financial statistics (MFS) are reported on a regular monthly basis to STA using the standardized report forms (SRFs) for the central bank, other depository corporations, and other financial corporations. The cross sectoral data consistency between MFS and other data sets is the major issue that should be addressed by the authorities. The authorities report seven out of 12 core financial soundness indicators and only one of the encouraged set.

Balance of Payments: In line with STA recommendations, the BCH has published consistent gross official reserves and international liquidity data in national and Fund's publications. Honduras disseminates its monthly Reserves Data Template on the Fund's website. Currently Honduras compiles and disseminates Coordinated Direct Investment Survey (CDIS) data, while the BCH is working towards compiling the Coordinated Portfolio Investment Survey (CPIS). The BCH are on time with its working program to compile public and private external debt data on an accrual basis. The work plan of the BCH on external sector statistics include: (a) improving the coverage of external debt figures; (b) achieving consistency between gross external debt by sectors and IIP statistics, and; (c) expanding coverage of outward direct investment. The process of automatic reporting of import and export forms of the free trade areas has been completed. Currently, the BCH, with support from CAPTAC, are in the process of implementing the BPM6 and the System of National Accounts 2008.

Data Standards and Quality: Honduras has participated in the General Data Dissemination System (GDDS) since September 29, 2005 and its metadata are posted on the Data Standards Bulletin Board (DSBB). A Report on the Observance of Standards and Codes—Data Module, Response by the Authorities, and Detailed Assessments Using the Data Quality Assessment Framework was published on the IMF website in July 2005.

Honduras: Table of Common Indicators Required for Surveillance

(As of October 24, 2014)

	Date of latest observation	Date received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of publication	Memo Items: Data Quality Methodological soundness	Memo Items: Data Quality Accuracy and reliability
Exchange Rates	10/23/14	10/24/14	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	10/23/14	10/24/14	D	M	D		
Reserve/Base Money	10/23/14	10/24/14	D	M	D		
Broad Money	8/31/14	10/24/14	M	M	M		
Central Bank Balance Sheet	10/23/14	10/24/14	D	M	D		
Consolidated Balance Sheet of the Banking System	8/31/14	10/24/14	M	M	M		
Interest Rates[3]	8/31/14	10/03/14	M	M	M		
Consumer Price Index	9/30/14	10/17/14	M	M	M		
Revenue, Expenditure, Balance and Composition of Financing[4]—General Government[5]	6/30/14	7/25/14	Q	Q	Q		
Stocks of Central Government and Central Government-Guaranteed Debt[6]	6/30/14	7/25/14	Q	Q	Q		
External Current Account Balance	6/30/14	10/03/14	Q	Q	Q		
Exports and Imports of General Goods	7/31/14	10/15/14	M	M	M		
GDP/GNP	2013	9/30/14	A	A	A		
IIP	6/30/14	10/03/14	Q	Q	Q		

[1] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

[2] Any reserve assets that are pledged of otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[3] Both market-based and officially-determined, including discounts rates, money market rates, rates on treasury bills, notes and bonds.

[4] Foreign, domestic bank, and domestic nonbank financing.

[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[6] Including currency and maturity composition.

INTERNATIONAL MONETARY FUND

COM COMMUNICATIONS DEPARTMENT

Press Release No. 14/545
FOR IMMEDIATE RELEASE
December 4, 2014

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$113.2 Million Stand-By Arrangement and US$75.4 Million Stand-By Credit Facility for Honduras

The Executive Board of the International Monetary Fund (IMF) yesterday approved a US$113.2 Stand-By Arrangement and a US$75.4 arrangement under the Stand-By Credit Facility[1] (SBA/SCF) for Honduras for a combined SDR 129.5 million (about US$188.6 million or 100 percent of Honduras's quota). The arrangements are intended to support the authorities' three-year economic program, which aims to maintain macroeconomic stability and improve conditions for sustainable economic growth and poverty reduction.

The Executive Board's decision makes available a total of SDR 38.85 million (about US$56.6 million) and the remainder in six varying tranches upon completion of semi-annual program reviews. The Honduran authorities plan to treat the arrangements as precautionary.

Following the Executive Board's discussion on Honduras, Mr. Min Zhu, Deputy Managing Director and Acting Chair, made the following statement:

"The Honduran authorities' program, which is supported by an SBA/SCF arrangement with the Fund, aims at preserving macroeconomic stability—by further strengthening fiscal and external positions—and improving the conditions for sustainable and inclusive growth.

"Sustained fiscal consolidation will be necessary to reduce the country's large fiscal deficit and contain public debt. The authorities began moving in this direction with the implementation of tax policy measures earlier this year, followed by expenditure reductions and steps to improve the financial position of the state electricity company. Looking forward, efforts should focus on further reducing current expenditure, improving tax administration, and strengthening the

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[1] The SCF provides financing to low-income countries on concessional terms.

electricity company's finances. The authorities' program also seeks to protect social spending and public investment, mainly by shifting the composition of public expenditure away from inefficient current outlays.

