INTERNATIONAL MONETARY FUND

IMF Country Report No. 18/206

HONDURAS

June 2018

2018 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR HONDURAS

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2018 Article IV consultation with Honduras, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its May 30, 2018 consideration of the staff report that concluded the Article IV consultation with Honduras.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on May 30, 2018, following discussions that ended on April 13, 2018, with the officials of Honduras on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 17, 2018.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF and the International Development Association.
- A **Statement by the Executive Director** for Honduras.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

Press Release No. 18/268
FOR IMMEDIATE RELEASE
June 29, 2018

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Concludes 2018 Article IV Consultation with Honduras

On May 30, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Honduras.

Honduras successfully concluded its 2014-2017 Fund-supported program. The program was instrumental in restoring investor confidence and reducing macroeconomic imbalances. It also catalyzed important structural reforms such as the modernization of the fiscal policy framework which is now anchored by a fiscal responsibility law (FRL).

Boosted by domestic demand, mainly private consumption supported by record remittances inflows and public investment, the economy grew 4¾ percent in 2017, well above expectations. Headline inflation picked up to 4¾ percent from 3¼ percent in 2016 on the back of strong demand and rising oil prices. Honduras' external position remains strong. International reserves were equivalent to 5.3 months of imports of goods and services at end-2017, within the Fund adequacy metrics.

The fiscal deficit increased slightly from ½ percent of GDP in 2016 to ¾ percent of GDP in 2017, still below the deficit ceiling of the FRL (1½ percent of GDP). Public revenues were boosted by a ½ percent of GDP windfall stemming from a series of tax amnesties granted after the introduction of the new tax code.

Monetary policy was accommodative in 2017 resulting in an increase in credit to the economy of 9½ percent. Modernization of the exchange rate regime continued as the authorities reduced surrender requirements by additional 10 percent (20 percent up to date) Financial indicators suggest that banking system is sound. As of end-2017, the 13¾ percent banks' capital adequacy ratio was well above the regulatory minimum, and non-performing loans ratio was at historical lows (2¼ percent at end-2017).
In 2018-19, growth is expected to hover around 3¾ percent reflecting worsening external conditions. The fiscal deficit would remain somewhat below the FRL ceiling as the

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

authorities plan to limit the increase in public debt further. The current account deficit would widen to about 4 percent of GDP both in 2018 and 2019 as remittances' growth moderates and oil prices rise.

Key risks include tighter global financial conditions, due to the normalization of the U.S. monetary policy, and more restrictive U.S. immigration policies. Honduras is also vulnerable to domestic political polarization and potential deterioration in the institutional framework.

Executive Board Assessment[2]

The Executive Directors commended the authorities for the successful completion of the Fund-supported program. Directors noted the reduction in macroeconomic imbalances and the institutional enhancements, particularly the Fiscal Responsibility Law (FRL), under the program. These gains are critical factors for a favorable medium-term outlook. Looking forward, Directors underscored the need for deeper reforms to entrench macroeconomic stability and place Honduras on a higher, more inclusive growth path.

Directors supported the authorities' near-term policy mix. A more prudent fiscal stance than required under the FRL will send an important signal of the commitment to maintain macroeconomic stability. Directors also welcomed the readiness to unwind the supportive monetary policy stance, if needed, to further anchor inflation expectations and contain inflationary pressures. These policies are particularly important in the context of downside risks from tightening global financial conditions, worsening terms of trade, and uncertainties related to overseas immigration policies.

Directors stressed the need for continued ambitious fiscal reforms and revenue mobilization efforts to boost potential growth, further expand the social safety net and reduce poverty. They noted the positive results of the conditional cash transfers program and its envisaged expansion within the ceilings of the FRL. A comprehensive review of large tax expenditures, and rationalization of expenditures is called for. Directors cautioned against the adverse effects of repeated tax amnesties on compliance and revenue mobilization efforts. Stronger efforts to resolve the financial situation of the state electricity company, right-size the wage bill, and enhance the transparency and efficiency of public expenditure will also be critical.

Directors welcomed the progress made toward the modernization of monetary policy, including the reductions in surrender requirements and the introduction of collateralized transactions in the interbank market. Directors recommended speeding up the adoption of the new central bank law to enshrine the primacy of inflation as a monetary policy target. They

---

[2] At the conclusion of the discussion, the Managing Director, as Chair of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

also recommended efforts to deepen the money and foreign exchange markets to support the development of domestic capital markets, as well as more exchange rate flexibility that will provide a cushion against external shocks.

Directors welcomed the stability of the banking system and commended the progress made toward adopting Basel III standards. They recommended sustained implementation of the Financial Sector Stability Review recommendations. Relatedly, Directors called for careful monitoring of household debt, the concentration of consumer loans in public pensions fund portfolios, and the expansion of development banks toward first-tier operations. They also underscored the need for a further strengthening of the AML/CFT framework.

Directors underscored the need to implement supply-side reforms to boost competitiveness, growth, and job creation. They noted that strengthening the rule of law is critical to improve the business environment. Directors acknowledged the ongoing progress in fighting corruption in collaboration with international agencies and recommended enhancing the transparency of the current asset disclosure regime for public officials. Directors underscored the need for continued efforts to reduce red tape and increase the ease of doing business.

Directors emphasized the need to update national statistics for effective policy formulation and welcomed the progress made by the authorities.

Honduras: Selected Economic Indicators

(Annual percent change unless otherwise indicated)

	2013	2014	2015	2016	Prel. 2017	Proj. 2018	Proj. 2019
National income and prices							
GDP at constant prices	2.8	3.1	3.8	3.8	4.8	3.7	3.7
GDP deflator	1.4	6.8	6.9	3.5	4.2	4.2	4.3
Consumer prices (eop)	4.9	5.8	2.4	3.3	4.7	5.0	4.5
Exchange rate (eop, depreciation -)							
Lempiras per U.S. dollar [1/]	20.7	21.6	22.4	23.5	23.6	23.8	...
Real effective rate [2/]	0.2	3.8	1.8	-2.3	-1.5	-1.2	...
Money and credit							
Private sector credit	11.2	10.7	10.4	10.6	9.4	10.8	10.6
Broad money	8.4	13.2	8.4	13.9	12.4	9.5	9.1
Lending rate (eop, in percent)	16.9	15.9	14.0	14.3	13.2	...	...
Deposit rate (eop, in percent)	11.0	10.4	8.8	8.2	8.4	...	...
Nonfinancial public sector							
Primary balance (percent of GDP)	-7.0	-3.4	0.1	0.3	0.1	0.3	0.5
Overall balance (percent of GDP)	-7.5	-3.9	-0.9	-0.5	-0.8	-0.8	-0.8
Gross debt (percent of GDP)	38.6	39.3	39.0	39.9	40.3	40.8	41.3
Saving and investment							
Gross fixed capital formation (percent of GDP)	22.9	23.0	25.1	23.4	24.0	24.9	25.1
Gross national savings (percent of GDP)	13.4	16.0	20.5	20.7	22.3	21.1	21.2
External sector							
Gross international reserves (millions of dollars)	3,255	3,698	3,992	4,177	5,086	5,172	5,351
Gross international reserves (in months of imports) [3/]	3.8	4.3	4.8	4.7	5.3	5.1	5.1
Change in net international reserves (increase -)	-546	-264	-303	124	-708	-50	-155
Current account balance (percent of GDP)	-9.5	-6.9	-4.7	-2.7	-1.7	-3.8	-3.9
Exports f.o.b.	-6.6	4.0	1.3	-3.5	9.3	2.4	3.8
Imports f.o.b.	-3.7	1.2	0.8	-5.5	7.2	5.7	3.9

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

[1/] 2018 data as of May 14, 2018.

[2/] 2018 data as of April.

[3/] Refers to the following year's imports of non maquila and nonfactor services.

HONDURAS

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION

May 15, 2018

KEY ISSUES

Context. The IMF-supported program (2014-17) succeeded in reducing Honduras' macroeconomic imbalances. The next step is to adopt institutional reforms to entrench macroeconomic stability to put Honduras on a higher potential growth path.

Policy advice. *The consultation focused on priorities to safeguard macroeconomic stability achieved under the program, strengthen policy frameworks, and improve institutions.*

- **Fiscal policy.** In the short run, maintain a prudent fiscal policy to contain vulnerabilities. In the medium term, make robust the past revenue mobilization gains by phasing out tax expenditures and implement structural reforms to keep a firm grip on the wage bill and enhance the quality of public expenditure.

- **Monetary policy.** In the short run, reverse the supportive monetary policy stance to curb inflationary pressures and anchor expectations; market conditions permitting, allow more exchange rate flexibility. In the medium term, adopt a new central bank law to give credibility to the inflation targeting regime.

- **Structural reforms.** Step up anti-corruption efforts, speed up reforms in the electricity sector and adopt broader reforms to improve the business climate.

- **Financial regulation and supervision.** Continue implementing the FSSR recommendations and monitor household debt.

Approved by:
Robert Rennhack (WHD) and Ana Corbacho (SPR)

Discussions took place in Tegucigalpa during April 2-13, 2018. The staff team comprised R. Garcia-Saltos (head), J. Kapsoli, D. Plotnikov (both WHD), M. Coelho (FAD), M. Tovar (CAPTAC-DR), and E. Korczyc (World Bank). J. Puig, Resident Representative, also participated in the meetings. C. Friend and J. Saboin provided editorial and research assistance at headquarters.

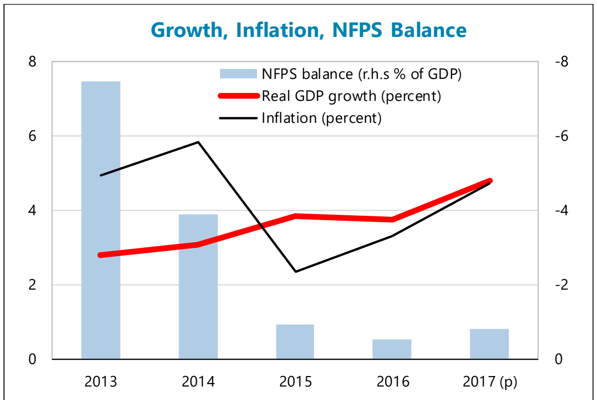
CONTENTS

TABLES

ANNEXES

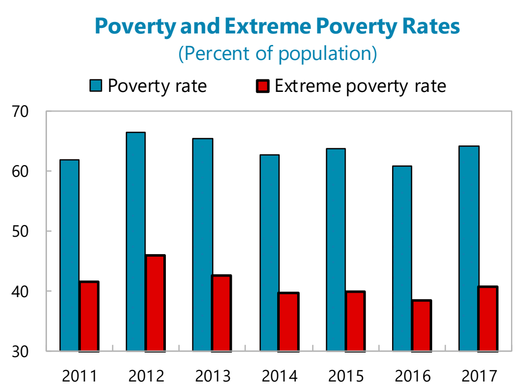
STABLE MACROECONOMIC CONDITIONS BUT STILL WEAK INSTITUTIONS AND HIGH POVERTY

1. Honduras completed successfully a 3-year Fund-supported program with a sustained recovery in economic activity, stable inflation, an improved security situation, and a vast reform agenda. Strong ownership and sustained fiscal discipline, with a reduction in the non-financial public sector (NFPS) deficit by 6¾ percentage points of GDP, were key elements to bring stability and improve confidence, as shown by the steady improvement of international sovereign debt credit ratings. The authorities also met most of their targets for end-2017. These were set to signal a commitment to prudent policies after the program's expiration in December 4, 2017.

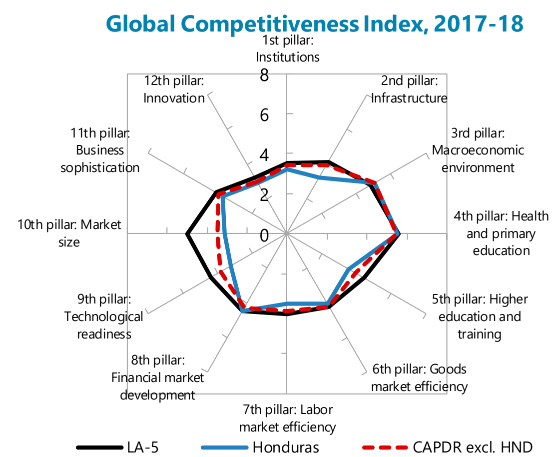


Sources: Honduras authorities and IMF staff estimates.

2. These successes have been clouded by the political events that emerged after the November Presidential elections. The incumbent president emerged as the winner with a narrow margin, and social unrest unveiled after the elections. His party won 61 seats in Congress, short of a majority in a 128-seat chamber. In response to the new political conditions, the president formed a coalition to secure a small congressional majority and called for a national dialogue among all political parties to define the country's policy priorities. For this, he has requested the participation of the U.N. as a facilitator. In sum, the new political reality increased the risk of political polarization which could affect the pace of the reform momentum.



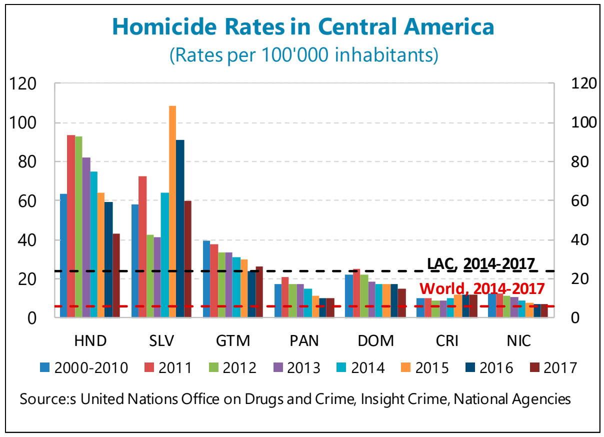
Source: INE.



Sources: World Economic Forum. The index, mostly survey-based, ranks issues on the scale from 1 (worst) to 7 (best).

3. High poverty and weak institutions remain key constraints to growth. Over sixty (forty) percent of the population lives below the poverty (extreme poverty) line, with even larger shares in rural areas. This condition has been nearly constant for more than a decade. Due to the significant level of informality (75 percent), the major share of poverty is structural. While the security situation improved considerably since 2013 (Box 1), the recent unveiling of high-profile corruption cases has exposed the country's significant institutional weaknesses.

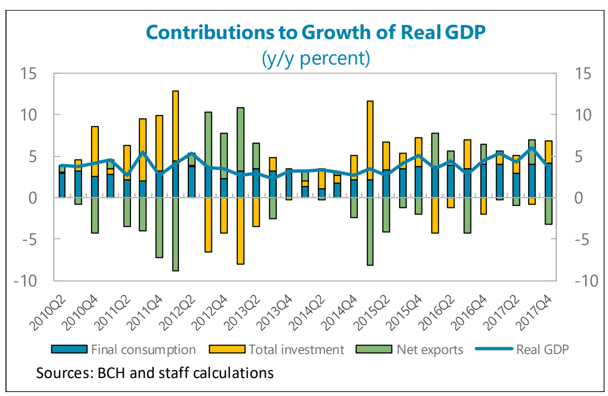
Box 1. The Reduction in Crime Since 2013



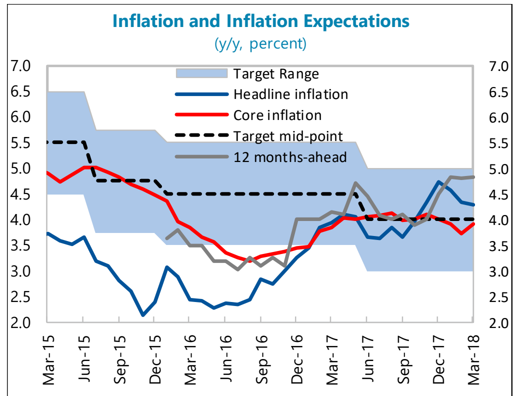
Since 2013 Honduras has achieved an impressive reduction in violence, although the homicide rate remains above the LAC average. To reduce homicides and drug trafficking, Honduras implemented tactical police operations and crime prevention programs to the highest crime areas, as well as improved the quantity and the quality of its police force. The authorities (i) captured and extradited to the U.S. many leaders of criminal organizations; (ii) focused on reducing extorsions, which often lead to murders, (iii) implemented several real-time monitoring initiatives (new 911 centers, security cameras, street lights and panic buttons in public buses); (iv) established a civilian committee to purge corrupt officers; (v) enlisted new police officers; (v) improved equipment, training, raised education requirements and increased salary of police officers. To support these operations, the resources devoted to security increased substantially (since 2012 as a percentage of GDP, the budget of Ministry of Security increased 20 percent, and of the Defense Ministry by more than 60 percent).

RECENT ECONOMIC DEVELOPMENTS

4. After two years of robust expansion, in 2017 the economy accelerated further and vanished the slack. In 2017 real GDP growth reached 4.8 percent, above the estimated 3¾ percent potential growth, resulting in a positive output gap of about ½ percent. Good harvests, a sharp increase in public investment—especially in the second half of the year—and strong growth in private consumption supported the expansion despite the drag imposed by higher oil prices and the effects of the social unrest at the end of the year.

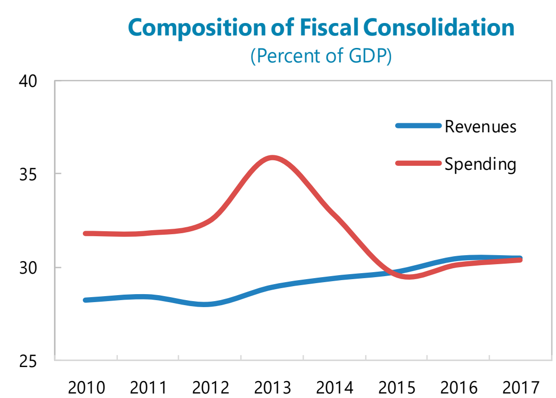


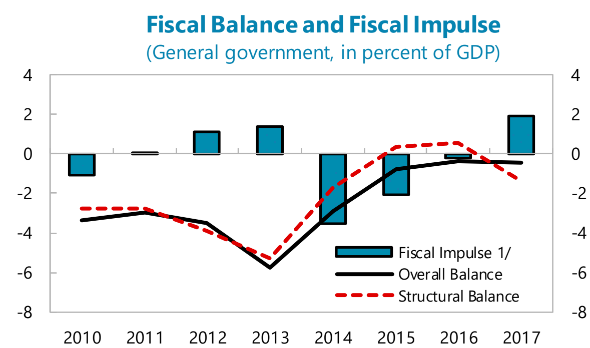
5. **Observed inflation and inflation expectations recently picked up, although both are still within the target range.** In 2017 inflation accelerated to 4¾ percent (from 3¼ percent at end-2016), still within the 4±1 percent tolerance range announced by the central bank. The pickup on headline inflation reflects a faster recovery in domestic demand, rising international oil prices and some supply disruptions in December 2017 (¶2). In 2018Q1 headline inflation has fluctuated above the target range mid-point and inflation expectations continued to rise and reached the upper limit of the target range. The Lempira depreciated mildly by ½ percent on a yearly basis by end-2017 against the U.S. dollar, which helped contain inflation.



Sources: Honduras Central Bank and IMF staff calculations.

6. **Fiscal discipline was maintained during the election cycle.** In 2017, the NFPS posted a deficit of ¾ percent of GDP, below the Fiscal Responsibility Law (FRL) ceiling of 1½ percent of GDP. Most of the stronger performance, however, was transitory as it included a windfall from the tax amnesties introduced during 2016-2017 (estimated at ½ percent of GDP) and restraint on the growth of current expenditures.





1/ Measured as the change in structural balance.

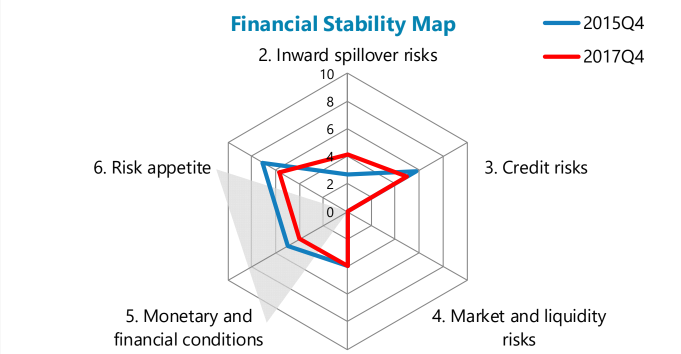
Sources: Honduras authorities and Fund staff calculations.

7. **At the end of 2017, the external position of Honduras was broadly in line with fundamentals and desired policies.** In 2017 the current account (CA) deficit shrank to 1¾ percent of GDP (2¾ percent in 2016). Most of the improvement reflected the unexpected surge in remittances (annual growth of 12 percent, almost double the average of 2010-2016 growth rates) and stronger performance in coffee exports. The CA continued to be primarily financed by FDI inflows. International reserves increased by US$883 million and were boosted by US$700 million external bond issuance. The stock of reserves reached 5.3 months of non-maquila imports of goods and services (4.7 months at end-2016), within the adequacy range of Fund's composite reserve metric. Staff used various approaches to assess the external sector position and have not found a significant deviation from fundamentals. These include quantitative indicators, regression-based

methods to estimate the distance of the current account (CA) balance from its equilibrium value and stability conditions for net foreign assets (Annex I).