"Sound monetary policy and exchange rate flexibility will help keep inflation in check and protect international reserves. Exchange rate flexibility would also protect competitiveness and ease the cost of fiscal adjustment. The presence of currency mismatches by borrowers calls for more stringent macroprudential measures to reduce risks in the banking sector.

"Structural reforms are an essential component of the authorities' program. Key reforms are being implemented in the electricity sector, pensions, and the framework for public-private sector partnerships. The authorities are also expanding the social safety net, which would support efforts to reduce poverty."

Recent economic developments

The government that took office in January 2014 has vowed to reduce macroeconomic imbalances, promote inclusive economic growth, and improve domestic security.

Macroeconomic conditions have been improving in 2014. Real economic activity rose by 2.6 percent from January–August (compared with 2.1 percent in the same period last year). The effects of ongoing fiscal consolidation on economic growth have been offset by more favorable external conditions and increased private investment related to the dissipation of political uncertainty (from last year's elections) and improved confidence. The fiscal position has also strengthened. The combined public sector deficit declined to 1 percent of GDP in January–August, from 3.3 percent of GDP in the same period last year. Driven by the December 2013 fiscal measures and weather-related factors, inflation increased to about 6.3 percent in October (4.6 percent in the previous year). The balance of payments has shown signs of improvement, with an improving trade balance, solid growth of remittances, and higher international reserves.

Growth of monetary aggregates remains moderate. The central bank has kept the policy rate and reserve requirements unchanged while withdrawing liquidity through open market operations and helping keep credit growth at about 10 percent. In the year ending September, the lempira depreciated by about 3 percent, which resulted in a small appreciation in real effective terms. For 2015, real GDP growth is expected to remain at 3 percent, with supportive external conditions, further improvements in confidence and a recovering coffee sector continuing to offset the effects of fiscal adjustment. Inflation is projected to fall to 5.8 percent in 2015, as the one-off effects that pushed it up in 2014 dissipate. The external current account deficit would decline to about 7 percent of GDP, reflecting more favorable external conditions and the effects of fiscal consolidation. International reserve coverage is expected to rise slightly to 3.8 months of imports. The combined public sector deficit is expected to continue to decline, falling to somewhat above 3 percent of GDP in 2015.

Program Summary

The government's economic program seeks to preserve macroeconomic stability by strengthening the fiscal and external positions, while improving conditions for sustainable inclusive growth. It is also expected to bolster investor confidence and catalyze resources from multilateral institutions and donors.

On the fiscal side, the program seeks to restore discipline and contain public debt growth, which would require reducing the overall balance of the combined public sector from around 7½ percent of GDP in 2013 to about 2 percent of GDP in 2017. To help achieve this, the authorities plan a reduction in the ratio of the wage bill to GDP over the next three years while keeping the level of spending in key social programs to preserve the expansion that these programs experienced in recent years. In particular, the government plans to use part of this spending on improving housing for low-income families under its recently-established Vida Mejor program, which will consolidate existing social programs (notably the conditional cash-transfer program *Bono 10 mil*). Part of the savings from reductions in the wage bill will be allocated to *Vida Mejor*.

Monetary policy will be managed proactively to keep inflation in check and help strengthen the external position. The central bank has adopted a plan to modernize its policy framework, which includes improving short-term liquidity management and enhancing the reporting of monetary and economic data necessary for decision making by the open market operations commission.

Finally, structural reforms are expected to play a crucial role in supporting fiscal consolidation and improving growth prospects. The program comprises reforms in the electricity sector, including ENEE; the telecommunications company (HONDUTEL); and the Social Security Institute. In addition, with IMF technical assistance, the National Tax Directorate (DEI) plans to implement a program to strengthen tax administration.

Honduras became a member of the IMF on December 27, 1945, has an IMF quota of SDR 129.5 million (about US$188.6 million).