8. The U.S. just announced the termination of the Temporary Protection Status (TPS) for Hondurans. To allow for an orderly transition, the termination date will be effective in January 5, 2020. The effects in term of remittances are expected to be modest. About 50,000 legal Honduran migrants, who send remittances of about 1 percent of GDP, are estimated to enjoy TPS status. Some TPS migrants are set to be regularized before the program expires and a small percentage is expected to return in the absence of a significant step-up in enforcement.

9. The banking system remains sound, and the credit gap is closed. Against the backdrop of improved financial conditions and lower risks, balance sheet buffers appear adequate. Nonperforming loans to total loans remain historically low, profitability is high, and the leverage ratio, at 11 percent, is well below crisis threshold rating. Meanwhile, balance sheet risks remain moderate. Specifically, liquidity remains ample, and credit dollarization continued the downward trend since mid-2015 consistent with the ongoing re-monetization. At the same time, credit cycle risk remains low, as private sector credit, currently at about 56½ percent of GDP, has been expanding at a sustainable rate, well below the threshold that defines a credit boom.[1] Private sector balance sheets remain sound, although exchange rate risks still pose risks due to a significant share of unhedged FX borrowers.



Note: Away from center signifies higher risks, easier monetary and financial conditions, or higher risk appetite.

Sources: Country Authorities and IMF staff calculations

10. Private sector credit, especially in foreign currency, has expanded amid a decline in real lending rates and relative stability in the Lempira. The gradual easing of monetary policy in the first half of 2016 resulted in lower bank lending rates and contributed to a steady expansion in total credit growth. In addition, banking spreads have begun to inch lower reflecting improved external conditions and better macroeconomic conditions. These two factors reinforced each other to foster remonetization and a reduction in credit dollarization. This trend has partially been reversed since the second half of 2017 when credit in FX began to pick up amid XR stability. Overall financial conditions remain stable and approximately on the same level as two years ago.

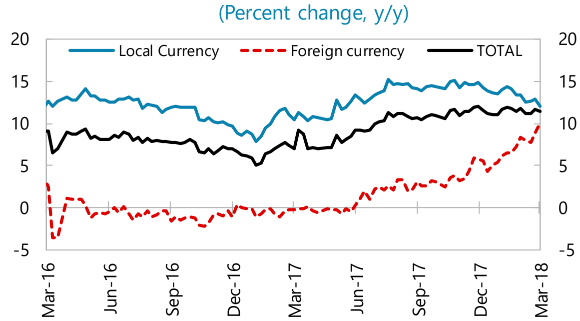
[1] See Dell'Aricca and others (2012) "*Policies for Macrofinancial Stability: How to Deal with Credit Booms*" for a discussion on indicators to identify credit booms.

Financial Soundness Indicator Map

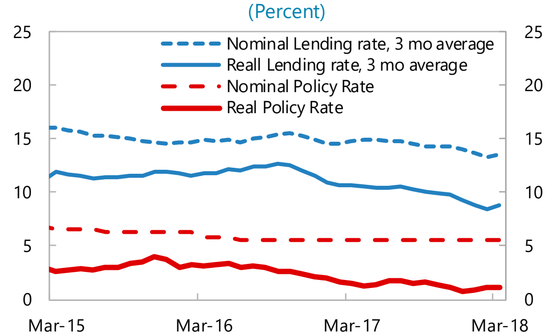
	2015Q2	2015Q3	2015Q4	2016Q1	2016Q2	2016Q3	2016Q4	2017Q1	2017Q2	2017Q3	2017Q4
Overall Financial Sector Rating	M	M	M	M	M	M	M	M	M	M	M
Credit cycle	L	L	L	L	L	L	L	L	L	L	L
Change in credit / GDP ratio (pp, annual)	0.2	0.1	0.0	0.5	0.8	1.2	1.6	1.2	0.9	0.5	0.2
Growth of credit / GDP (%, annual)	0.3	0.2	0.1	0.8	1.6	2.3	2.9	2.2	1.5	0.9	0.3
Credit-to-GDP gap (st. dev)	-1.9	-1.9	-1.8	-1.4	-1.2	-0.9	-0.7	-0.6	-0.5	-0.3	-0.1
Balance Sheet Soundness	M	M	M	M	M	M	M	M	M	M	M
Balance Sheet Structural Risk	M	M	M	M	M	M	M	M	M	M	M
Deposit-to-loan ratio	99.0	97.5	97.3	98.2	98.3	96.9	97.3	101.4	101.3	101.0	99.3
FX liabilities % (of total liabilities)	36.5	36.4	36.1	36.0	35.3	35.2	35.3	31.8	31.3	31.1	31.5
FX loans % (of total loans)	33.6	32.9	32.5	32.9	31.0	30.8	31.4	31.6	30.3	29.7	30.5
Balance Sheet Buffers	L	L	L	L	L	L	L	L	L	L	L
Leverage	L	L	L	L	L	L	L	L	L	L	L
Leverage ratio (%)	10.5	10.6	10.5	10.4	10.4	10.4	10.4	10.9	10.8	10.9	11.1
Profitability	L	L	L	L	L	L	L	L	L	L	L
ROA	2.4	2.6	2.8	2.0	2.3	2.6	2.0	2.0	2.0	1.9	1.9
ROE	23.1	25.4	28.9	18.5	22.6	25.5	21.1	19.2	19.3	18.7	18.4
Asset quality	L	L	L	M	M	L	L	L	L	L	L
NPL ratio	3.4	3.7	3.1	3.7	3.6	3.5	2.9	2.6	2.5	2.5	2.6
NPL ratio change (%, annual)	-10.0	-7.4	-6.6	10.9	8.4	-4.9	-4.4	-30.5	-31.2	-27.9	-12.0

Source: IMF staff calculations
Note: Low (L), High (h), Medium (M)

Private Sector Credit Growth
(Percent change, y/y)



Interest Rates
(Percent)



Sources: BCH and IMF staff calculations.

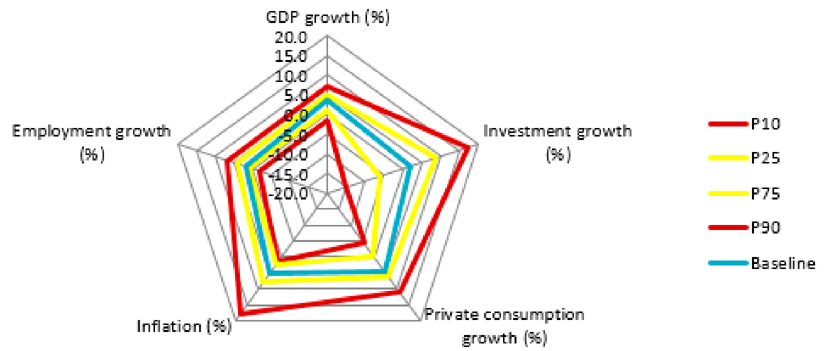
11. **The post-election political turmoil forced the government to concede to long-standing demands from interest groups.** These included: (i) multiannual wage increases (estimated medium-term effect is 0.4 percent of GDP); (ii) a lending program for housing that consists of an interest rate subsidy and partial funding *via* a de facto reduction in reserve requirements (e.g. outright monetary expansion over the next three years equivalent to 10½ percent of end-2017 currency issue); and (iii) a gradual reduction in the minimum corporate tax that was introduced in 2014 (estimated annual cost of about ½ percentage points of GDP).[2]

[2] The fiscal cost in 2018 would be considerable lower (¼ percent of GDP) as income tax clearings (due at end-April) will be paid at the corporate tax system valid under the previous legislation.

POSITIVE OUTLOOK WITH EMERGING DOWNSIDE RISKS

12. The 2018 scenario envisages a moderation in growth and slightly higher inflation.

Distribution of Macro Outcomes



Note: The chart shows variables projections in distributions conditional on credit growth based on historical data of LAC countries.

- **Real growth is projected to slow to about 3¾ percent**. Political uncertainty and worsening external conditions will affect exports and consumer confidence triggering a growth deceleration. Private consumption will continue to be the main contributor to growth. Private investment, mostly in construction, will respond to the announced housing program. Imports growth will be contained as a bulk of intermediate inputs were pre-imported ahead of the November 2017 elections. The financial system is expected to remain liquid, well capitalized and supportive of a sound credit expansion. For the medium term, growth is expected to remain around potential (3¾ percent).

- **Inflation is to stay close to the upper limit of the tolerance band**. On the back of mild excess demand, somewhat expansionary monetary policy stance, higher energy prices reflecting rising fuel prices and electricity tariffs, inflation would remain above 4 percent.

- **The NFPS deficit is projected at 0.8 percent of GDP, same as in 2017.** Tax revenues are projected to fall by ½ percent of GDP reflecting a reduction of presumptive corporate taxation (¶10); the full impact of tax exemptions introduced in 2017, lower customs duties due to the customs union with Guatemala; and the lingering effects of the new tax code that weakened the collection and enforcement powers of the tax authority. The latter include the possibility of an absolutory excuse of criminal charges related to tax fraud. Simultaneously, current spending will be restrained by the FRL expenditure rule and recent policy decisions (see ¶17 and ¶19). The financial situation of the public electricity company ENEE, however, will add to expenditure pressures. In the medium-term, the deficit is expected to hover below the FRL target as the authorities' revised macro-fiscal framework prioritizes the reduction in public debt.

- **The current account deficit is projected to widen to about 4 percent of GDP.** Despite strong growth by trading partners, higher oil prices —as well as a reduction in the growth of remittances— are expected to widen the current account deficit. The slowdown in remittances is explained by the ongoing crackdown on undocumented immigrants and the termination in 2020 of the TPS for Hondurans.

- **The debt sustainability analysis (DSA) suggests a favorable outlook and staff recommends maintaining the external risk rating as moderate** (Annex II).

Medium-Term Scenario

	Act. 2015	2016	Prel. 2017	2018	2019	Projections 2020	2021	2022	2023
					(Annual percent change)				
Output and Inflation									
GDP at constant prices	3.8	3.8	4.8	3.7	3.7	3.7	3.7	3.8	3.8
Consumer prices (eop)	2.4	3.3	4.7	5.0	4.5	4.0	4.0	4.0	4.0
					(In percent of GDP, otherwise indicated)				
Nonfinancial Public Sector									
Net lending (+) / Net borrowing (-)	-0.9	-0.5	-0.8	-0.8	-0.8	-0.8	-0.7	-0.7	-0.7
Primary balance	0.1	0.3	0.1	0.3	0.5	0.7	0.7	0.7	0.5
Gross debt	39.0	40.0	40.7	41.4	42.1	42.7	43.5	43.9	43.6
External sector									
Current account balance	-4.7	-2.7	-1.7	-3.9	-4.0	-4.1	-4.0	-3.9	-3.9
GIR (in months of non maquila imports)	4.8	4.7	5.2	5.2	5.1	5.1	5.1	5.1	5.1

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

13. Risks to the outlook are tilted to the downside (Annex III).

- **External risks.** Tighter-than-expected global financial conditions (e.g., due to higher-than-expected inflation in the U.S.) could discourage risk appetite for emerging markets. Tighter immigration policies in the U.S. may reduce remittances, and FDI flows to Honduras, which could produce negative impacts on consumption and investment. Under the current crawling-peg regime, this reduction in external flows could exert some pressure on the foreign exchange market triggering a reduction in reserves and/or an abrupt depreciation of the Lempira, which given the extent of credit dollarization could also produce adverse balance sheet effects. Climate change recently emerged as a medium-term risk.

- **Domestic risks.** An unresolved and prolonged political polarization may worsen business and consumer confidence and thus growth. Similarly, further institutional weakening caused, for example, by a perceived lack of commitment to quelling corruption or reform fatigue could negatively impact investor sentiment discouraging domestic and external investment.

Authorities' Views

14. The authorities broadly concurred with the risks highlighted by staff but were more positive about the outlook. The authorities shared staff's assessment of downside risks, emphasizing the country's external vulnerability to changes in U.S. immigration policies and tighter external financial conditions. However, they downplayed the adverse effect of political uncertainty on the growth of private investment projected by the staff. The authorities foresaw real GDP growth of about 4 percent, which results from the expected expansion of construction (housing) and tourism sectors. On inflation, the authorities saw merit in enhancing their credibility by adopting a more cautious stance on monetary policy and more gradual implementation of the new housing credit policy.

POLICY DISCUSSIONS

15. The consultation focused on the policy mix appropriate for the current cyclical conditions and on bolstering sustained and inclusive growth. Stagnant productivity is at the core of relatively low growth in Honduras. This is a byproduct of high crime, low human capital, high cost of capital, and a weak business environment. To ameliorate these obstacles and foster employment creation, especially for women, the mission discussed how to: (i) reduce fiscal vulnerabilities, (ii) foster credibility of monetary policy institutions, (iii) safeguard financial sector resilience, and (iv) improve the efficiency of institutions.

A. Near-Term Policy Mix to Safeguard Macroeconomic Stability

16. Mild overheating conditions and risks affecting confidence call for a cautious and more coordinated policy response to signal the authorities' commitment to macroeconomic stability. While the burden to control inflation rests with monetary policy, limiting vulnerabilities associated with rising public debt will require maintaining a prudent fiscal stance.

17. Maintain a prudent fiscal stance. If fully executed, the 2018 budget envisaged a fiscal impulse —about ½ percent of GDP relative to 2017, which could add to the incipient overheating conditions. Staff viewed the budget's pace of execution of public investment as overly optimistic, and proposed a reduction in the deficit by ½ percentage point of GDP. The financial situation of ENEE remains the primary fiscal challenge as the finances of the company has been deteriorating sharply despite the central government support in 2017. Staff recommended to strengthen revenue mobilization efforts by making a dent in the inequitable and unsustainable level of tax exemptions, and ensure adequate funding for social programs.

18. Gradually reverse the supportive monetary policy stance. The staff recommended reversing the currently supportive monetary stance in BCH's policy rate, which has been at 5½ percent since mid-2016, to rein in emerging inflation pressures and anchor expectations near the midpoint of the recently reduced target band (¶5). The reversal should also require offsetting the monetary expansion implicit in the new lending program for housing. Lower import growth and net capital outflows could result in the accumulation of international reserves by US$50 million. A more cautious policy stance would slow real growth only modestly in 2018, as multipliers are likely small given the state of the cycle, with growth then bouncing back at about 4 percent.

Neutral Interest Rate for Honduras

		Expected Inflation Dec-2018	4.80
		Actual Monetary Policy Rate	5.50

Method 1/	Neutral Real Interest Rate (NRIR)	Neutral Nominal Interest Rate (NNIR)	Nominal Monetary Policy GAP (bps) 2/
Uncovered Interest Parity	0.6	5.4	10
Expected-Inflation Augmented Taylor Rule	1.3	6.1	-60
General Equilibrium Model	1.9	6.7	-120
Average	1.3	6.1	-57

Sources: Country Authorities and IMF staff estimates.
1/ All units expressed as percent points unless otherwise stated.
2/ (bps): Basis points.

Authorities' Views

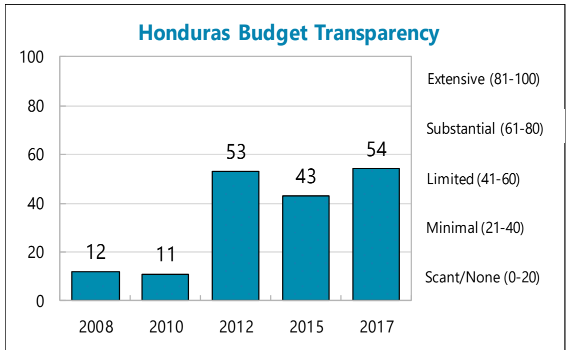
19. The authorities broadly agreed with staff on the importance of taking measures to maintain macroeconomic stability as a critical condition for sustained growth. They shared the staff's assessment that a tighter fiscal position relative to the FRL's ceiling will be essential in this regard. They committed to curbing spending as needed to maintain the NFPS deficit unchanged from last year. They highlighted that the recent decree to revise the minimum income tax reform also authorized curtailing expenditures to guarantee the neutrality of the measure. The authorities expressed their commitment to carefully monitor liquidity and inflation developments, standing ready to take policy actions if needed to maintain inflation within the central bank's tolerance band.

B. Resolving Long-Standing Fiscal Issues

20. Rationalize tax expenditures. At close to 7 percent of GDP, tax expenditures in Honduras are among the highest in the region. The bulk of these exemptions are concentrated in special corporate income tax regimes, and in untargeted goods and services, otherwise subject to VAT. In addition to direct tax revenue losses, these exemptions increase tax avoidance and create inequities. With no space for higher tax rates, staff recommended phasing out tax exemptions yielding at least 1½ percent of GDP over the next three years. In staff's view, these additional revenues should be used to expand poverty-reducing expenditure, as stated in the social protection framework law. To increase fiscal transparency, the information of beneficiaries of tax expenditures (where applicable) and the associated estimates of revenue forgone should be publicly available (Box 2). In line with the mandate from the FRL, the cost-benefit analysis of any new tax exemption should be published.

Box 2. Enhancing Transparency and Public Information Access

Honduras has improved budget transparency since 2008. The survey-based Open Budget Index, which measures the amount and timeliness of publicly available standard budget information, has improved from 12 in 2008 to 54 in 2017. Also, the 2016 PEFA assessment acknowledges the progress in increasing the public access to fiscal information through the Public Employees Registry System (SIREP) and the Integrated Municipal Administration System (SAMI).



Sources: International Budget Partnership, www.internationalbudget.org

In 2018 the authorities plan to enhance transparency and public information further. These include:

- ***Enhanced electronic platform with information on procurement contracts beyond the signing stage***. Currently only limited information is available on public procurement processes, which constitute 28 percent of total expenditures. The Government plans to launch a new transparency module based on the Open Contracting Data Standard for public procurement information system and increase information about the suppliers through the Registry of the Users of Public Funds. Additionally, the link with the Government's financial information system SIAFI will improve payment controls of the public contracts;
- ***Establishment of a PPP disclosure portal and the public investment portal with detailed investment map and relevant financial information***. Both initiatives will facilitate citizen monitoring of investment projects and improve the accountability of public expenditure;
- ***Open Data Initiative*** to provide enhanced and user-friendly access to public data. The data portal would allow public access to variety of datasets, from budget execution information to socio-economic indicators, information about social service delivery and key public programs, thereby providing a platform to introduce elements of performance-informed budgeting.

Despite the progress, sizable challenges remain. First, significant public resources are channeled through the extra-budgetary trust funds, which are outside the expenditure control chain. Second, the current legislation (Decree 418-2013, known as the "Secrecy Law") includes a broad definition of national security and defense, which can potentially be misused to restrict access to information. Third, the disclosed information is often incomplete, or is unavailable in a timely manner, or in not user-friendly formats, which limits its usefulness. The planned Fiscal Transparency Evaluation will assess country's compliance with the basic requirements for fiscal risk disclosure under the new IMF fiscal transparency code.

21. Rightsize the wage bill. During 2014-2017 the authorities achieved a remarkable retrenchment of the wage bill (about 3 points of GDP) by relying mainly on stopgap measures.[3] Containing wage growth in a sustainable manner remains crucial to fund the expansion of social spending. The reform needs to: (i) streamline the compensation schemes ("*estatutos*"); (ii) create a centralized institution overseeing civil service reform; and, (iii) ensure a competitive compensation scheme compared with the private sector. Staff estimates that around ½ percent of GDP could be saved over the medium term if this reform is implemented. The authorities are currently developing a general wage policy for civil servants, targeted for approval in the first half of 2019.

[3] Some high-quality measures were also implemented. These included: the elimination of redundancies in public companies (which were largely overstaffed); and the adoption of a centralized payroll system for the central government.

22. Ensure financial sustainability of ENEE. While important progress has been achieved on strengthening ENEE's financial position during the previous administration, some structural issues continue dragging the finances of the company. Among them:

- *Electricity losses*. At end-2017 they stood at 31 percent, still too high to ensure a financial soundness for ENEE.
- *Large unpaid bills from public sector entities*. Due to poor budgeting practices, public entities maintain large unpaid electricity bills (about ½ percent of GDP).
- *Existing contracts of energy purchases*. These agreements restrict ENEE's operational autonomy to minimize costs in purchases of electricity.
- *Ancillary services*. ENEE's critical services to stabilize the power grid are being provided at zero cost.

ENEE needs a comprehensive plan to tackle these issues alongside immediate actions to restore its financial position including adjusting electricity tariffs and faster reduction in non-technical electricity losses.

23. Continue to strengthen the risk management framework and build buffers. The authorities have already made impressive progress on accounting of contingent liabilities and risks. They quantified implicit guarantees from the central government to credit obligations of other NFPS entities, PPP contracts, and lawsuits against the state. In 2018 they plan to further quantify risks associated with debt accumulation by municipalities, natural disasters, and public enterprises (such as ENEE). The authorities expect the first report of contingent liabilities to accompany the 2019 budget bundle.

24. Continue reforms on public financial management (PFM). Sustained PFM reforms are critical to entrench accountability and support enforcement of the FRL. The mission recommended to:

- *Conduct a Fiscal Transparency Evaluation (FTE) led by FAD to identify areas that remain below the benchmarks of the fiscal transparency code.*
- *Phase out extra-budgetary trust funds by incorporating them into the budget. In exceptional cases, where this is not possible in the short-term, implement at a minimum independent ex-post expenditure audits.*
- *Incorporate performance-based indicators into the medium-term fiscal framework.*
- *Enhance budget transparency standards. (see Box 2)*

25. Accelerate the implementation of the operational and strategic plan for the revenue administration. The collection and enforcement powers of the tax authority should be strengthened, including by re-instating the criminality of tax fraud without enabling absolutory excuse in cases of payment of dues before any legal action is taken. Moreover, several laudable efforts have been pursued since the beginning of the year by SAR, including over the expediency of the tax debt liquidation process and the analysis of mandatory purchases declarations for large taxpayers. However, SAR, SEFIN and the central bank should improve information exchange for policy evaluation among them. Other administrative measures previously recommended by FAD technical assistance remain relevant (Box 3).

Box 3. Main Recommendations on Tax Administration

Tax Registry

- Update of the taxpayer registry for the ten-thousand most important taxpayers.
- Redesign the taxpayers single account.
- Strengthen controls over non-filers.
- Increase oversight over declared tax liabilities.
- Reduce the amount of non-posted payments.
- Ensure 100 percent electronic filing, payment and reporting through a suitable IT platform covering Customs Administration, Tax Administration, and the Ministry of Finance.

Risk Management

- Establish a Compliance Management Committee at strategic and operational levels to improve governance and accountability.
- Improve access and exploitation of information for tax purposes, such as a monthly sales report,
- Redesign the processes of identification, evaluation, and prioritization of risks.
- Redesign the audit process for large taxpayers to reduce firms' costs and increase tax compliance.

26. Improve the coordination between tax and customs administration. The customs authority (COPRISAO) has achieved tangible improvements in the time taken for customs clearance, as well as in revenue collected through customs. It has also increased the number of declarations for goods eligible to go through the more expedient green channel. The transition to a fully independent and functioning customs authority is expected by August 2018.

27. Standardize the domestic public debt primary market. Over the last two years the authorities have made significant progress in standardizing the issuance of domestic government bonds, including by having a periodic auction calendar, and incentivizing private buy-side appetite at the long tail of the yield curve. This process is intended to support the eventual development of a more liquid secondary market for Lempiras-denominated bonds.

Authorities' Views

28. The authorities concurred with the importance of reducing tax expenditures and expressed the intention to strengthen the analysis of their effectiveness to achieve their stated goals as a preceding step for their rationalization. They also agreed on the need to deepen their efforts to increase the transparency of public spending, as well as to improve public wage policies to continue rightsizing the wage bill. The authorities indicated their intention to assess the scope for comprehensive reforms in the electricity sector to resolve the persistent financial disequilibrium of ENEE. This reform could consider options to charge for ancillary services to generators and allow purchases of electricity at minimum available cost. The authorities are committed to continue enhancing tax and customs revenue administration, with technical assistance from the Fund, to support their revenue mobilization efforts.

C. Providing a Robust Anchor for Inflation Targeting

29. Reforming the central bank law is a crucial step for a credible inflation targeting regime (IT). A stronger institutional foundation for IT will help lower real interest rates, anchor inflation expectations, and provide greater predictability of policies. Consistent with previous staff recommendations, the law should include the following principles: (i) a clear mandate to control inflation; (ii) greater institutional, financial and operational autonomy; (iii) solid institutional governance with a transparent appointment of the central bank board of directors and a clear separation of between daily management, policy setting and oversight responsibilities, and (iv) robust accountability mechanisms, including the adoption of the International Financial Reporting Standards (IFRS).

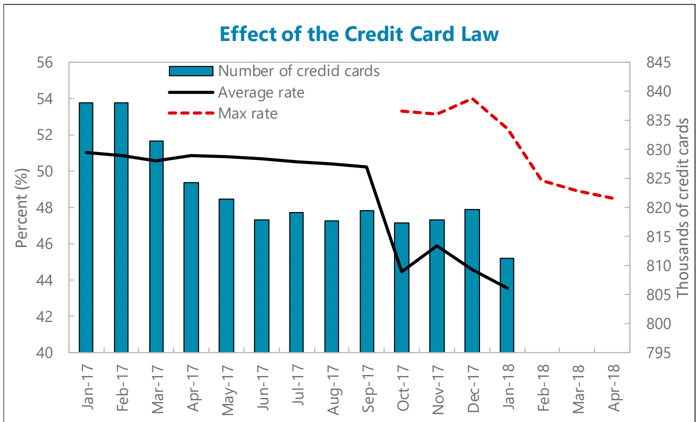
30. Accelerating the development of money and FX market infrastructure. Several measures have already been implemented such as: introducing fully collateralized securities in the interbank market, reducing the surrender requirements for FX operations by 20 percent, and strengthening the technical capacity of central bank's staff. Staff recommended to accelerate the pace of the reduction in FX surrender requirements to create a more vibrant FX market and increase exchange rate flexibility. The latter should also support de-dollarization. Other steps going forward include development of the secondary securities market, supported by the adoption of a new securities market law, and adopting a more transparent and forward-looking communication strategy by the central bank.

Authorities' Views

31. The authorities expressed their continuing commitment to monetary policy modernization and requested a set of follow up TA to help them with the transition process.

D. Ensuring Financial Stability

32. Continue implementing the recommendations of the recent FSSR. The authorities have completed several of the FSSR's recommendations, including production of a new supervisory manual with methodologies for risk-based supervision (RBS), improved training programs for inspectors, new AML/CFT rules, and additional information sharing agreements with other regional supervisors to enhance monitoring of financial conglomerates (Annex IV). Against this background the mission emphasized the need to enhance the monitoring of household debt and mitigate the risks associated with the large concentration of personal loans in public pension funds' portfolio.[4] The credit card law enacted in 2017 seems to have reduced the average rate with some moderate reduction in the number of cards issued.



Sources: Central Bank of Honduras and National Comission of Banks and Securities

33. Stress tests on the banking sector, conducted by staff, show the sector is broadly resilient to most standardized shocks. The tests highlight the banking sector resistance in managing interest rate, FX, and liquidity shocks individually with capital adequacy falling below the regulatory minimum only in the combined shock scenario (Box 4). The mission indicated that an abrupt increase in NPLs could put capital adequacy ratios close to the statutory minimum and recommended monitoring closely developments in NPLs, which have been at historic lows. Increasing credit from commercial companies is a potential risk that needs to be assessed.

34. The expansion of lending programs by the public development bank BANHPROVI and pension funds should be gradual. Staff stated that in the future the central bank should avoid direct financing of development projects, which is the primary objective of the state-own bank BANHPROVI. This bank should proceed with caution with the first-tier lending to projects not covered by traditional banks given its higher risk. As for the pension funds, hasty expansion of consumer lending without appropriate provisions and loan underwriting standards could add to the fiscal risks.

Authorities' Views

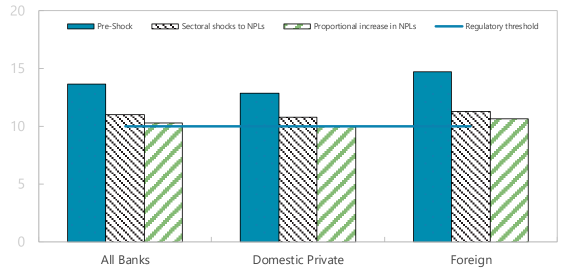
35. The authorities broadly agreed with staff's assessment of vulnerabilities and risks. The authorities did not see the rising household debt as a macro-financial risk but as a problem limited to specific groups (e.g., teachers and low-wage public sector workers). On pension funds, the authorities see the provision of consumer loans to affiliates as the consequence of minimum profit requirements and limited investment opportunities. In their view, the Honduran demographic composition should alleviate a potential maturity mismatch. On BANHPROVI, the authorities committed to prevent any further expansion of the central bank financing and underscored that direct financing from the central bank is within its 2008 legal mandate. They viewed first-tier lending

[4] Prudential regulations limit to 35 percent the share of consumer loans, but funds can increase this share by 5 percent if the NPL rate for personal loans remains under 3 percent. As these loans are full-recourse, the limit is 40 percent.

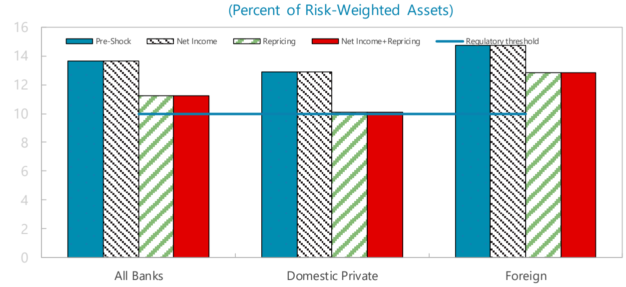
to SMEs and agriculture important to support as these sectors are not attractive to private banks and are critical to foster employment and growth.

Box 4. Stress Test Results

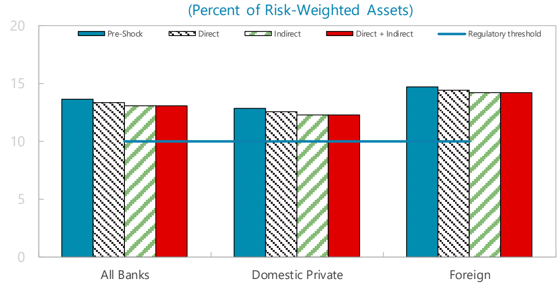
Credit Risk: Capital Adequacy Ratio
(Percent of Risk-Weighted Assets)



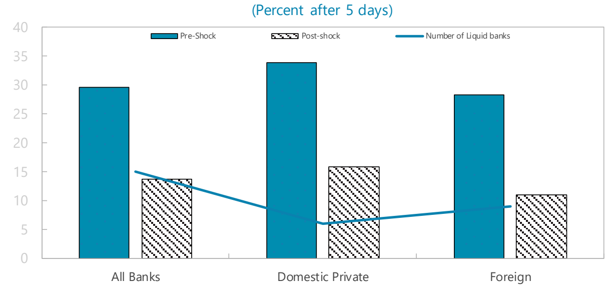
Interest Risk: Capital Adequacy Ratio
(Percent of Risk-Weighted Assets)



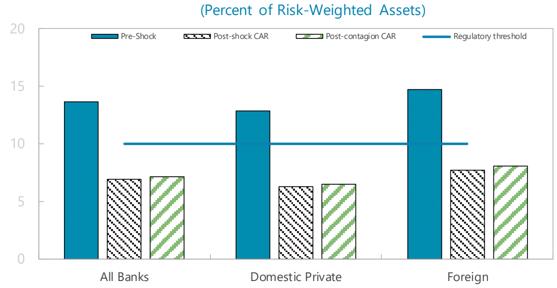
FX Risk:Capital Adequacy Ratio
(Percent of Risk-Weighted Assets)



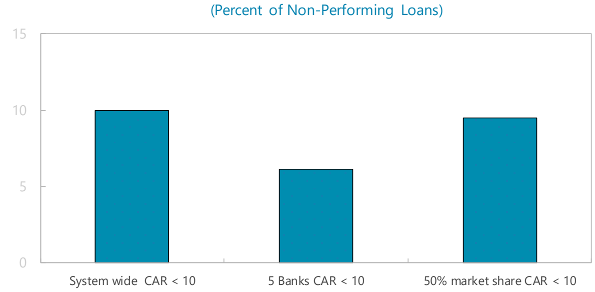
Liquidity Risk: Liquid Assets/Total Assets
(Percent after 5 days)



Combined Shock: Capital Adequacy Ratio
(Percent of Risk-Weighted Assets)



Reverse Stress Test: NPL Increase for Simulated Scenarios
(Percent of Non-Performing Loans)



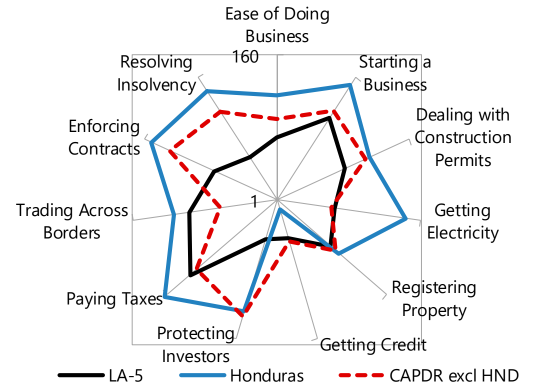
Sources: Country Authorities and IMF staff calculations.

E. Removing Structural Impediments to Bolster Medium-Term Growth

36. Sustained anti-corruption efforts are crucial to enhance the rule of law. A recent setback in anti-corruption efforts highlights the deep-rooted nature of corruption. Specifically, last January, Congress approved a law that gives investigative powers to the court of accounts and potentially prevents the criminal prosecution of embezzlement cases. The mission acknowledged advances made in AML/CFT legislation in line with GAFILAT recommendations and collaboration with the OAS special anti-corruption mission—including the creation of a special anti-corruption unit in the public prosecutor's office and prosecution of some high-profile cases. The mission recommended continued progress on implementing GAFILAT recommendations. However, public prosecutors prefer to use civil asset forfeiture, which results in a low percentage of criminal prosecution, and fuels perceptions of corruption and judicial uncertainty. Prosecutors should use all legal tools at their disposal. The mission also suggested to enhance the current asset declaration system (including mechanisms for verification and public access) of public officials by including assets legally owned and assets which are beneficially owned.

37. Making product and labor markets more competitive. The World Bank's Doing Business Indicators shows Honduras could improve in contract enforcement, trade facilitation, and protecting minority investors. In addition, speeding-up business licenses and easing the procurement process are key to reduce red-tape. The authorities have already implemented many simplification and automatization measures in the customs process, handling VAT exemptions for the agricultural sector. In the medium term the authorities plan to fully implement the use of the electronic signature, consolidate paperwork procedures within and among different public entities and publish this information online. The mission underscored the need for an education plan consistent with the employment objectives in the country's development plan.

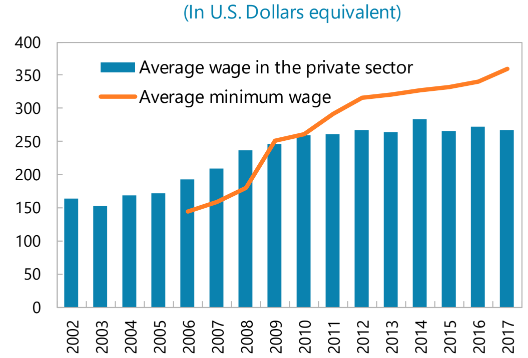
Doing Business Ranking, 2018



Source: Doing Business Report, 2018.

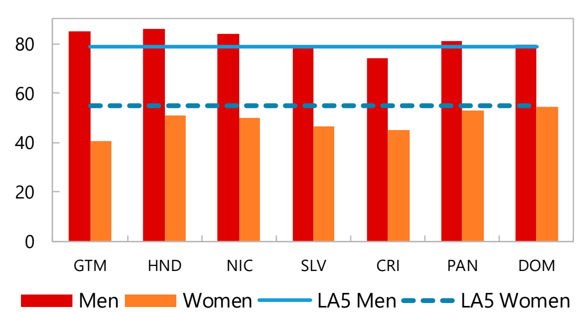
38. Strengthen labor market institutions. The large and widening wedge between the minimum and the average wage observed in Honduras since 2010 shows the non-binding nature of the minimum wage, which likely reflects the large costs of labor formalization. In this regard, avoiding further expansion of the labor informality requires a reform of the framework used in the setting of minimum wages simplifying and making it consistent with current labor market conditions. Also, public interventions, particularly in health and education are essential to increase labor productivity over the medium term, reduce informality, and narrow the gender gap in labor force participation.

Monthly Wage in the Private Sector
(In U.S. Dollars equivalent)



Sources: Country Authorities and IMF staff calculations.

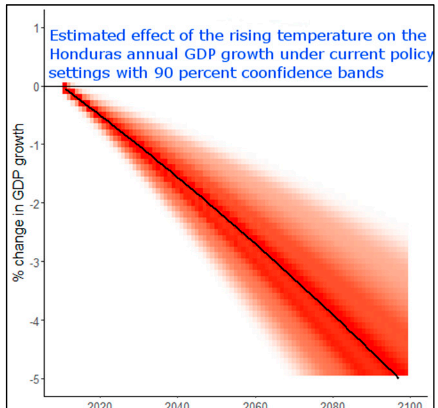
CAPDR Labor Force Participation Rates
(Percent of 15+ population, 2016)



Source: World Bank Development Indicators

39. Improving social outcomes. Social spending primarily comprises social benefits such as conditional cash transfers (CCT) and other cash/in-kind transfers. Social spending has been increasing gradually from ½ percent of GDP in 2009 to close to 2 percent of GDP in 2017.[5] Even though the coverage gap remains high (the number of families living under extreme poverty is around 800,000), the authorities presented solid evidence of effectiveness of their CCTs program (*bono Vida Mejor*). They have documented a structural reduction in child malnutrition which is widely accepted as the main mechanism to break the intergenerational transmission of poverty. [6]

40. Honduras requires a comprehensive set of structural reforms to increase resilience to climate change. Except the direct cost of more frequent natural disasters, Honduras is susceptible to the long-term increase in global temperature associated with the global warming which would decrease agricultural yield, labor productivity of outside economic activities and increase costs of inside activities. Staff estimates that by 2100 in the absence of a structural policy change, the increase in global temperature could eliminate economic growth.[7] To reduce the vulnerability in the agricultural sector and mitigate this risk, structural reforms to promote the production of goods higher in the value chain will be required. On the fiscal front, existing initiatives to quantify fiscal contingencies stemming from climate change are welcome.



Source: Burke et al (2015)

Authorities' Views

41. The authorities are working on several measures to reduce red tape and increase the ease of doing business as part of their objective to boost employment creation and reduce poverty. The newly created National Economic Council will play an essential role in identifying needed reforms and ensuring adequate coordination among government agencies to implement these reforms efficiently.

STATISTICS

42. Honduras urgently needs to update both the base year and methodology of National Accounts (NA) and the CPI to maintain their relevance and accuracy. These projects are also critical elements to ensure a smooth transition to an inflation targeting regime. The current

[5] Social spending was reduced to 1¾ percent of GDP in 2017 from 2¼ percent of GDP in 2016 due to the persistent under execution of trust funds.

[6] Note also that the prevalence of anemia in children below 5 years, measured by the World Health Organization, has reduced from 33¼ percent in 2008 to 31½ percent in 2016.

[7] See Burke, Hsiang and Miguel (2015) "Global Non-linear effect of temperature on Economic Production", Nature, doi:10.1038/nature15725 for the description of the methodology.

reference year for NA and CPI is based on the 1998-99 survey and, therefore, significantly outdated. The authorities agreed to start a new household survey in June 2019 to publish the new CPI in the beginning of 2021. As a second best, the authorities plan to first update the NA compilation methodology first to publish new GDP series in the beginning of 2021 and only later incorporate the new household survey to avoid further delays.

STAFF APPRAISAL

43. The economy continues to expand in 2018, and the outlook for the medium term is broadly positive. The outlook is heavily influenced by the successful reduction in macroeconomic imbalances achieved during 2014-17, which unraveled a virtuous cycle with sustained expansion in the GDP per-capita, greater coverage of the social safety net and stronger foundations for fiscal sustainability. The external position of Honduras was broadly in line with fundamentals and desirable policy settings.

44. In the near-term, however, downside risks prevail. The high and unexpected GDP growth of 2017, translated into mild overheating conditions this year. In this regard, staff welcomes the authorities' decision to adopt a more prudent fiscal stance and unwind, if necessary, the supportive monetary policy stance to rein in potential inflationary bouts. The proposed fiscal tightening is especially relevant given the recent revenue-weakening measures, and the need to signal the authorities' commitment to maintain macroeconomic stability when faced with several risks, such as: worsening in terms of trade, faster tightening in global financial conditions, higher uncertainty about the U.S. immigration policy and the difficult political situation.

45. Beyond the near-term, policy actions are required resolve long-standing fiscal issues. These include the rationalization of untargeted tax expenditures; rightsizing and streamlining the public-sector wage bill; restoring once and for all ENEE's financials; enhancing fiscal transparency and improving the efficiency of social spending.

46. The central bank has made important progress to modernize monetary policy, and the process should continue. For credible inflation targeting regime, enacting a central bank law with a clear mandate to control inflation and robust institutional accountability mechanisms, including the adoption of IFRS, is a priority. Giving the emergence of external risks and the need to generate more cushions against external shocks, staff recommends accelerating the pace of the reduction in FX surrender requirements to create a more vibrant FX market and increase exchange rate flexibility.

47. The implementation of the FSSR recommendations to contain financial risks is welcome, but more efforts may be needed. While the banking sector remains resilient to standardized shocks, several stability concerns are emerging that require monitoring. These include rising household debt, expansion of consumer lending by the public pension funds and commercial companies as well as growth in public bank operations, including first-tier banking. Over the next years, the implementation of the Basel III standard would also require further strengthening capacity development in the Banks' superintendence and better coordination with the central bank.

48. Structural reforms are required to bolster inclusive growth and improve the country's competitive position. The reform priorities are: enhancing the rule of law by continuing the fight against corruption, resolving once and for all ENEE's financials, improve social and education outcomes and enabling private sector entrepreneurship with a policy to ease business. The announced creation of the National Economic Council is a welcome step to coordinate the priorities and sequence of the structural reform agenda.