Honduras: Selected Economic Indicators

	2010	2011	2012	2013	Proj. 2014	Proj. 2015
		(Annual percentage change, unless otherwise indicated)				
National income and prices						
GDP at constant prices	3.7	3.8	4.1	2.6	3.0	3.0
GDP deflator	4.7	7.8	3.6	1.5	5.3	5.7
Consumer prices (eop)	6.5	5.6	5.4	4.9	6.5	5.8
Exchange rate (eop, depreciation -)						
Lempiras per U.S. dollar 1/	19.0	19.0	19.5	20.4	21.0	...
Real effective rate 2/	4.3	1.8	-1.7	0.4	1.2	...
Money and credit						
Private sector credit	3.5	9.6	16.9	11.2	9.9	10.5
Broad money	9.4	12.7	6.6	8.4	10.2	10.6
Lending rate (eop, in percent) 2/	15.1	14.2	16.7	16.9	16.9	...
Deposit rate (eop, in percent) 2/	8.0	7.4	11.4	11.0	9.9	...
		(In percent of GDP, unless otherwise indicated)				
Combined public sector						
Noninterest revenue and grants	22.7	21.8	21.1	21.3	22.8	22.9
Noninterest expenditure	26.1	24.8	25.4	28.4	28.0	25.0
Primary balance	-3.4	-3.0	-4.3	-7.1	-5.2	-2.1
Capital expenditure	5.3	5.6	5.5	6.4	6.2	4.5
Overall balance	**-2.8**	**-2.8**	**-4.2**	**-7.6**	**-5.9**	**-3.2**
Public sector debt 3/	**29.8**	**32.1**	**34.4**	**45.1**	**47.8**	**49.4**
Of which: External debt	18.0	18.1	19.7	28.1	29.7	31.8
Public sector external debt service (in percent of nonmaquila exports)	3.9	4.4	3.0	2.8	7.3	7.9
Savings and investment						
Gross fixed capital formation	21.6	24.4	24.4	25.6	25.6	25.3
Gross national savings	17.2	16.5	15.8	16.0	17.7	18.2
External sector						
Gross international reserves (millions of dollars)	2,921	3,043	2,778	3,255	3,329	3,507
GIR (In months of imports) 4/	3.6	3.6	3.3	3.7	3.7	3.8
External current account balance	-4.3	-8.0	-8.5	-9.5	-7.8	-7.1
Exports, f.o.b. (annual percentage change)	29.8	27.3	4.8	-6.6	4.7	3.9
Imports, f.o.b. (annual percentage change)	20.8	24.9	2.2	-3.7	3.2	3.4

Sources: Central Bank of Honduras, Ministry of Finance, and IMF staff estimates and projections.

1/ 2014 data as of October.

2/ 2014 data as of August.

3/ Debt series revised based on more comprehensive data series provided by the authorities in September 2012.

4/ Refers to the following year's imports of nonmaquila goods and nonfactor services.

Honduras: Selected Economic Indicators

	2010	2011	2012	2013	Proj. 2014	Proj. 2015
	(Annual percentage change, unless otherwise indicated)					
National income and prices						
GDP at constant prices	3.7	3.8	4.1	2.6	3.0	3.0
GDP deflator	4.7	7.8	3.6	1.5	5.3	5.7
Consumer prices (eop)	6.5	5.6	5.4	4.9	6.5	5.8
Exchange rate (eop, depreciation -)						
Lempiras per U.S. dollar 1/	19.0	19.0	19.5	20.4	21.0	...
Real effective rate 2/	4.3	1.8	-1.7	0.4	1.2	...
Money and credit						
Private sector credit	3.5	9.6	16.9	11.2	9.9	10.5
Broad money	9.4	12.7	6.6	8.4	10.2	10.6
Lending rate (eop, in percent) 2/	15.1	14.2	16.7	16.9	16.9	...
Deposit rate (eop, in percent) 2/	8.0	7.4	11.4	11.0	9.9	...
	(In percent of GDP, unless otherwise indicated)					
Combined public sector						
Noninterest revenue and grants	22.7	21.8	21.1	21.3	22.8	22.9
Noninterest expenditure	26.1	24.8	25.4	28.4	28.0	25.0
Primary balance	-3.4	-3.0	-4.3	-7.1	-5.2	-2.1
Capital expenditure	5.3	5.6	5.5	6.4	6.2	4.5
Overall balance	**-2.8**	**-2.8**	**-4.2**	**-7.6**	**-5.9**	**-3.2**
Public sector debt 3/	**29.8**	**32.1**	**34.4**	**45.1**	**47.8**	**49.4**
Of which: External debt	18.0	18.1	19.7	28.1	29.7	31.8
Public sector external debt service (in percent of nonmaquila exports)	3.9	4.4	3.0	2.8	7.3	7.9
Savings and investment						
Gross fixed capital formation	21.6	24.4	24.4	25.6	25.6	25.3
Gross national savings	17.2	16.5	15.8	16.0	17.7	18.2
External sector						
Gross international reserves (millions of dollars)	2,921	3,043	2,778	3,255	3,329	3,507
GIR (In months of imports) 4/	3.6	3.6	3.3	3.7	3.7	3.8
External current account balance	-4.3	-8.0	-8.5	-9.5	-7.8	-7.1
Exports, f.o.b. (annual percentage change)	29.8	27.3	4.8	-6.6	4.7	3.9
Imports, f.o.b. (annual percentage change)	20.8	24.9	2.2	-3.7	3.2	3.4

Sources: Central Bank of Honduras, Ministry of Finance, and IMF staff estimates and projections.

1/ 2014 data as of October.

2/ 2014 data as of August.

3/ Debt series revised based on more comprehensive data series provided by the authorities in September 2012.

4/ Refers to the following year's imports of nonmaquila goods and nonfactor services.