49. Honduras urgently needs to update both the base year and methodology of National Accounts (NA) and the CPI to maintain their relevance and accuracy. Updating GDP and price statistics and conducting a household survey will improve authorities' grasp of the economy and foster credibility of the inflation targeting regime.

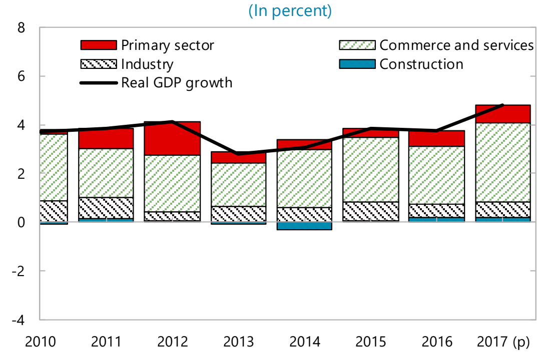
50. Staff supports the authorities' request for temporary approval of two multiple currency practices subject to Fund jurisdiction under Article VIII, Section 3. The MCPs arises from the operation of the foreign exchange auction (see Information Annex), and are maintained for non-balance of payments reasons. The MCPs do not materially impede the member's balance of payments adjustment, harm the interests of other members, or discriminate among members; they are temporary; and the authorities are unable to replace it at present. Staff note that the authorities' ongoing FX liberalization should ultimately eliminate these measures. Staff therefore recommends Executive Board approval for their retention for one year or the conclusion of the next Article IV consultation, whichever is earlier.

51. It is proposed that the next Article IV consultation with Honduras takes place on the 12-month consultation cycle.

Figure 1. Honduras: Real Sector Developments

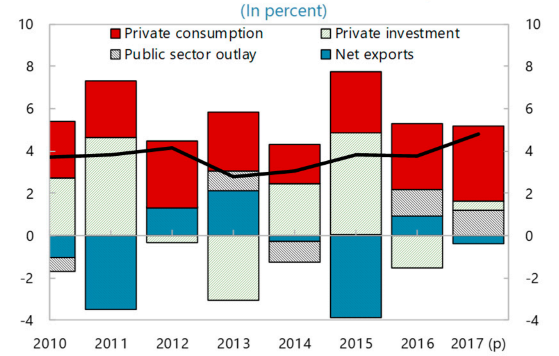
The services sector continues to lead the recovery.

Contributions to Growth by Sector
(In percent)



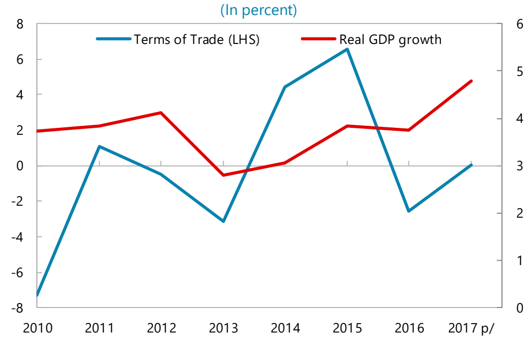
Private consumption benefited from the increase in remittances.

Contributions to Growth, Demand Components
(In percent)



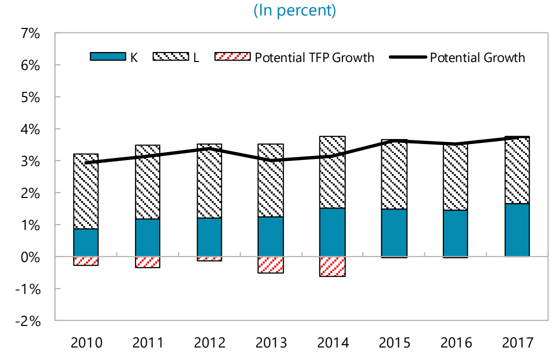
In 2017 ToT were stable.

Terms of Trade and Growth
(In percent)



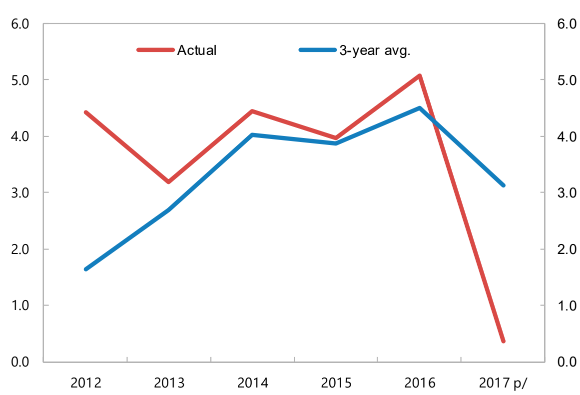
Productivity remained stagnant as contributor to potential growth.

Contributions to Potential Growth, Production Function
(In percent)



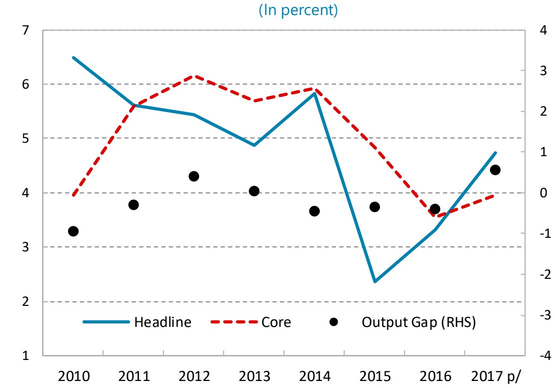
Stable Lempira helped contain inflationary pressures…

Exchange Rate Depreciation



…while vanishing slack and higher oil prices added to inflationary pressures.

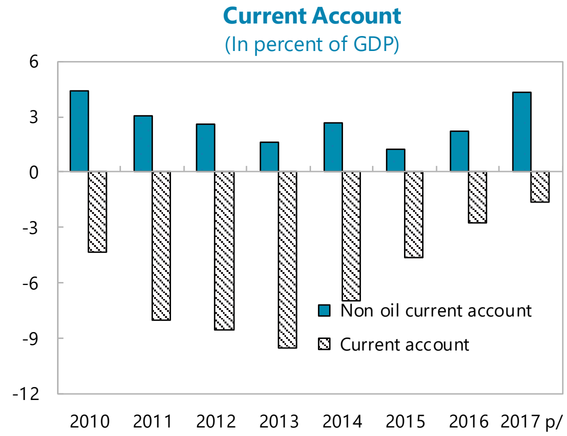
Output Gap and Inflation Measures
(In percent)



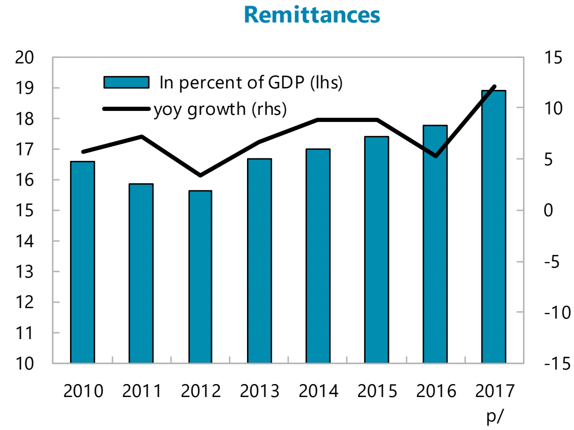
Sources: Central Bank of Honduras and Fund staff estimates and projections.

Figure 2. Honduras: External Sector Developments

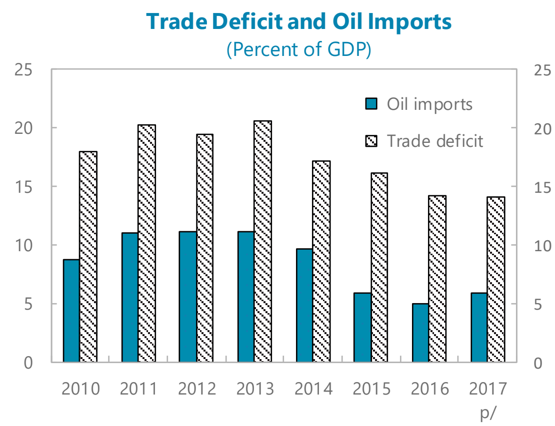
The current account deficit improved significantly in 2017…



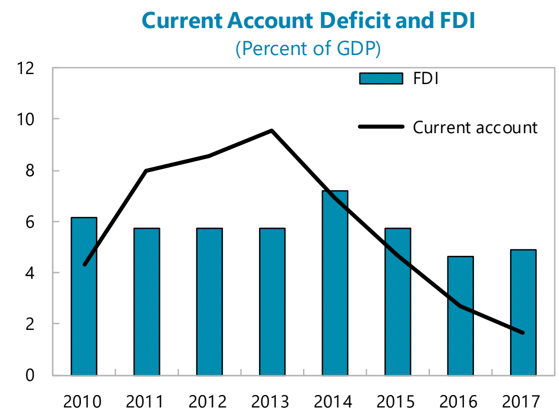
…due to a surge in remittances from the U. S.



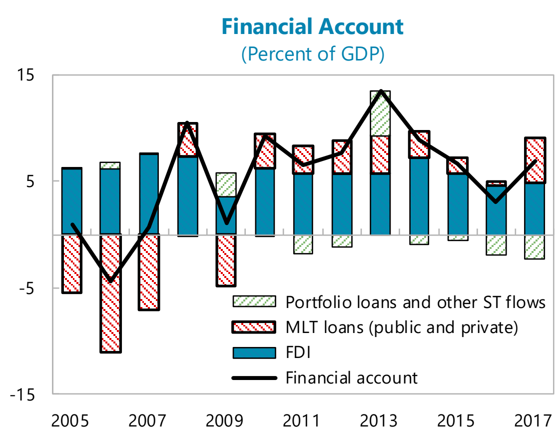
Trade balance remained broadly constant as exports gains were offset by higher oil imports.



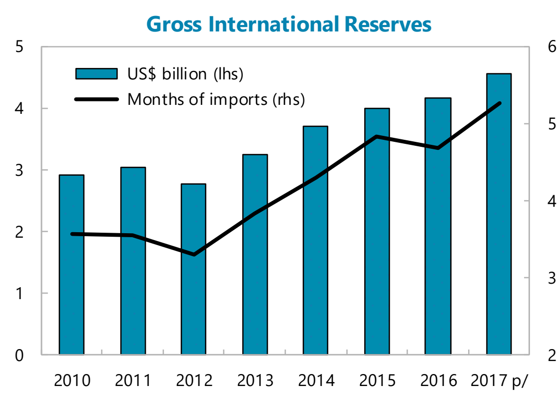
Current account continues to be more than financed by stable FDI inflows.



Public external bond placement in 2017…



…further contributed to the boost in reserves and their coverage has improved significantly.

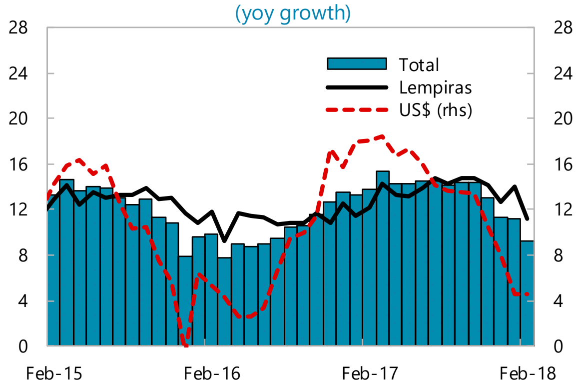


Sources: Central Bank of Honduras and Fund staff estimates and projections.

Figure 3. Honduras: Financial Sector Developments

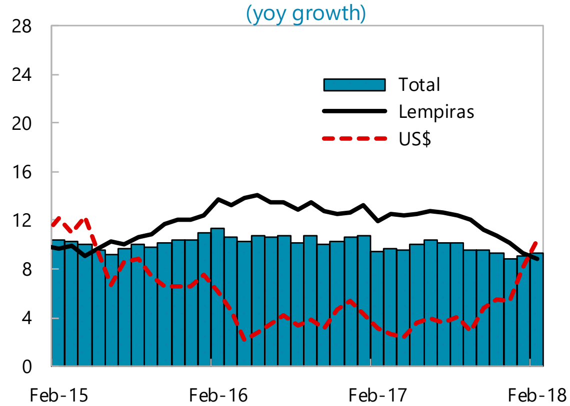
Healthy growth in deposits…

Bank Deposits
(yoy growth)



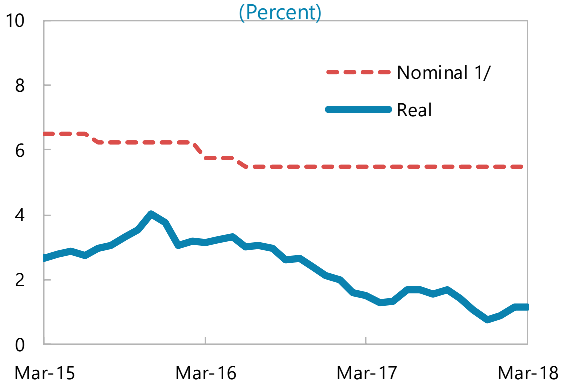
…continues to provide stable financing to the private sector.

Credit to the Private Sector
(yoy growth)



The policy rate has been constant since June 2016 when the central bank reduced it by 25 basis points…

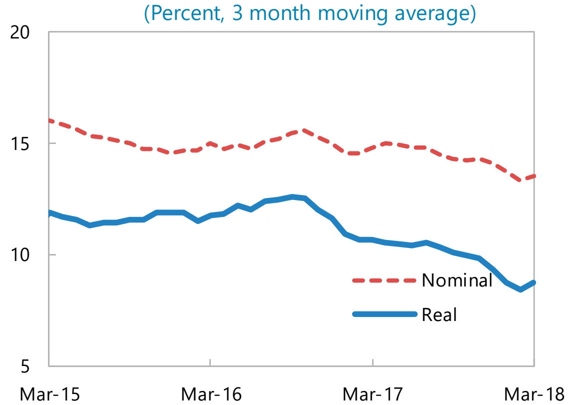
Policy Rate
(Percent)



1/ In June 2016, the Central Bank lowered its policy rate to 5.5 from 5.75 percent .

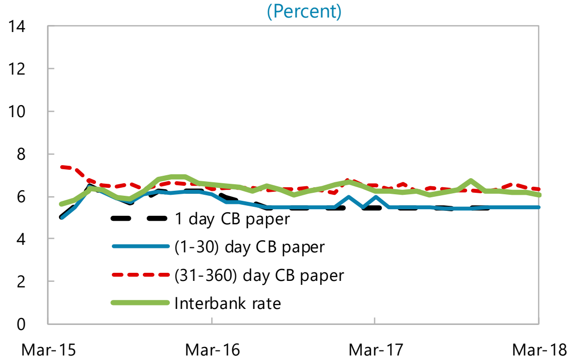
Nominal lending rates continue to inch lower.

Lending Rates
(Percent, 3 month moving average)



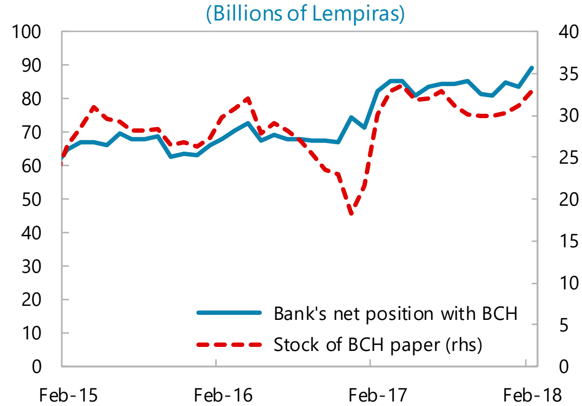
Yields on central bank paper have been stable…

Yield on Central Bank Paper
(Percent)



…as the central bank continued to absorb excess liquidity.

Banks' Net Position with BCH
(Billions of Lempiras)

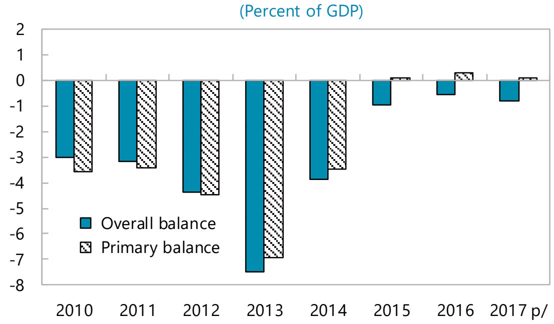


Sources: Central Bank of Honduras and Fund staff estimates and projections.

Figure 4. Honduras: Public Finances

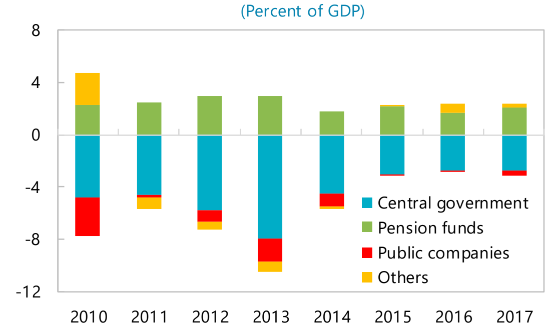
In 2017 the fiscal position remained below the FRL deficit ceiling of 1.5 percent of GDP...

Nonfinancial Public Sector
(Percent of GDP)



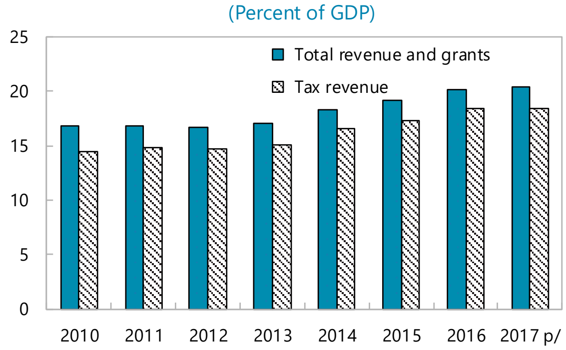
...on the back of central government effort.

NFPS Balance, by Sector
(Percent of GDP)



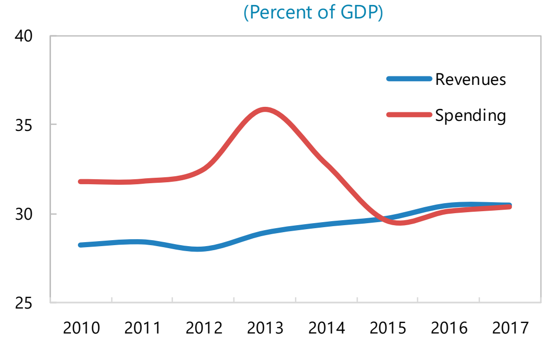
Fiscal discipline was sustained on stable tax revenues...

Revenues and Grants-Central Government
(Percent of GDP)



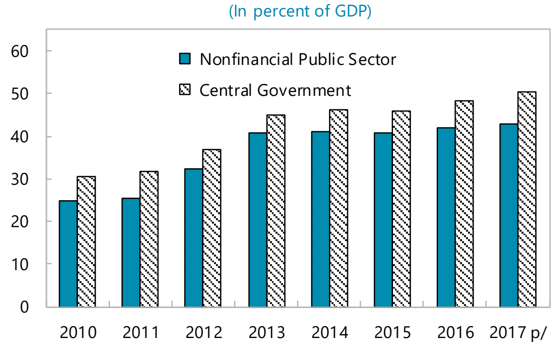
...and a continuous control of primary spending.

Composition of Fiscal Consolidation
(Percent of GDP)



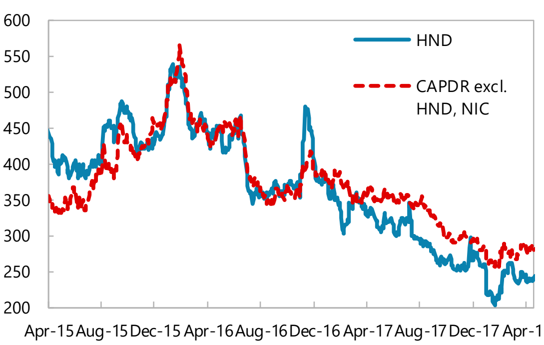
The stronger fiscal position helped contain debt growth, ...

Public Debt
(In percent of GDP)



..and improve conditions to access global markets.

EMBI Spreads

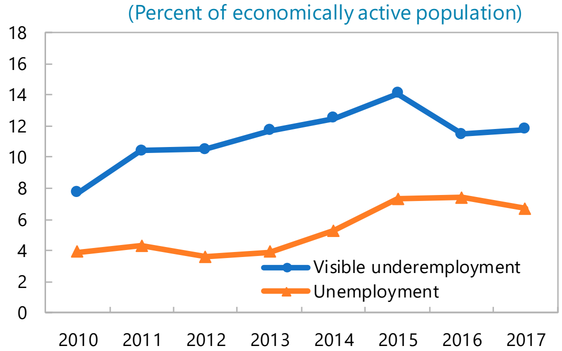


Sources: Central Bank of Honduras and Fund staff estimates and projections.

Figure 5. Honduras: Institutional Factors

Higher potential growth is needed to create employment…

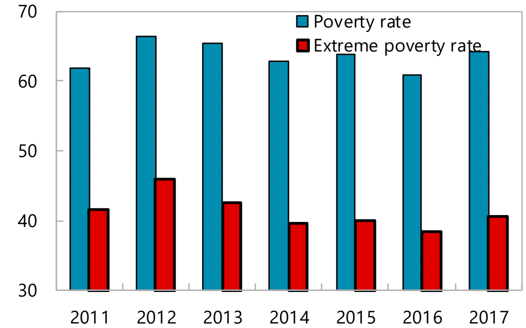
Labor Market Indicators
(Percent of economically active population)



Sources: Permanent Household Survey and IMF staff calculations.

… and make greater progress toward poverty reduction.

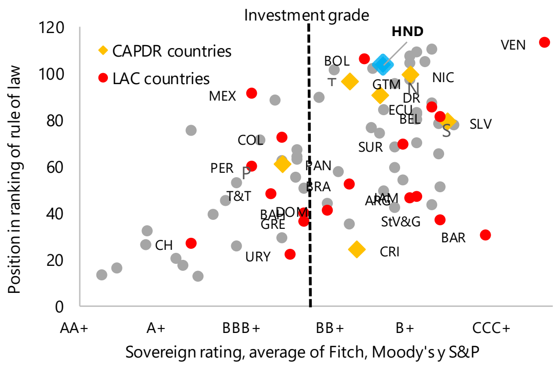
Poverty and Extreme Poverty Rates
(Percent of population)



Source: INE.

To reach higher potential growth, institutional reforms are needed …

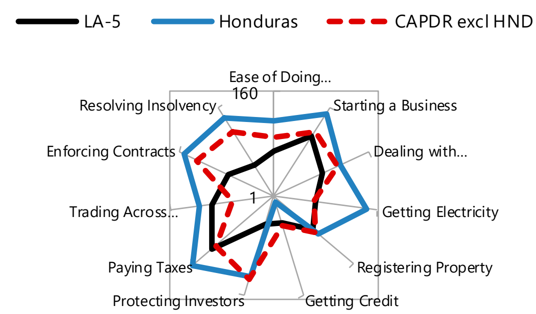
Emerging Markets: Sovereign Ratings and Rule of Law



Source: World Justice Project, Fitch, Moody's, and S&P.

… together with lower transaction costs and better conditions to conduct business …

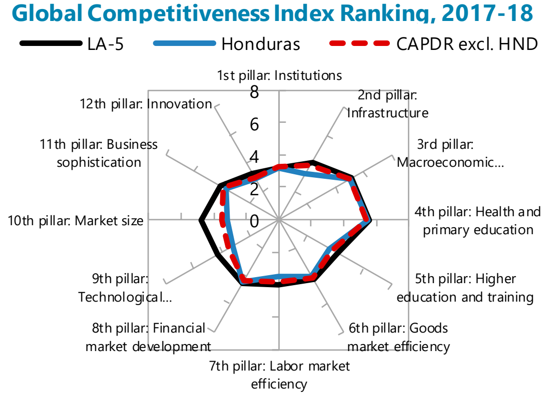
Doing Business Ranking, 2018



Source: Doing Business Report, 2018.

… thereby improving the country's competitiveness and investment prospects.

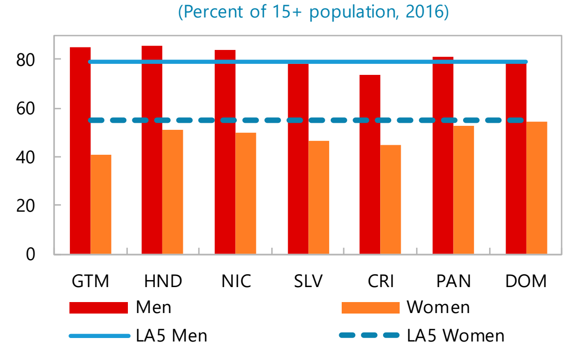
Global Competitiveness Index Ranking, 2017-18



Sources: Global Competitiveness Report, 2018.

Reducing the female labor participation gap is also important to reach higher growth.

CAPDR Labor Force Participation Rates
(Percent of 15+ population, 2016)



Source: World Bank Development Indicators

Table 1. Honduras: Selected Economic Indicators

I. Social Indicators

Population (2016)	9.1 million	Life expectancy at birth in years (2015)	73
Per capita income in U.S. dollars (PPP, 2016)	4,738	Adult literacy (percent of ages 15 and above, 2014)	89
Rank in UNDP Development Index (2016)	130 of 188	Percent of pop. below poverty line (2016)	61
Unemployment rate (2017)	6.7	Gini index (2014)	51
Underemployment rate (2012)	54.1	Oil imports (2017)	US $1.3 billion
Net FDI (as percent of GDP, 2017)	4.4	Main exports: coffee, bananas, palm oil, and maquila.	

II. Economic Indicators

	2013	2014	2015	2016	2017 Prel.	2018 Proj.	2019	2020	2021	2022	2023
Real Sector (percentage changes in contributions to growth)											
Real GDP	**2.8**	**3.1**	**3.8**	**3.8**	**4.8**	**3.7**	**3.7**	**3.7**	**3.7**	**3.8**	**3.8**
Domestic demand	0.7	3.3	7.7	3.4	5.2	3.3	4.1	4.2	4.3	4.3	4.3
Consumption	3.2	1.5	3.2	3.8	3.8	3.3	3.0	3.0	3.1	2.8	3.1
Private	2.8	1.9	2.9	3.1	3.5	3.3	2.9	2.9	3.0	2.7	3.0
Public	0.5	-0.4	0.3	0.7	0.3	0.0	0.1	0.1	0.1	0.1	0.1
Investment	-2.5	1.8	4.6	-1.0	1.4	0.0	1.1	1.2	1.3	1.5	1.2
Private 1/	-3.0	2.4	4.8	-1.5	0.4	0.3	0.7	1.1	1.0	1.1	1.2
Public	0.5	-0.6	-0.2	0.6	0.9	-0.4	0.4	0.1	0.3	0.4	-0.1
Net exports	2.1	-0.3	-3.9	0.9	-0.4	0.4	-0.4	-0.5	-0.6	-0.4	-0.4
Exports	-0.8	1.9	1.7	0.2	3.1	0.5	1.6	1.3	1.8	2.1	1.9
Imports	2.9	-2.2	-5.6	0.7	-3.5	-0.1	-2.0	-1.7	-2.4	-2.6	-2.3
Prices (annual percentage change)											
GDP deflator	1.4	6.8	6.9	3.5	4.2	4.2	4.3	4.1	4.1	4.0	4.0
Consumer prices (eop)	4.9	5.8	2.4	3.3	4.7	5.0	4.5	4.0	4.0	4.0	4.0
Consumer prices (average)	5.2	6.1	3.2	2.7	3.9	4.8	4.5	4.0	4.0	4.0	4.0
Saving and Investment (percent of GDP)											
Gross domestic investment	**22.9**	**23.0**	**26.4**	**23.4**	**24.0**	**24.9**	**25.1**	**25.6**	**26.0**	**26.7**	**27.1**
Private sector	17.9	19.2	22.6	20.2	19.5	21.2	21.1	21.6	21.9	22.2	22.8
Public sector	5.0	3.8	3.8	3.2	4.4	3.7	4.0	4.0	4.1	4.5	4.3
Gross national savings	**13.4**	**16.0**	**20.5**	**20.7**	**22.3**	**21.1**	**21.2**	**21.6**	**22.2**	**22.9**	**23.2**
Private sector	16.2	16.4	17.7	18.1	18.8	18.4	18.1	18.5	18.7	19.2	19.7
Public sector	-2.8	-0.3	2.8	2.6	3.5	2.5	2.9	2.9	3.2	3.5	3.3
Nonfinancial public sector (percent of GDP)											
Primary balance	-7.0	-3.4	0.1	0.3	0.1	0.3	0.5	0.6	0.6	0.5	0.6
Overall balance	-7.5	-3.9	-0.9	-0.5	-0.8	-0.8	-0.8	-0.7	-0.7	-0.7	-0.7
o/w interest payments (net)	-0.5	-0.4	-1.1	-0.9	-0.9	-1.1	-1.3	-1.4	-1.3	-1.2	-1.2
Public sector gross debt	38.6	39.3	39.0	39.9	40.3	40.8	41.3	41.4	41.4	40.8	39.9
Balance of payments											
External current account balance (percent of GDP)	-9.5	-6.9	-4.7	-2.7	-1.7	-3.8	-3.9	-4.0	-3.9	-3.9	-3.8
Exports, f.o.b. (annual percentage change)	-6.6	4.0	1.3	-3.5	9.3	2.4	3.8	4.6	3.6	4.5	4.6
Imports, f.o.b. (annual percentage change)	-3.7	1.2	0.8	-5.5	7.2	5.7	3.9	4.2	3.9	4.8	4.8
Worker's Remittances (percent of GDP)	16.7	17.0	17.4	17.8	18.7	18.6	18.7	18.7	18.8	18.9	19.0
Net International Reserves (millions of dollars)	2,211	2,475	2,778	2,655	3,363	3,413	3,568	3,765	4,027	4,313	4,620
GIR (In months of imports) 2/	3.8	4.3	4.8	4.7	5.3	5.1	5.1	5.1	5.1	5.1	5.1
M1 to Net International Reserves (ratio)	1.6	1.7	1.6	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Terms of Trade (annual percent change)	-3.2	4.4	6.5	-2.5	0.0	-0.3	2.2	1.4	0.5	0.2	0.1
Real effective exchange rate (eop, depreciation -)	0.2	3.8	1.8	-2.2	-1.5	...	...	...	...	...	...
Money and Financial											
Broad money (percentage change)	8.4	13.2	8.4	13.9	12.4	9.5	9.1	9.1	9.7	10.2	9.1
Private sector credit (percentage change)	11.2	10.7	10.4	10.6	9.4	10.8	10.6	9.1	9.0	8.8	8.8
Bank Assets (percent of GDP)	88.9	104.6	97.0	96.7	96.8	99.3	101.6	102.6	103.5	104.3	105.0
Private Credit (percent of GDP)	54.3	54.6	54.3	55.9	56.0	57.4	58.8	59.3	59.8	60.3	60.7
Non-Performing Loans to total loans (ratio)	3.4	3.3	3.0	2.9	2.8	2.6	2.5	2.3	2.2	2.1	2.0
Capital Adequacy (percent)	14.5	14.6	14.0	13.8	13.8	...	...	...	...	...	...

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

1/ Net of change in inventories

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

Table 2. Honduras: Statement of Operations of the Central Government

(In percent of GDP)

	Act.		Prel.	Projections					
	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	**19.2**	**20.1**	**20.4**	**19.6**	**19.3**	**19.2**	**19.2**	**19.1**	**19.1**
Taxes	17.3	18.4	18.4	17.9	17.6	17.6	17.5	17.5	17.5
Taxes on income	5.5	6.0	6.2	5.9	5.9	5.8	5.8	5.7	5.8
Taxes on property	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Taxes on goods and services	10.5	11.0	10.9	10.6	10.6	10.6	10.6	10.6	10.6
Taxes on foreign trade	0.8	0.8	0.8	0.8	0.6	0.6	0.6	0.6	0.6
Other taxes	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Social contributions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	0.9	0.8	0.6	0.6	0.6	0.6	0.6	0.6	0.5
Other revenue	0.9	0.9	1.4	1.1	1.1	1.1	1.1	1.1	1.0
Expenditure	**22.1**	**22.9**	**23.1**	**22.1**	**22.2**	**22.3**	**22.2**	**22.3**	**22.2**
Expense	**20.1**	**20.9**	**20.3**	**20.2**	**20.3**	**20.4**	**20.1**	**20.1**	**20.0**
Compensation of employees	8.4	8.1	8.5	8.8	8.8	8.8	8.8	8.8	8.8
Purchases of goods and services	3.0	2.8	2.7	2.8	2.8	2.8	2.8	2.8	2.8
Interest	2.6	2.6	2.8	2.9	3.2	3.2	3.0	3.0	2.8
Domestic	1.7	1.7	1.8	1.9	2.2	2.1	2.1	2.0	1.9
Foreign	0.9	0.9	1.0	1.0	1.0	1.1	1.0	1.0	1.0
Subsidies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	3.3	3.7	2.6	2.5	2.3	2.3	2.3	2.3	2.3
Current	2.1	2.4	1.5	1.4	1.2	1.2	1.2	1.2	1.2
Capital	1.1	1.3	1.0	1.1	1.1	1.1	1.1	1.1	1.1
Social benefits	1.1	1.6	1.9	1.6	1.6	1.6	1.6	1.6	1.6
Other expense	1.7	2.0	1.8	1.5	1.5	1.5	1.5	1.5	1.5
Current	0.3	0.3	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Capital	1.4	1.7	1.6	1.5	1.5	1.5	1.5	1.5	1.5
Net acquisition of nonfinancial assets	**2.0**	**2.0**	**2.8**	**2.0**	**1.9**	**1.9**	**2.1**	**2.2**	**2.2**
Gross Operating Balance	**-1.0**	**-0.8**	**0.1**	**-0.6**	**-1.1**	**-1.1**	**-1.0**	**-1.0**	**-0.9**
Net lending (+)/borrowing (-)	**-3.0**	**-2.8**	**-2.7**	**-2.6**	**-2.9**	**-3.1**	**-3.1**	**-3.2**	**-3.1**
Net financial transactions	**-3.0**	**-2.8**	**-2.7**	**-2.6**	**-2.9**	**-3.1**	**-3.1**	**-3.2**	**-3.1**
Net acquisition of financial assets	**0.5**	**-0.3**	**2.5**	**-0.1**	**0.6**	**0.1**	**-0.2**	**-0.2**	**-1.0**
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.5	-0.3	2.5	-0.1	0.6	0.1	-0.2	-0.2	-1.0
Currency and deposits	0.5	-0.3	2.5	-0.1	0.6	0.1	-0.2	-0.2	-1.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	**3.5**	**2.5**	**5.2**	**2.5**	**3.6**	**3.2**	**2.9**	**3.0**	**2.1**
Foreign	2.2	0.7	3.7	1.1	1.9	1.0	1.9	3.4	-0.6
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	2.2	0.7	3.7	1.1	1.9	1.0	1.9	3.4	-0.6
Disbursment	2.4	1.5	4.8	2.0	2.9	3.8	2.8	4.9	0.9
Amorizations	-0.2	-0.8	-1.1	-0.8	-1.0	-2.8	-0.9	-1.5	-1.5
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing 1/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other external	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	1.3	1.8	1.5	1.4	1.7	2.2	1.0	-0.4	2.7
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	1.3	3.0	1.2	1.2	1.4	2.4	1.4	0.1	3.1
Other accounts payable	0.4	-1.3	0.3	0.0	0.0	0.0	0.0	0.0	0.0
PPPs/other	0.0	0.5	0.4	0.5	0.7	0.2	0.0	-0.1	-0.1
Adjustment for HIPC debt relief 2/	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3
Memorandum items:									
Net lending minus interest payments	-0.4	-0.1	0.0	0.3	0.3	0.2	-0.1	-0.2	-0.2
Gross debt	46.0	48.2	50.0	50.5	51.3	52.3	52.7	52.4	52.6
Excluding BCH recapitalization	42.6	44.4	45.6	46.4	47.0	47.9	48.6	48.2	48.7
Nominal GDP (in billions of Lempiras)	460.4	494.2	539.6	582.8	629.9	680.5	735.3	794.2	857.7

Sources: Honduran authorities, Fund staff estimates and projections.

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

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

Table 3. Honduras: Statement of Operations of the Nonfinancial Public Sector

(In percent of GDP)

	Act.		Prel.	Projections					
	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	**31.0**	**32.4**	**32.0**	**31.4**	**30.9**	**30.9**	**30.9**	**30.7**	**30.3**
Taxes	17.9	19.4	18.8	18.3	18.2	18.1	18.2	18.3	18.1
Taxes on income	5.5	6.0	6.2	5.9	5.9	5.8	5.8	5.7	5.8
Taxes on property	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Taxes on goods and services	10.5	11.0	10.9	10.6	10.6	10.6	10.6	10.6	10.6
Taxes on foreign trade	0.8	0.8	0.8	0.8	0.6	0.6	0.6	0.6	0.6
Other taxes	1.0	1.5	0.9	0.9	1.0	1.0	1.2	1.3	1.0
Social contributions	2.9	3.1	3.3	3.3	3.3	3.4	3.4	3.4	3.4
Grants	0.9	0.8	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Other revenue	9.3	9.1	9.3	9.2	8.8	8.8	8.6	8.5	8.3
Expenditure	**31.9**	**32.9**	**32.8**	**32.2**	**31.7**	**31.6**	**31.5**	**31.4**	**31.0**
Expense	**28.1**	**29.7**	**28.4**	**28.6**	**27.7**	**27.7**	**27.4**	**26.9**	**26.7**
Compensation of employees	11.7	11.3	11.3	11.5	11.5	11.5	11.5	11.5	11.5
Purchases of goods and services	8.1	8.1	8.4	8.8	8.7	8.6	8.4	8.2	8.0
Interest	2.3	2.8	2.4	2.6	2.7	2.7	2.5	2.4	2.4
Domestic	1.4	1.8	1.4	1.5	1.7	1.6	1.6	1.4	1.4
Foreign	0.9	1.0	1.0	1.1	1.0	1.1	1.0	1.0	1.0
Subsidies	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Social benefits	3.2	3.6	4.1	3.8	3.8	3.8	3.8	3.8	3.8
Other expense	2.8	3.8	2.2	1.9	1.0	1.0	1.1	1.0	1.0
Current	1.2	1.1	0.3	0.1	0.1	0.1	0.1	0.1	0.1
Capital	1.6	2.7	1.8	1.7	0.9	0.9	1.0	0.8	0.9
Net acquisition of nonfinancial assets	**3.8**	**3.2**	**4.4**	**3.7**	**4.0**	**4.0**	**4.1**	**4.5**	**4.3**
Gross Operating Balance	**2.9**	**2.7**	**3.6**	**2.8**	**3.2**	**3.2**	**3.5**	**3.8**	**3.6**
Net lending (+)/borrowing (-)	**-0.9**	**-0.5**	**-0.8**	**-0.8**	**-0.8**	**-0.7**	**-0.7**	**-0.7**	**-0.7**
Net financial transactions	**-0.9**	**-0.5**	**-0.8**	**-0.8**	**-0.8**	**-0.7**	**-0.7**	**-0.7**	**-0.7**
Net acquisition of financial assets	**0.9**	**0.1**	**1.1**	**1.5**	**1.4**	**0.5**	**0.8**	**-1.0**	**0.1**
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.9	0.1	1.1	1.5	1.4	0.5	0.8	-1.0	0.1
Currency and deposits	0.7	-0.5	0.9	1.3	1.3	0.4	0.8	-1.0	0.0
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.1	0.6	0.2	0.2	0.2	0.1	0.0	0.0	0.0
Other accounts receivable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	**1.8**	**0.6**	**1.9**	**2.3**	**2.2**	**1.3**	**1.5**	**-0.3**	**0.7**
Foreign	2.1	1.0	4.1	1.4	1.7	1.0	1.4	0.2	-0.7
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	2.1	1.0	4.1	1.4	1.7	1.0	1.4	0.2	-0.7
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing 1/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other external	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	0.1	0.0	-1.8	1.3	0.9	0.6	0.4	-0.2	1.8
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.6	1.0	-0.5	0.9	0.1	0.5	0.4	0.0	1.9
Other accounts payable	-0.8	-1.4	-1.7	-0.2	0.0	0.0	0.0	0.0	0.0
PPPs/other	0.3	0.5	0.4	0.5	0.7	0.2	0.0	-0.1	-0.1
Adjustment for HIPC debt relief 2/	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3
Memorandum items:									
Net lending minus net interest payments	0.1	0.3	0.1	0.3	0.5	0.6	0.6	0.5	0.6
Gross total debt	39.0	39.9	40.3	40.8	41.3	41.4	42.2	40.8	39.9
Nominal GDP (in billions of Lempiras)	460.4	494.2	539.6	582.8	629.9	680.5	735.3	794.2	857.7
Memorandum items									
Net lending of ENEE	-0.3	-0.3	-0.6	-0.9	-0.8	-0.6	-0.3	-0.2	0.0

Sources: Honduran authorities, Fund staff estimates and projections.

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

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

Table 4. Honduras: Summary Accounts of the Financial System
(In millions of Lempiras; end-December)

	2015	2016	2017	2018	2019	2020	2021	2022	2023
				Projections					
				I. Central Bank					
Net International Reserves 1/	**85,495**	**91,370**	**112,883**	**120,662**	**131,339**	**143,905**	**158,318**	**174,824**	**188,158**
(In millions of US$)	3,809	3,868	4,758	4,872	5,050	5,270	5,575	5,948	6,215
Net International Reserves (in millions of US$) 2/	2,778	2,655	3,363	3,413	3,568	3,765	4,027	4,313	4,620
Net Domestic Assets	**-56,043**	**-60,010**	**-75,317**	**-80,087**	**-87,490**	**-96,530**	**-107,127**	**-119,537**	**-128,446**
Credit to the public sector (net)	3,368	9,645	7,472	5,341	3,443	3,656	3,903	4,177	4,517
Other depository institutions (net)	-63,211	-74,216	-84,589	-89,694	-95,174	-104,521	-115,452	-128,218	-136,999
Other financial institutions	8,026	10,277	8,109	10,809	10,935	11,014	11,094	11,174	11,254
Nonfinancial private sector	-858	-214	-230	-242	-277	-312	-347	-382	-417
Medium and long-term net foreign assets	1,038	956	898	943	990	1,039	1,081	1,119	605
Other items net	-4,406	-6,457	-6,982	-7,243	-7,406	-7,406	-7,406	-7,406	-7,406
Currency issue	**29,452**	**31,359**	**37,567**	**40,575**	**43,850**	**47,376**	**51,190**	**55,287**	**59,712**
				II. Depository Institutions					
Net Foreign Assets	**-18,603**	**-14,280**	**-14,026**	**-11,035**	**-13,629**	**-20,247**	**-21,877**	**-28,783**	**-31,550**
(In millions of US$)	-829	-605	-591	-446	-524	-741	-770	-979	-1,042
Foreign assets (million Lempiras)	10,568	12,220	15,165	20,493	20,444	16,566	17,899	14,177	14,847
Foreign assets (in million of US$)	471	517	639	827	786	607	630	482	490
Net Domestic Assets	**238,902**	**263,795**	**290,547**	**312,396**	**342,473**	**379,002**	**415,421**	**462,764**	**504,732**
Credit to the monetary authorities (net)	71,087	81,483	97,703	93,465	98,863	108,082	118,579	130,804	138,952
Credit to other financial institutions (net)	-30,372	-31,865	-34,120	-37,740	-40,786	-46,370	-53,294	-63,852	-86,842
Credit to the nonfinancial public sector (net)	1,099	-1,915	-8,849	-10,964	-18,040	-18,288	-20,812	-13,094	2,639
Central government	-12,541	-15,625	-20,088	-20,723	-24,261	-24,335	-26,102	-18,847	-3,979
Other nonfinancial public sector	9,612	9,250	5,459	4,613	3,198	3,148	2,416	2,493	2,572
Local governments	4,028	4,460	5,780	5,146	3,023	2,899	2,874	3,259	4,046
Credit to the private sector	249,894	276,298	302,188	334,708	370,060	403,884	440,063	478,787	520,727
Local currency	178,301	200,895	222,714	246,651	272,669	297,555	324,170	352,652	383,496
Foreign currency	71,593	75,403	79,474	88,057	97,391	106,329	115,894	126,135	137,231
Other items net	-49,048	-60,207	-66,375	-67,072	-67,624	-68,306	-69,115	-69,881	-70,744
Liabilities	**220,299**	**250,498**	**276,521**	**301,361**	**328,844**	**358,756**	**393,544**	**433,981**	**473,182**
Of which: Deposits in domestic currency	156,364	176,036	198,333	216,831	238,414	262,073	289,651	319,412	348,264
Of which: Deposits in foreign currency	62,609	72,425	78,188	84,530	90,430	96,683	103,894	114,569	124,918
				III. Financial System					
Net Foreign Assets	**64,235**	**74,291**	**95,972**	**106,827**	**114,911**	**120,859**	**133,641**	**143,241**	**153,809**
(In millions of US$)	2,862	3,145	4,069	4,313	4,419	4,426	4,706	4,873	5,081
Net Domestic Assets	**178,057**	**199,622**	**215,803**	**232,940**	**255,825**	**283,580**	**309,986**	**345,622**	**379,487**
Credit to the nonfinancial public sector	4,467	7,730	-1,377	-5,623	-14,597	-14,632	-16,909	-8,917	7,156
Credit to the private sector	249,894	276,298	302,188	334,708	370,060	403,884	440,063	478,787	520,727
Local currency	178,301	200,895	222,714	246,651	272,669	297,555	324,170	352,652	383,496
Foreign currency	71,593	75,403	79,474	88,057	97,391	106,329	115,894	126,135	137,231
Other assets net	-6,010	-1,033	-15,761	-22,676	-20,975	-22,010	-25,233	-32,340	-52,917
Other items net 3/	-70,294	-83,373	-69,247	-73,468	-78,664	-83,662	-87,936	-91,908	-95,479
Broad Money (M4)	**242,292**	**276,011**	**310,292**	**339,767**	**370,736**	**404,439**	**443,626**	**488,863**	**533,296**
				(Rate of growth 12 months)					
Currency issue	11.6	6.5	19.8	8.0	8.1	8.0	8.1	8.0	8.0
Currency in circulation	12.7	27.7	22.6	9.0	9.1	9.1	9.7	9.7	9.6
Broad money	8.4	13.9	12.4	9.5	9.1	9.1	9.7	10.2	9.1
Broad money (constant exchange rate)	7.4	11.6	13.7	7.7	7.8	7.8	8.7	9.3	8.3
Credit to the private sector	10.4	10.6	9.4	10.8	10.6	9.1	9.0	8.8	8.8
Credit to the private sector (constant exchange rate)	9.2	9.1	9.3	9.4	9.2	7.8	7.9	7.8	7.9
M1	14.7	11.0	26.7	10.0	9.7	9.7	9.9	9.4	9.3

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

			Prel.			Projections			
	2015	2016	2017	2018	2019	2020	2021	2022	2023
	(In millions of U.S. dollars; unless otherwise indicated)								
Current account	**-978**	**-587**	**-380**	**-915**	**-962**	**-1,011**	**-1,021**	**-1,058**	**-1,100**
Trade Account	-2,949	-2,619	-2,649	-3,093	-3,229	-3,331	-3,488	-3,675	-3,872
Exports f.o.b.	5,720	5,556	6,145	6,360	6,623	6,980	7,216	7,557	7,931
Maquila Net (exports-imports)	1,728	1,635	1,550	1,654	1,700	1,753	1,812	1,921	2,038
Coffee	986	913	1,318	1,285	1,457	1,617	1,681	1,749	1,819
Others	3,006	3,008	3,278	3,421	3,466	3,610	3,722	3,887	4,075
Imports f.o.b.	-8,669	-8,175	-8,794	-9,453	-9,853	-10,311	-10,703	-11,232	-11,803
Petroleum products	-1,246	-1,073	-1,366	-1,595	-1,563	-1,562	-1,585	-1,644	-1,734
Others	-7,423	-7,102	-7,428	-7,859	-8,290	-8,749	-9,118	-9,588	-10,069
Services (net)	-445	-463	-589	-679	-699	-731	-748	-770	-805
Income (net)	-1,426	-1,508	-1,635	-1,772	-1,823	-1,882	-1,915	-1,997	-2,076
Of which: payments on direct investments	-1,183	-1,278	-1,392	-1,500	-1,544	-1,588	-1,642	-1,710	-1,789
Transfers (net)	3,842	4,003	4,493	4,628	4,789	4,933	5,129	5,384	5,653
Of which: Remittances	3,652	3,847	4,305	4,473	4,630	4,769	4,959	5,207	5,468
Others	191	155	188	155	160	164	170	177	185
Capital and Financial account	**1,525**	**788**	**1,753**	**965**	**1,117**	**1,208**	**1,283**	**1,344**	**1,407**
Financial account	**1,382**	**658**	**1,572**	**809**	**954**	**1,040**	**1,109**	**1,163**	**1,218**
Direct investment (net)	952	900	1,013	1,013	1,048	1,083	1,126	1,179	1,241
Other private capital flows (net)	48	-395	-229	-476	-532	-296	-399	-415	177
General government (net)	383	152	789	271	438	253	382	400	-200
Capital account	**142**	**130**	**181**	**157**	**163**	**168**	**174**	**181**	**189**
Errors and omissions	-256	-151	-488	0	0	0	0	0	0
Overall balance	**290**	**50**	**885**	**50**	**155**	**197**	**262**	**286**	**307**
Change in central bank reserves (- increase)	**-303**	**-66**	**-884**	**-50**	**-155**	**-197**	**-262**	**-286**	**-307**
Exceptional financing	**13**	**16**	**-1**	**0**	**0**	**0**	**0**	**0**	**0**
	(In percent of GDP; unless otherwise indicated)								
Current account	**-4.7**	**-2.7**	**-1.7**	**-3.8**	**-3.9**	**-4.0**	**-3.9**	**-3.9**	**-3.8**
Trade Account	-14.1	-12.1	-11.5	-12.8	-13.0	-13.0	-13.2	-13.4	-13.5
Exports f.o.b.	27.3	25.7	26.7	26.4	26.7	27.3	27.3	27.5	27.6
Maquila net (exports-imports)	8.2	7.6	6.7	6.9	6.9	6.9	6.9	7.0	7.1
Coffee	4.7	4.2	5.7	5.3	5.9	6.3	6.4	6.4	6.3
Others	14.3	13.9	14.3	14.2	14.0	14.1	14.1	14.1	14.2
Imports f.o.b.	-41.3	-37.8	-38.3	-39.2	-39.7	-40.4	-40.5	-40.9	-41.1
Petroleum products	-5.9	-5.0	-5.9	-6.6	-6.3	-6.1	-6.0	-6.0	-6.0
Others	-35.4	-32.8	-32.3	-32.6	-33.4	-34.3	-34.5	-34.9	-35.0
Services (net)	-2.1	-2.1	-2.6	-2.8	-2.8	-2.9	-2.8	-2.8	-2.8
Of which: tourism receipts	3.2	3.2	3.1	3.1	3.1	3.1	3.2	3.2	3.2
Income (net)	-6.8	-7.0	-7.1	-7.3	-7.3	-7.4	-7.3	-7.3	-7.2
Of which: payments on direct investments	-5.6	-5.9	-6.1	-6.2	-6.2	-6.2	-6.2	-6.2	-6.2
Of which: public sector interest payments	-0.9	-0.9	-0.8	-1.0	-1.0	-1.1	-1.0	-1.0	-1.0
Transfers (net)	18.3	18.5	19.6	19.2	19.3	19.3	19.4	19.6	19.7
Of which: Remittances	17.4	17.8	18.7	18.6	18.7	18.7	18.8	18.9	19.0
Capital and Financial account	**7.3**	**3.6**	**7.6**	**4.0**	**4.5**	**4.7**	**4.9**	**4.9**	**4.9**
Financial account	**6.6**	**3.0**	**6.8**	**3.4**	**3.8**	**4.1**	**4.2**	**4.2**	**4.2**
Direct investment (net)	4.5	4.2	4.4	4.2	4.2	4.2	4.3	4.3	4.3
Other private capital flows (net)	0.2	-1.8	-1.0	-2.0	-2.1	-1.2	-1.5	-1.5	0.6
Public sector borrowing (net)	1.8	0.7	3.4	1.1	1.8	1.0	1.4	1.5	-0.7
Capital account	**0.7**	**0.6**	**0.8**	**0.6**	**0.7**	**0.7**	**0.7**	**0.7**	**0.7**
Errors and omissions	-1.2	-0.7	-2.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	**1.4**	**0.2**	**3.8**	**0.2**	**0.6**	**0.8**	**1.0**	**1.0**	**1.1**
Change in central bank reserves (- increase)	**-1.4**	**-0.3**	**-3.8**	**-0.2**	**-0.6**	**-0.8**	**-1.0**	**-1.0**	**-1.1**
Exceptional financing	**0.1**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:									
Terms of trade (percent change)	6.5	-2.5	0.0	-0.3	2.2	1.4	0.5	0.2	0.1
Exports of goods (percent change)	1.3	-3.5	9.3	2.4	3.8	4.6	3.6	4.5	4.6
Of Which: volume growth (percent change)	3.7	2.3	6.6	0.2	2.0	3.4	2.9	4.3	4.5
Imports of goods (percent change)	0.8	-5.5	7.2	5.7	3.9	4.2	3.9	4.8	4.8
Of Which: volume growth (percent change)	9.9	-2.4	4.6	3.3	4.3	4.4	3.4	3.4	3.4
Gross reserves (end of period, millions of U.S. dollars)	3,992	4,177	5,086	5,137	5,292	5,488	5,750	6,037	6,344
In months of next year imports (excluding maquila)	4.8	4.7	5.3	5.1	5.1	5.1	5.1	5.1	5.1
Total external debt to GDP ratio (in percent)	35.5	34.6	37.4	36.1	36.1	36.1	36.5	36.6	34.5
Nominal GDP (millions of U.S. dollars)	20,980	21,644	22,975	24,106	24,812	25,530	26,401	27,484	28,751

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

Table 6. Honduras: External Financing Needs and Sources

(In millions of U.S. dollars)

				Projections					
	2015	2016	2017	2018	2019	2020	2021	2022	2023
Current account deficit	978	587	380	915	962	1,011	1,021	1,058	1,100
Debt amortizations	354	388	411	448	453	956	445	626	630
Subtotal (requirements)	**1,333**	**975**	**791**	**1,363**	**1,415**	**1,968**	**1,465**	**1,684**	**1,730**
Capital account flows (net)	142	130	181	157	163	168	174	181	189
Foreign direct investment (net)	952	900	1,013	1,013	1,048	1,083	1,126	1,179	1,241
Public sector borrowing (projects)	580	391	573	522	700	523	646	350	260
Bonds	0	0	700	0	0	500	0	500	0
Other capital flows (net) 1/	-215	-380	-791	-278	-340	-110	-218	-240	347
Change in reserves (+ decrease)	-303	-66	-884	-50	-155	-197	-262	-286	-307
Subtotal (sources)	**1,156**	**975**	**791**	**1,363**	**1,415**	**1,968**	**1,465**	**1,684**	**1,730**
Financing gap	**177**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
World Bank	50	0	0	0	0	0	0	0	0
IADB	100	0	0	0	0	0	0	0	0
IMF	0	0	0	0	0	0	0	0	0
EU	27	0	0	0	0	0	0	0	0

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

1/ Includes errors and omissions.

Table 7. Honduras: External Vulnerability Indicators

			Prel	Projections					
	2015	2016	2017	2018	2019	2020	2021	2022	2023
Exports of goods and services, annual percent	1.2	-2.4	8.5	2.9	2.4	4.9	3.8	4.7	5.1
Imports of goods and services, annual percent	0.8	-4.2	7.6	6.4	3.0	4.4	4.0	4.5	5.1
Terms of trade (deterioration -)	6.5	-2.5	0.0	-1.6	2.0	1.4	0.5	0.2	0.1
Real effective exchage rate (eop, depreciation -)	1.8	-2.2	-1.5	...	...	...	...	...	...
Current account balance (percent of GDP)	-4.7	-2.7	-1.7	-3.9	-4.0	-4.1	-4.1	-3.9	-3.9
Capital and financial account (percent of GDP)	7.3	3.6	7.6	3.5	4.6	4.5	4.6	4.7	5.0
External public debt (percent of GDP)	28.2	28.2	31.1	30.8	31.5	32.2	32.5	32.3	31.8
Gross official reserves									
in millions of U.S. dollars	3,992	4,177	5,060	4,960	5,092	5,184	5,309	5,527	5,837
in percent of short-term external debt	1,187	1,366	1,582	1,562	1,616	1,602	1,589	1,591	1,609
Net international reserves									
in millions of U.S. dollars	2,783	2,655	3,363	3,263	3,395	3,486	3,612	3,829	4,140
in percent of short-term external debt	828	868	1,106	1,083	1,133	1,131	1,133	1,153	1,189

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

Table 8. Honduras: Medium-Term Macroeconomic Framework

(In percent of GDP, unless otherwise specified)

						Projections					
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Growth and prices (in percent)											
Real GDP growth	2.8	3.1	3.8	3.8	4.8	3.7	3.7	3.7	3.7	3.8	3.8
GDP deflator	1.4	6.8	6.9	3.5	4.2	4.2	4.3	4.1	4.1	4.0	4.0
CPI inflation (eop)	4.9	5.8	2.4	3.3	4.7	5.0	4.5	4.0	4.0	4.0	4.0
Investment and saving											
Gross domestic investment	**37.6**	**23.0**	**26.4**	**23.4**	**24.0**	**24.9**	**25.1**	**25.6**	**26.0**	**26.7**	**27.0**
Private sector	17.9	19.2	22.6	20.2	19.5	21.2	21.1	21.6	21.9	22.2	22.8
Public sector	19.7	3.8	3.8	3.2	4.4	3.7	4.0	4.0	4.1	4.5	4.3
Gross national savings	**12.2**	**16.0**	**21.7**	**20.7**	**22.3**	**21.1**	**21.2**	**21.6**	**22.2**	**22.9**	**23.2**
Private sector	15.0	16.4	19.0	18.1	18.8	18.5	18.3	18.7	19.0	19.3	19.9
Public sector	-2.8	-0.3	2.8	2.6	3.5	2.5	2.9	2.9	3.2	3.5	3.3
Balance of payments											
External current account	-9.5	-6.9	-4.7	-2.7	-1.7	-3.8	-3.9	-4.0	-3.9	-3.9	-3.8
Non oil current account	1.6	2.7	1.3	2.2	4.3	2.8	2.4	2.2	2.1	2.1	2.2
Gross international reserves (millions of dollar:	3,255	3,698	3,992	4,177	5,086	5,137	5,292	5,488	5,750	6,037	6,344
Terms of Trade (annual percent change)	-3.2	4.4	6.5	-2.5	0.0	-0.3	2.2	1.4	0.5	0.2	0.1
External debt	**35.9**	**36.3**	**35.5**	**34.6**	**37.4**	**36.1**	**36.1**	**36.1**	**36.5**	**36.6**	**34.5**
Nonfinancial public sector											
Revenue	30.5	31.0	31.0	32.4	32.0	31.4	30.9	30.9	30.9	30.7	30.3
Of which: Non-interest revenue and grants	28.9	29.4	29.8	30.5	30.5	29.9	29.5	29.5	29.6	29.5	29.2
Expenditure	37.9	34.9	31.9	32.9	32.8	32.2	31.7	31.6	31.5	31.4	31.0
Of which: Non-interest expenditure	35.9	32.8	29.6	30.2	30.4	29.6	29.0	28.9	29.0	29.0	28.6
Primary balance	**-7.0**	**-3.4**	**0.1**	**0.3**	**0.1**	**0.3**	**0.5**	**0.6**	**0.6**	**0.5**	**0.6**
Overall balance	**-7.5**	**-3.9**	**-0.9**	**-0.5**	**-0.8**	**-0.8**	**-0.8**	**-0.7**	**-0.7**	**-0.7**	**-0.6**
Central government											
Revenue	17.0	18.3	19.2	20.1	20.4	19.6	19.3	19.2	19.2	19.1	19.1
Expenditure	24.9	22.9	22.1	22.8	23.1	22.1	22.2	22.3	22.2	22.3	22.1
Of which: Non-interest expenditure	22.6	20.4	19.5	20.2	20.4	19.2	19.0	19.1	19.2	19.3	19.3
Primary balance	**-5.6**	**-2.1**	**-0.4**	**-0.1**	**-0.1**	**0.2**	**0.1**	**0.0**	**-0.2**	**-0.4**	**-0.4**
Overall balance	**-7.9**	**-4.5**	**-3.0**	**-2.7**	**-2.7**	**-2.6**	**-2.9**	**-3.1**	**-3.1**	**-3.2**	**-3.1**
Nonfinancial public sector debt											
Total	**38.6**	**39.3**	**39.0**	**39.9**	**40.3**	**40.8**	**41.3**	**41.4**	**41.4**	**40.8**	**39.9**
Domestic debt	7.8	11.0	10.8	11.5	9.6	9.8	9.2	9.0	8.7	8.1	9.3
External debt	30.8	28.3	28.2	28.5	30.7	31.0	32.0	32.4	32.6	32.8	30.5
Monetary and financial											
Broad money (percentage change)	8.4	13.2	8.4	13.9	12.4	9.5	9.1	9.1	9.7	10.2	9.1
Private sector credit (percentage change)	11.2	10.7	10.4	10.6	9.4	10.8	10.6	9.1	9.0	8.8	8.8
Bank assets	90.7	96.1	97.0	96.7	96.8	99.3	101.6	102.6	103.5	104.3	105.0
Private credit	54.3	54.6	54.3	55.9	56.0	57.4	58.8	59.3	59.8	60.3	60.7
Non-performing loans to total loans (ratio)	3.4	3.3	3.0	2.9	2.6	2.7	2.6	2.4	2.3	2.1	2.1
Capital adequacy (percent)	14.5	14.6	14.0	13.8	13.8	…	…	…	…	…	…
Lending rate (eop, in percent)	16.9	15.9	14.0	14.3	13.2	…	…	…	…	…	…
Deposit rate (eop, in percent)	11.0	10.4	8.8	8.2	8.4	…	…	…	…	…	…
Memo items:											
Nominal GDP (in billions of lempiras)	377	415	460	494	540	583	630	681	735	794	858

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

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

(In percent, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	2016	2017	2018M3
Total assets (in millions of Lempiras) 1/	**236,665**	**270,981**	**302,662**	**341,614**	**393,763**	**432,178**	**473,722**	**521,869**	**528,043**
(In percent of GDP)	79	81	84	91	95	94	96	97	91
Number of banks	**17**	**17**	**17**	**17**	**17**	**15**	**15**	**15**	**15**
Domestic	8	7	7	7	8	6	6	6	6
Foreign	9	10	10	10	9	9	9	9	9
Bank concentration									
Number of banks accounting for at least									
25 percent of total assets	2	2	2	2	2	2	2	2	2
75 percent of total assets	6	6	6	6	6	5	5	5	5
Capital adequacy									
Regulatory capital to risk weighted assets (RWA)	14.9	14.9	14.7	14.5	14.6	14.0	13.8	13.7	13.8
Capital (net worth) to assets	9.2	9.1	9.3	9.1	9.2	8.7	8.7	8.7	8.9
Asset quality and composition									
Nonperforming loans(NPLs) to total loans 2/	3.7	2.9	3.3	3.4	3.3	3.0	2.9	2.3	2.3
NPLs net of provisions to capital 2/	-4.4	-6.5	-4.6	-5.2	-5.2	-5.1	-3.4	-5.8	-5.9
Restructured loans to regulatory capital	19.8	26.6	24.7	25.3	22.3	27.9	23.7	25.0	25.4
Non earning assets net of provisions									
to regulatory capital	47.9	46.9	45.0	44.1	51.2	54.6	48.4	41.6	41.1
Provisions to total loans	4.3	3.9	4.0	4.2	4.1	3.8	3.4	3.2	3.2
Provisions to NPLs 2/	118.9	135.0	121.8	123.7	125.5	126.1	117.4	138.0	139.8
Sectoral distribution of loans to total loans:									
Commerce	12.7	13.0	14.4	14.3	14.3	13.6	13.0	14.9	14.9
Construction and real estate	34.2	32.9	30.8	28.9	27.1	24.6	23.6	23.3	23.4
Agriculture and related sectors	0.0	0.0	4.4	4.7	5.0	5.9	7.2	7.4	7.2
Industry	13.6	12.3	11.7	11.9	11.1	11.1	10.4	10.3	9.9
Consumption	16.5	18.3	20.5	21.9	21.0	21.3	23.1	20.9	20.9
Other	23.0	23.6	18.3	18.3	21.5	23.6	22.7	23.2	23.8
Profitability									
Return on assets (ROA)	1.3	1.3	1.5	1.4	1.4	1.4	1.3	1.2	1.3
Return on equity (ROE)	12.5	13.2	15.9	14.5	13.4	14.6	14.6	12.0	12.0
Interest margin to total income	48.2	48.9	52.1	47.5	52.1	52.8	52.9	51.1	50.3
Personnel expenses to administrative expenses	39.6	39.6	39.4	41.8	41.7	42.0	41.8	45.5	45.7
Liquidity									
Liquid assets to total assets	24.4	24.3	21.4	25.0	25.2	24.6	24.3	26.3	26.0
Liquid assets to total short-term liabilities	58.2	58.8	56.2	69.7	70.8	69.5	66.3	71.5	67.9
Dollarization									
Deposits in foreign currency in percent of total	29.5	29.1	30.6	30.6	32.0	29.8	30.2	29.9	29.4
Credit in foreign currency in percent of total	28.3	30.1	31.2	33.5	34.7	33.2	32.1	31.2	32.4

Source: National Commission of Banking and Insurance.
1/ Includes contingent assets.
2/ As of 2012 NPLs include delinquency of restructured loans.

Table 10. Honduras: Summary of Stress Tests Results

	All Banks	Domestic Private	Foreign
Asset Quality			
Nonperforming loans (NPLs, percent of total loans)	2.5	3.2	1.7
Capital adequacy ratio (CAR) pre-shock	13.7	12.9	14.7
Credit Risk Stress Test [1/]			
1. Proportional increase in NPLs			
NPLs (gross)/ total loans	6.9	7.5	6.1
Post-shock CAR (Percent)	10.3	10.0	10.6
2. Sectoral shocks to NPLs			
NPLs (gross)/ total loans	5.3	5.8	4.7
Post-shock CAR (Percent)	11.0	10.8	11.3
Interest Rate Risk Stress Test [2/]			
1. Net interest income impact			
Post-shock CAR (Percent)	13.7	12.9	14.7
CAR change (Pct Point)	0.0	0.0	0.0
2. Repricing impact			
Post-shock CAR (Percent)	11.2	10.1	12.8
CAR change (Pct Point)	-2.4	-2.8	-1.9
Overall change in CAR (NII and Repricing)	-2.4	-2.8	-1.9
FX Stress Tests [3/]			
1. Direct Foreign Exchange Risk			
Post-shock CAR (Percent)	13.3	12.5	14.4
CAR change (Pct Point)	-0.3	-0.3	-0.3
2. Indirect Foreign Exchange Risk			
Post-shock CAR (Percent)	13.1	12.3	14.2
CAR change (Pct Point)	-0.3	-0.3	-0.2
Overall change in CAR (Direct and Indirect)	-0.6	-0.6	-0.6
Liquidity Stress Test (# of liquid banks after 5 days) [4/]			
Simple liquidity test (run on all banks, fire-sale of assets)	15	6	9

Notes. The sample includes a total of 15 private banks of which 6 are domestic and 9 foreign.

1/ Proportional increase in NPLs assumes 5 percent of outstanding performance loans to become nonperforming (10-year average NPL plus 2 stds) ; Sectoral shocks assumes 9, 6, and 8 percent of outstanding loans in the retail, construiction and credit cards sectors becoming nonperforming.

2/ The Interest Rate shock assumes 3.25 percenteage points increase in nominal interest rate.

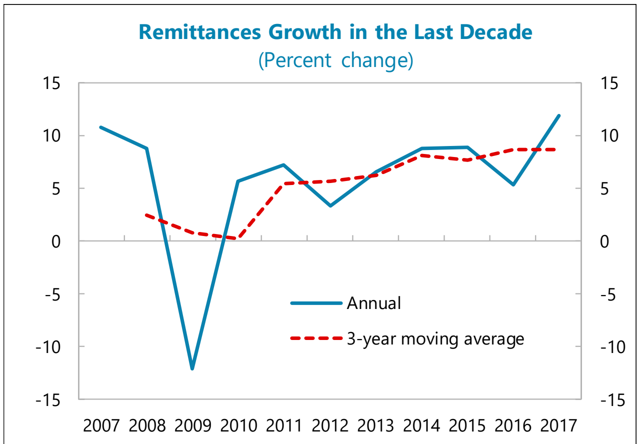
3/ The FX Shock shock assumes a 14 percent depreciation of the FX rate leading to 60 percent of FX koans becoming NPLs.

4/ The Liquidity Shock assumes a 10 and 8 percent withdrawal of demand deposits in domestic and foreign currency respectively; and a 5 and 3 percent per day withdrawal of time deposits in domestic and foreign currency respectively.

Annex I. External Sector Assessment

The external position of Honduras was broadly in line with fundamentals and desirable policy settings in 2017. Staff used various approaches to assess the external balance and the exchange rate position. These include quantitative indicators, regression-based methods to estimate the distance of the current account (CA) balance from its equilibrium value, and debt-stabilizing conditions for net foreign assets.

1. The CA deficit narrowed to 1¾ percent of GDP in 2017 mostly due to temporary factors. The major one is remittances, which surged 12 percent in 2017 relative to stable annual average remittances growth since 2010 of about 6½ percent.[1] A slight improvement in the goods balance (½ percent of GDP) was entirely offset by a decline in the services account due to higher transportation costs linked to rising oil prices.



Sources: BCH and IMF staff calculations.

2. In 2017, the REER depreciated slightly and significantly less than in 2016. As headline inflation in 2017 continued to recover and reached 4¾ percent at the end of 2017, REER depreciation in 2017 slowed to ¾ percent (2¼ percent in 2016). Nominal depreciation in 2017 slowed as well to 3 percent (3¾ percent in 2016) as the stock of reserves increased due to external financing inflows and because some of Honduras' trading partners experienced larger exchange rate depreciations.

3. The financing structure of the CA and low external liabilities are mitigating factors. The CA continues to be largely financed by FDI inflows. While the net International Investment Position (IIP) is negative at more than 65 percent of GDP, FDI comprises more than 60 percent of total liabilities and is well diversified across countries. The external debt profile presents no significant sustainability concerns, with a stable external debt-to-GDP ratio and with a low share of short-term debt. International reserves increased by almost US$900 million in 2017, boosted by a US$700 million external bond issuance and stronger remittances inflows (see above). The resulting stock of reserves reached 5.3 months of non-maquila imports of goods and services at end-2017 and is within the adequacy range of Fund's composite reserve metric.[2]

[1] Surveys suggest that the 2017 boost in remittances represents precautionary savings sent by Hondurans fearing deportation.

[2] As of the end-2017 reserves reached 107 percent of the composite EM ARA metric for non-floating exchange rate regimes.

Summary of EBA-Lite Approaches ("+" = Overvaluation) \1						
	Actual CA cycl. adj.	Underlying CA	CA Norm cycl. adj.	CA gap	REER gap	REER gap (2016 A4)
CA model	-3.0		-4.7	1.7	-4.6	-1.1
REER model					-2.9	7.1
ES approach		-3.8	-2.7	-1.1	3.0	7.0
Overall assessment				0.0	0.0	
Source: Fund estimates						
1/ In percent (REER) or percent of GDP (CA)						

4. **The Fund's multilaterally consistent estimates suggest that Honduras's REER has gained competitiveness over last two years and was broadly in line with fundamentals and desirable policy settings in 2017.**

EBA Current Account Model	
CA-Actual	**-1.7%**
Cyclical Contributions (from model)	0.1%
additional temporary/statistical factors	1.3%
Cyclically adjusted CA	**-3.0%**
CA-Norm	**-4.6%**
additional adjustments to the norm	
Cyclically adjusted CA Norm	**-4.7%**
CA-Gap	1.7%
o/w Policy gap	1.5%
Elasticity	-0.36
REER Gap	-4.6%

- **The CA model in the EBA-lite assessment that includes a larger number of countries, estimates REER undervaluation of about 4½ percent.** Staff adjusted the 2017 CA outturn for cyclical factors to reflect the temporary nature of the remittances surge in 2017, which was driven by uncertainty related to U.S. immigration policy (higher CA deficit by about US$250 million, or 1¼ percent of GDP), leading to a cyclically adjusted CA in 2017 of -3.0 percent of GDP. In comparison, the EBA-lite model calculates a cyclically adjusted CA norm of -4.7 percent of GDP. This norm results from the effects of a small fiscal deficit, appropriate accumulation of reserves, and still favorable demographics offsetting lagging productivity growth and strong remittance inflows. The difference between the cyclically adjusted 2017 CA and the CA norm leads to a CA gap of 1.7 percent of GDP, consistent with REER undervaluation of 4.6 percent. Of the CA gap, 1.5 percent of GDP reflects a policy gap. This in turn mainly reflects Honduras's strong fiscal position during 2014-17, while the rest of the world has maintained more expansionary fiscal policy than desired.

- **The REER Index model in the EBA-lite assessment similarly shows about 3 percent undervaluation.** With the policy gap at zero, the REER norm was mainly pushed down by consistently lagging productivity growth and relatively high openness, which more than offset strong remittances and reserves accumulation in 2017.

- **The external sustainability (ES) approach, which seeks a CA that stabilizes the IIP as a share of GDP at its current level (-65 percent of GDP), finds overvaluation of 3 percent.** This result differs from the CA model because (i) the requirement that the IIP be stabilized results in a higher CA norm and (ii) in the ES approach the norm is compared to the medium-term CA (not the 2017 CA) and the CA is expected to widen to about 4 percent of GDP over the medium term, partially on the back of the oil price recovery.

5. Staff's bottom-line assessment is that Honduras's external position in 2017 was broadly in line with fundamentals and desirable policy settings. Given the quite negative IIP, staff does not consider it prudent for Honduras's CA norm to be significantly weaker than the level that stabilizes the IIP at its current level. Similarly, staff views the CA norm implied by the CA model to be risky from a financing perspective, given that FDI inflows have been slowing. Hence, staff considers the results of the ES approach as the most relevant. However, giving some modest weight also to the REER and CA models results in an overall assessment of the CA and REER gaps being near zero in 2017.

6. According to opinion-based assessments by other international institutions, the competitiveness of Honduras has remained broadly the same or worsened somewhat. The WEF Global Competitiveness Index, which is mostly based on a private sector executives' survey, remains low, somewhat below LAC average in most categories, and has worsened slightly over the last two years (from 4.0 to 3.9 on the scale from 1 (worst) to 7 (best). While the macroeconomic environment improved significantly under the IMF program (the survey score improved from 4.1 to 5.0, a level above LAC average), many other pillars worsened. Specifically, public institutions score deteriorated from 3.5 to 2.9, innovation and sophistication factors worsened from 3.8 to 3.3 as well as did higher education and training (from 3.8 to 3.6 and below LAC average) both consistent with sluggish productivity growth. Inefficient government bureaucracy, still high crime and corruption rates as well as tax rates and regulations continue to be cited as the most problematic factors for doing business. Honduras broadly maintained its 2016 score in 2018 Doing Business Survey by the World Bank. High cost of starting a business, getting electricity, paying taxes, weak contract enforcement, insolvency resolution and poor protection of minority investors persist as main concerns of the private sector according to the survey data.

Annex II. Risk Assessment Matrix[1]

Source of Risk	Relative Likelihood[2]	Impact if Realized	Policy Responses
1. Tighter global financial conditions.	**High**	**Medium/High**	
	Against the backdrop of monetary policy normalization and increasingly stretched valuations across assets classes, an abrupt change in global risk appetite (e.g. due to higher-than-expected inflation in the U.S. could lead to tighter global financial conditions (High). Tightening would strengthen the U.S. dollar and the Euro relative to other currencies (High).	A decline in capital flows to emerging markets could disrupt foreign credit lines and reduce banking sector liquidity (Medium). An appreciation of the Lempira in line with the dollar is likely to adversely impact competitiveness of the export sector (Medium). Higher interest rates will increase financing costs for the government which is gradually moving from concessional towards market financing (High).	Create fiscal and international reserves buffers. Pre-finance wherever is possible, particularly treasury obligations in FX. Monetary tightening and increase exchange rate flexibility.
2. Structurally weak growth in key advanced economies.	**Medium/High**	**High**	
	Low productivity growth (U.S., euro area, and Japan), high debt, and failure to fully address crisis legacies by undertaken structural reforms amidst persistent low inflation (euro area and Japan) could undermine medium-term growth in these countries (High). The U.S. could also experience some stagnation due to persistently low productivity. The impact of policy measures such as tax cuts is expected to be temporary (High).	Protracted period of weaker-than-expected growth in advanced economies would lower export demand and remittances, significantly weighing on activity and tax revenues (High).	Ease monetary policy, but ensure that inflation expectations remain anchored. Increase nominal exchange rate flexibility. Some fiscal stimulus could be considered through targeted expenditure measures.
3. Retreat from cross border integration	**Medium**	**High**	
	Fraying consensus about the benefits of globalization leads to protectionism and economic isolationism, resulting in reduced global and regional policy and regulatory collaboration with negative consequences for trade, capital and labor flows, sentiment, and growth. (Medium).	Likely to restrict remittances and investment flows. Appreciation of REER could impact competitiveness (High).	Increase exchange rate flexibility. Foster competitiveness through structural reforms particularly in labor market.
4. Further social unrest	**High**	**High**	
	Continuous social unrest with risk of violence. Weakening on the anti-corruption measures.	Investment, productivity and potential growth would be negatively impacted.	Introduce accountability frameworks Strengthen political consensus Build adequate buffers

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path discussed in this report (which is the scenario most likely to materialize in the view of the staff). The RAM reflects staff's views on the source of risks and overall level of concerns as of the time of discussions with the authorities. The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding this baseline.

[2] In case the baseline does not materialize.

Annex III. Financial Sector Stability Review Main Recommendations

Key Recommendations	Recommended Timeframe/Current Status
Bank Regulation and Supervision	
Complete the transition towards RBS, complete the implementation of the Risk Management Unit, and define a clear division of labor relative to the existing superintendencies, including responsibility for consolidated supervision.	Near Term/In progress
Complete the regulatory framework on market and liquidity risk	Near Term/In progress
Enhance the supervisory capacity building program	Medium Term/Completed
Intensify efforts to improve AML/CFT, considering the results of the mutual evaluation now underway	Near term/Completed
Provide effective legal protections to current and former supervisors at all levels	Near term/Completed
Develop a methodology for identifying systemically important banks and supervise these intensively	Near term/In progress
Provide the CNBS with the power to compel economic groups to provide information on cross-border activities	Near term/Completed
Require that the chair of the audit committee of a commercial bank be an independent board member	Near term/Completed
Build the capacity of CONSUCOOP to supervise cooperatives, paying special attention to large cooperatives	Near term/Completed
Introduce a capital requirement for operational risks	Medium term/Pending
Insurance Regulation and Supervision	
Restore resources to the Insurance Superintendency to allow it to complete its RBS program	Near term/In progress
Develop an insurance supervisory manual, including the methodology for RBS	Near term/Completed
Amend the Insurance Act to allow the CNBS rather than the BCH to license insurance companies and to devolve rule-making powers from the Congress to the CNBS	Medium term/Completed
Require firms to complete an Own Risk and Solvency Assessment (ORSA) to allow a forward-looking assessment of risk and capital needs	Near term/In progress
Develop a framework for assessing market conduct risks	Near term/In progress
Stress Testing	
Implement a fully-developed stress testing framework encompassing macro scenario building and satellite models to understand financial sector vulnerabilities to severe shocks	Near term/In progress
Coordinate BCH and CNBS work to ensure the smooth integration of macroeconomic and financial models	Near term/In progress

Annex IV. Implementation of the 2016 Article IV Key Recommendations

Recommendation	Implementation
Fiscal Policy	
• The government should maintain fiscal stability through the electoral cycle. The targeted medium-term reduction in public sector debt should be regarded as a minimum. Trust funds should operate under the budgetary framework.	• The authorities maintained fiscal discipline in 2017, with only a marginal increase in the deficit of the NFPS to ¾ percent of GDP still well below the FRL ceiling. No progress was made to bring trust funds under the budgetary framework.
• Tax exemptions should be streamlined to raise revenues for the implementation of the Social Protection Law. This should include, in addition to planned non-renewal upon expiration, active rationalization of other ineffective exemptions.	• There have been no revisions of existing exemptions, and new exemptions were introduced for the tourism and agricultural sectors.
• Efficiency of health and education spending should be enhanced, including the revision of the public sector compensation framework.	• The authorities are receiving technical assistance from the World Bank and the Fund for the design of civil service reform and performance-based budgeting, respectively.
Monetary and Foreign Exchange Policy	
• The BCH should avoid further easing in the near term, while remaining vigilant and ready to tighten if inflation or credit growth accelerate and there are signs of overheating.	• The authorities maintained the policy rate unchanged and sterilized the surge in inflows from sovereign bond issuance and strong remittances growth.
• Immediate priorities in transition toward inflation targeting are to develop domestic and foreign exchange interbank markets, while reforming the central bank law to give it a clear mandate to achieve price stability. New regulations are needed to establish an interbank FX rate market, and start relaxing the surrender requirements on foreign exchange earnings.	• The BCH implemented most of the recommendations in the 2016 technical assistance missions related to short-term liquidity management, and to a lesser extent structural liquidity and communications. The BCH began to reduce FX surrender requirements by (so far it reduced twice, 10 percent each time). The BCH took steps to prepare a new central bank law but submission to Congress was delayed to grant the new government ownership of the reform.
Financial Sector	
• While banks have ample liquidity and capital appears adequate, it is important to monitor closely credit concentration and the buildup of household debt. Steadfast implementation of higher capital requirements for foreign currency borrowing by unhedged borrowers will be critical to support the de-dollarization process. AML/CFT supervision needs to be stepped up.	• The CNBS is making progress toward implementation of risk-based supervision, enhancing AML/CFT, and better monitoring cross-border activities of banks, in line with recommendations of the FSSR. Higher capital requirements for unhedged FX borrowers contributed to the reduction in dollarization rates. The regulatory framework has been strengthened as part of the implementation of the Basel III standard.
Structural Reforms	
• Reforms in the energy sector are required to strengthen ENEE's finances and foster competition in the electricity market.	• The targeted 4 percent reduction in nontechnical losses was achieved during the first year of operations of the new losses recovery operator in 2017. However, tariff adjustments decided by the regulatory body were only partially implemented.

INTERNATIONAL MONETARY FUND

HONDURAS

May 15, 2018

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared by: The Western Hemisphere Department

CONTENTS

FUND RELATIONS

(As of February 28, 2018)

Membership Status: Joined: December 27, 1945

General Resources Account:	**SDR Million**	**% Quota**
Quota	249.8	100.00
Fund holdings of currency (Exchange Rate)	211.1	84.51
Reserve Tranche Position	38.7	15.49

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	123.85	100.00
Holdings	53.46	43.16

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-By	12/03/2014	12/02/2017	77.70	0.00
SCF	12/03/2014	12/02/2016	51.80	0.00
Stand-By	10/01/2010	3/31/2012	64.75	0.00

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

	Forthcoming				
	2018	2019	2020	2021	2022
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.43	0.58	0.58	0.58	0.58
Total	**0.43**	**0.58**	**0.58**	**0.58**	**0.8**

Implementation of Enhanced HIPC Initiative: Enhanced Framework

Commitment of HIPC Assistance	
Decision point date	June 30, 2000[1]
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

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

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)[2]	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

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable.

Exchange Rate Arrangement. Honduras' de jure exchange rate arrangement is crawling band since July 2011, when the Central Bank of Honduras (BCH) reactivated the crawling band arrangement that had been in operation until mid-2005. The de facto exchange arrangement is a crawling peg. The exchange rate of the lempira is determined by foreign exchange auctions of the 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 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 this setting, the lempira has followed a slow depreciating trend against the U.S. dollar.

The BCH calculates an official exchange rate (TCR) daily as the weighted average of the accepted bids submitted by participants in BCH's foreign exchange auction. The TCR is then used the next day for (i) sales of foreign exchange by authorized dealers to the BCH, (ii) purchases of

[2] 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.

foreign exchange by authorized dealers from their clients, (iii) sales and purchases of foreign exchange between public institutions and the BCH and (iv) interbank foreign exchange market.

Honduras has accepted the obligations under Article VIII, Section 2, 3, and 4 of the Articles of Agreement, and currently maintains two multiple currency practices subject to Fund approval under Article VIII, Section 3. The two multiple currency practices arise from the absence of a mechanism to prevent the potential deviation of more than two percent at any given time among effective exchange rates for spot exchange transactions: (i) between successful bids within the foreign exchange auction; and (ii) between the official exchange rate (TCR) of the day and the exchange rates at which foreign exchange is sold at the auction on that day.

Article IV Consultation. The last Article IV consultation with Honduras was concluded on October 22, 2016.

The latest safeguards assessment for the Banco Central de Honduras (BCH) was completed on April 13, 2015. The assessment concluded that the BCH Law continues to pose a significant risk to central bank autonomy and that the bank's Board and audit committee do not have any independent members, which undermines these bodies' oversight function. The assessment recommended amendments to the BCH Law to protect the bank from political interference, establish its financial autonomy, and strengthen its governance arrangements. These recommendations are yet to be implemented. In addition, the assessment noted that recurring operating losses since the 1990s have severely weakened the bank's financial position and a recapitalization plan has been initiated, with the BCH expected to achieve positive equity in 2021. The assessment also recommended that the BCH adopt International Financial Reporting Standards (IFRS). While the BCH Board approved a plan to adopt IFRS for FY 2018, the implementation is significantly delayed.

FSAP, FSSR 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. FSSR conducted on June 8-9 and July 11-22, 2016.

Technical Assistance. Honduras has received substantial technical assistance. The table below details assistance provided by department since January 2015.

Technical Assistance

Department	Purpose	Time of Delivery
LEG	Legal Framework for Bank Resolution	May 2016
MCM	FX Lending Prudential Requirements	Feb 2015
MCM	CAPTAC-DR: Strengthening Monetary Policy Framework	Feb 2015
MCM	Financial Supervision	March 2015
MCM	Strengthening Monetary Policy Operational Framework	May 2015
MCM	CAPTAC-DR: Risk Based Supervision Implementation	May, June 2015
MCM	Domestic consolidated supervision	June 2015
MCM	CAPTAC-DR: Strengthening and Expanding the Macroeconomic Model	August 2015
MCM	Operational risk supervision	August 2015
MCM	Modernizing the Foreign Exchange System	Sep 2015
MCM	CAPTAC-Strengthening Capacities for Financial Stabilities Analysis	Sept 2015
MCM	FSSR Scoping Mission	January 2016
MCM	Regional Macroprudential Policies, Central America Countries	January 2016
MCM	Macroprudential policies	January 2016
MCM	CAPTAC: Training on Macroeconomic Forecast Models	February 2016
MCM	Operational risk supervision	February 2016
MCM	CAPTAC: Forecast Efficiency of the Central Bank´s Semi-Structural Macroeconomic Model	March 2016
MCM	CAPTAC: Support capacity building projection and economic analysis	April 2016
MCM	Stress testing models for credit risk with data panel	April 2016
MCM	Risk-based supervision	April 2016
MCM	Financial Sector Stability Review (FSSR)	July 2016
MCM	Modernization of the Monetary Policy Framework: Scoping mission	July 2016
MCM	Liquidity risk regulation	August, November 2016
MCM	Strengthening of the credit, market and liquidity off-site supervision	September 2016
MCM	Modernization of the Monetary Policy Framework: Roadmap	September 2016
MCM	Enhancing the monetary policy operational framework and liquidity management	October 2016
MCM	Strengthening of the credit, market and liquidity off-site supervision	February 2017
MCM	Strengthening the stress testing framework for credit risk	March 2017
MCM	Monetary Policy Modernization: FPAS work plan	May 2017

Technical Assistance

Department	Purpose	Time of Delivery
MCM	Strengthening the Monetary and Exchange Rate Policies Operational Frameworks	June 2017
MCM	CAPTAC: Stress Test	February 2018
MCM	CAPTAC: Financial Supervision	July, August, September 2017, March 2018
FAD	Medium-term expenditure framework	March, July, November 2015
FAD	Treasury Single Account	July, October 2015
FAD	CAPTAC: Degree of maturity of government paper	July 2015
FAD	CAPTAC: Strengthen control of VAT credit	May, December 2015
FAD	Introducing PBB to MDAs	August 2015
FAD	CAPTAC: Strengthen Audit Procedures	September 2015
FAD	Ex-post Inspection	October 2015
FAD	Tax Administration	October, December 2015
FAD	CAPTAC: Medium-term Expenditure Framework	January 2016
FAD	Treasury Single Account	February, June, August, November 2016
FAD	Customs Administration	March, April, December 2016
FAD	Streamlining Tax Exemptions	March 2016
FAD	Tax Administration	April, May 2016
FAD	Strategic Change Management	April 2016
FAD	CAPTAC: Strengthen audit procedures	May, October 2016
FAD	Budget - Preparation	June 2016
FAD	Fiscal Risks	July 2017
FAD	Taxpayer Service Improvement	February, October 2017
FAD	Treasury Single Account	February 2017
FAD	CAPTAC: Strengthen control of VAT credit	March 2017
FAD	Budget - Preparation	March 2017
FAD	CAPTAC: Strengthen audit procedures	March, October 2017
FAD	Fiscal Risks	April 2017
FAD	CAPTAC: Customs Administration	April, October 2017
FAD	CAPTAC: Tax Administration	January, February 2018
FAD	CAPTAC: Fiscal Statistics	December 2017
FAD	CAPTAC: Public Finance Management	April 2018
STA	Balance of Payments and IIP	Feb 2015

Technical Assistance

Department	Purpose	Time of Delivery
STA	Topics of the Financial Account	March 2015
STA	CAPTAC: National Accounts-Statistics and Construction Data Sources	May 2015
STA	CAPTAC: Export and Import Price Index	May 2015
STA	Balance of Payments and IIP	July 2015
STA	External debt	July 2015
STA	CAPTAC: Consumer Price Index	September 2015
STA	CAPTAC: Balance of Payments	November 2015
STA	CAPTAC: Quarterly National Accounts	January 2016
STA	Balance of Payments and IIP	June-July 2016
STA	Basic STA surveys and directories	March 2016
STA	Enhanced General Data Dissemination System (e-GDDS)	March 2016
STA	National Accounts Source Data	March 2016
STA	National Accounts Statistics	April 2016
STA	Special Surveys of Agricultural Products	April 2016
STA	Financial Accounts – Cash Flow	April 2016
STA	Balance of Payments	June 2016
STA	CAPTAC: Non-observed Economy-Employment Matrix	July 2016
STA	CAPTAC: National Accounts Rebasing Process	July 2016
STA	CAPTAC: Improvements Quarterly Construction Survey-Revision of Sample Frames	March 2017
STA	CAPTAC: National Accounts Rebasing Project	June 2017
STA	CAPTAC: Non-observed Economy-Employment Matrix	August 2017
STA	CAPTAC: Balance of payments and IIP statistics	March 2018

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

(As of April 3, 2018)

A. Recent Projects and Objectives

1. On December 2014, the IDB approved its country strategy with Honduras for the period 2015-2018. It focused on the following areas: (i) fiscal consolidation; (ii) sustainability and competitiveness in the energy sector; (iii) road infrastructure for regional integration; (iv) social inclusion; and (v) sustainable development in the Central District.

2. As of April 3, 2018, the portfolio of approved sovereign-guaranteed loans under execution amounted to USD653.8 million, with an undisbursed balance of USD397.6 million.

3. The existing portfolio of the IDB group focuses on public and private projects. In the public sector, the portfolio focuses on: (i) social protection (24.45 percent); (ii) transportation (36.25 percent); (iii) energy (14.67 percent); (iv) fiscal administration (5.66 percent); (v) sustainable development (6.73 percent), education (9.18 percent) and gender (3.06 percent). In the private sector, IDB Investments's portfolio focuses on: financial institutions (92.3 percent), energy (4.3 percent) and industry (3.4 percent). In addition, the IDB has one project in execution through Multilateral Investment Fund – Loan, amounting USD1 million, to support the Competitiveness of Small, Forest Producers and Communities in Honduras.

4. The pipeline program for IDB sovereign-guaranteed approvals until April 3, 2018 includes seven operations in the public sector distributed as follow: (a) one operation for Citizen coexistence and neighborhood Program; (b) the National Power Transmission Program (c) Development of PPPs in Support of Sustainable Tourism; (d) two Programs to Support Social Protection and (e) a Decentralized Health Management Program, are expected to be approved before the end of the year.

IDB Sovereign Guaranteed Loan Portfolio in Honduras as of April 3, 2018
(In millions of U.S. Dollars)

Sector	Current Approved	Available Amount
Social protection	159.87	54.87
Transportation	237	153.39
Energy	95.93	68.98
Fiscal	37	19.46
Sustainable Development	44	24.25
Education	60	60
Gender	20	16.71
Total	**653.8**	**397.6**

IDB Non-Sovereign Guaranteed Loan Outstanding in Honduras as of March 30, 2018 (In millions of U.S. Dollars)		
Sector	**Current Approved**	**Available Amount**
Financial Markets	105.1	0
Energy	4.9	0
Industry	3.8	0
Competitiveness	1.0	1.0
Total	**114.8**	**1.0**

IDB Disbursement of Sovereign Guaranteed Loan Portfolio in Honduras 2010-17 (In millions of U.S. Dollars)	
Year	**Amount**
2010	162.8
2011	256.1
2012	206.8
2013	224.3
2014	302.0
2015	216.3
2016	135.2
2017	176.2

IDB Annual Net Flows with Sovereign Guarantee in Honduras 2010-17 (In millions of U.S. Dollars)								
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Repayments	25.3	24.3	17.1	12.0	12.7	19.5	25.4	35.8
Disbursement	162.8	256.1	206.8	224.3	302.0	216.3	135.2	176.2
Net Loan Flow	**137.5**	**231.7**	**189.7**	**212.2**	**289.3**	**196.8**	**109.9**	**132**
Subscriptions and Contributions	1.3	0.0	15.9	8.7	9.3	1.7	1.7	0
Net Capital Flow	**136.2**	**231.7**	**173.8**	**203.6**	**280.1**	**195.1**	**108.1**	**132**
Interest and Charges	10.2	12.7	16.5	22.1	26.1	32.7	42.3	43.8
Net Cash Flow	**125.9**	**219.1**	**157.2**	**181.5**	**254.0**	**162.4**	**65.8**	**88.2**

RELATIONS WITH THE WORLD BANK GROUP

(As of March 25, 2018)

1. A Country Partnership Framework (CPF) for 2016-2020 was endorsed by the Board on December 2015 using inputs from the Systematic Country Diagnostic (which was prepared in October 2015). The 2016-20 CPF seeks to support Honduras in its efforts to foster social inclusion, while bolstering conditions for growth and reducing vulnerabilities to enhance the country's resilience. The CPF is aligned with the priorities identified in the Honduras' Country Vision for 2038 (adopted in 2010). Strengthening institutions and enhancing governance are critical cross-cutting themes that will underpin the strategic pillars.

2. The combined World Bank Group active portfolio in Honduras (IDA, IFC, MIGA plus trust funds), equals US$1.02 billion. The IDA18 allocation is SDR243.4 million (US$340 million), which will be allocated within the next three years, with Government expressing interest towards projects in agricultural competitiveness, water and sanitation, social protection.

3. The active portfolio is made up of 5 projects, totaling US$193.95 million (US$163.95 million in IDA commitments, plus US$30 million from the Global Agriculture and Food Security Program - GAFSP), of which approximately US$67 million are undisbursed. Project disbursements (excluding budget support) dropped from US$70.1 million in FY14 to US$40.7 million in FY15 and stabilized around US$30 million in FY16-FY17, consistent with Government's fiscal consolidation objectives.

4. The World Bank's current activities are supporting Honduras efforts to strengthen social protection, enhance rural competitiveness and citizen security, and improve disaster risk management. Please see details under sections A and B.

5. In line with its regional strategy, IFC's investment activities focus on renewable energy generation, strengthening and broadening the financial sector, and supporting competitive agribusiness and commercial sectors. Furthermore, IFC has played a catalytic role in PPP development, improving access to finance for SMEs, streamlining administrative processes for business regulation and regional trade, and facilitation of international trade. IFC's current portfolio stands at US$505.5 million, mostly in financial sector, infrastructure, and commercial real estate.

6. MIGA has US$327.01 million in gross exposure through three projects in the transport and energy sectors. MIGA has provided guarantees of US$187.9 million for the construction and operation of a toll road which will improve the connectivity between Honduras' second largest city and the coast. In energy sector, MIGA granted US$82.4 million in guarantees for a 24MW expansion of the existing 102MW Cerro de Hula wind farm, and an investment of US$56.7 million in guarantees in three photovoltaic projects supporting 80 MW solar power.

A. Projects

7. The active IDA portfolio is made of 5 projects totaling US$193.95 million (US$163.95 million in IDA funding and US$30 million from the GAFSP), of which approximately US$67 million is undisbursed.

8. **Honduras Rural Competitive Project.** The Project Development Objective (PDO) is to contribute to increased productivity and competitiveness among organized rural small-scale producers through their participation in productive alliances. Responding to Government's request, an Additional Financing of US$25.0 million was approved by the Board to expand the model to other areas and to incorporate new clusters. The closing date of this Project is November 30, 2020.

9. **Corredor Seco Food Security Project.** The PDO of the Project is to enhance food and nutritional security of vulnerable households in Selected Areas of the Corredor Seco. Project will increase household availability of quality food and revenues of poor and extremely poor rural residents in 25 municipalities as a basis for improving nutrition and in the long-term for reducing child stunting. Project will also improve nutrition and nutritional practices especially for children and women in selected municipalities. Project is implemented with US$30 million of GAFSP (trust fund) resources.

10. **Social Protection**. The PDOs of this Project are 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 9 among Program beneficiaries in rural areas; and (d) improve the Recipient's capacity to respond promptly and effectively to an Eligible Emergency. The closing date of this Project is December 31, 2018.

11. **Safer Municipalities**. The PDO of this Project are to 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. The closing date of this Project is August 31, 2018.

12. **Disaster Risk Management**. The PDO of this Project are to 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. The closing date of this Project is April 30, 2019.

Recently Closed Projects:

13. **Honduras Water and Sanitation Sector Modernization Project (PROMOSAS), closed December 2016.** The PDO of PROMOSAS was 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.

14. Second Land Administration, closed January 2017. The PDO of the Project was to provide improved, decentralized land administration services, including better access to and more accurate information on property records and transactions.

15. First Fiscal Sustainability and Enhanced Competitiveness DPF, closed March 2017, to support the Government's efforts in (i) strengthening institutional arrangements to support fiscal sustainability; and (ii) enhancing the regulatory framework to promote competitiveness.

B. Non-Lending Activities

16. Economic and Sector Work. Honduras benefits from a comprehensive series of completed, ongoing and planned analytical and advisory activities to support the CPF pillars. Recently completed economic and sector work includes: "Honduras - Unlocking Economic Potential for Greater Opportunities : Systematic Country Diagnostic" (2015), "Honduras Economic Diagnostic for National Action (DNA)" (2015); a Guidance for Enhanced Regulatory Capacity for Improved Governance in Extractive Industries (2016); a regional study on the Fiscal and Welfare Impacts of Electricity Subsidies in Central America (2017); a "Technical and Economic Analysis of the Penetration of Wind and Solar Energy in the Honduran Electricity Grid" (2017). The current ongoing analytical and advisory services include: support to the development of the Education Sector Plan, Jobs Diagnostic; the regional study Women in Central America: An Overview of Progress and Challenges and a study on the migration and remittances. The Bank is also providing technical assistance in the area of public finances, contingent liabilities, energy sector reform as well as transparency and accountability through the Global Partnership for Social Accountability grant provided by the USAID.

C. Financial Relations

Project	Loan	Original Amount (USD Eq)	Percent Disbursed	Approval Date	Sign Date	Closing Date	Undisbursed Balance (USD Eq)	Disbursed Outstanding Balance (USD Eq)
Disaster Risk Management Project	IDA 51900	30,000,000.00	51.32%	13-Dec-12	18-Dec-12	30-Apr-19	11,980,445.98	12,628,605.71
HN Safer Municipalities	IDA 51920	15,000,000.00	77.26%	13-Dec-12	18-Dec-12	31-Aug-18	2,700,920.58	9,176,562.48
Social Protection	IDA 56030	25,000,000.00	86.04%	31-Mar-15	19-May-15	31-Dec-18	3,488,840.83	21,511,159.17
Social Protection	IDA 52940	12,300,000.00	99.76%	8-Aug-13	26-Aug-13	30-Jun-18	28,160.79	11,899,723.21
Social Protection	IDA 47740	40,000,000.00	99.97%	29-Jun-10	2-Aug-10	30-Jun-18	10,679.33	38,536,750.67
Honduras Rural Competitiveness Project	IDA 44650	30,000,000.00	98.83%	17-Jun-08	17-Sep-08	31-Dec-18	239,190.88	20,125,489.12
Honduras Rural Competitiveness Project	IDA 60460	25,000,000.00	0.00%	18-May-17		30-Nov-20	25,000,000.00	0.00
PROSASUR – Corredor Seco Food Security Project	TF 17904	30,000,000.00	20.80%	24-Sept-15	11-Nov-15	30-Oct-21	23,761,042.82	6,238,957.18

Period	Disb. Amt.	Repay Amt.	Net Amt.	Charges	Fees
Jul 2006 - Jun 2007	41,624,795.86	0.00	41,624,795.86	2,424,638.03	596,191.13
Jul 2007 - Jun 2008	62,219,851.37	0.00	62,219,851.37	1,395,496.53	1,810,261.38
Jul 2008 - Jun 2009	49,391,574.72	0.00	49,391,574.72	0.00	3,313,284.34
Jul 2009 - Jun 2010	31,696,088.07	0.00	31,696,088.07	0.00	3,643,503.66
Jul 2010 - Jun 2011	118,584,340.26	1,105,404.96	117,478,935.30	0.00	4,103,991.95
Jul 2011 - Jun 2012	147,730,043.84	2,635,298.73	145,094,745.11	0.00	4,855,712.31
Jul 2012 - Jun 2013	87,062,015.07	3,202,199.84	83,859,815.23	1,186,246.38	5,943,753.48
Jul 2013 - Jun 2014	68,112,870.03	4,390,624.09	63,722,245.94	1,098,579.63	6,554,020.70
Jul 2014 - Jun 2015	91,206,208.19	7,633,158.67	83,573,049.52	1,165,256.68	6,484,201.02
Jul 2015 - Jun 2016	76,539,217.77	21,332,670.75	55,206,547.02	2,166,183.33	6,653,254.21
Jul 2016 – Jun 2017	28,378,659.17	24,761,314.50	3,617,344.67	3,035,493.00	7,912,871.45
Jul 2017 – Feb 2018	11,525,663,05	17,289,263.89	-5,763,600.84	2,927,110.05	5,521,288.30
Total	**815,579,511.20**	**84,959,105.33**	**730,620,405.87**	**15,399,003.63**	**58,144,078.82**

STATISTICAL ISSUES

(As of March 27, 2018)

I. Assessment of Data Adequacy for Surveillance
General: Data provided to the Fund are broadly adequate for surveillance and program monitoring purposes. However, monitoring will benefit from both better timing of data release and more comprehensive data coverage. Some issues that were flagged in the previous Article IV have not been fully addressed, including the lack of comprehensive data on the financial operations of public enterprises, enhancing reporting of government guarantees and fiscal contingent liabilities, and a valid and reliable methodology to estimate private capital flows.
National Accounts: The Central Bank of Honduras (BCH) compiles national accounts estimates following the *System of National Accounts 1993* (*1993 SNA*). The base year is 2000. The quarterly GDP data are consistent with the annual series. The BCH has developed a project to rebase the national accounts series to 2016, including the adoption of the main recommendations of the *2008 SNA*, with support of CAPTAC-DR, planned to be concluded by 2021. **Labor statistics:** Estimates of average wages and unit labor costs will help assess competitiveness and conducting a comprehensive household survey will help evaluate labor market conditions.
Price Statistics: The BCH prepares and publishes (since April 2000) the consumer price index (CPI), with reference period of December 1999. The selection of products included in the CPI basket and corresponding weights are based on the National Household Income and Expenditure Survey (NHIES) of 1998–99. A new NHIES for 2019 is being planned. The BCH expanded the coverage of the producer price index and updated its base (to 2010) and classification, in the context of the last revision of the national accounts (base year 2000). The index, currently compiled for internal use, only includes goods for processing activities (maquila), trade and transport margins, which limits its 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 sector. 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. Currently, the SEFIN and the BCH are participating in the GFS data enhancement project for Central America, Panama, and Dominican Republic. Under this project, country participants will elaborate and publish comparable GFS across countries to support decision making, permit a comparative analysis of fiscal developments and facilitate the regional policy dialogue. The components of the projects are: (i) compilation and dissemination of high quality sub-annual and annual data using the GFSM 2014 framework, and (ii) work towards the gradual implementation of the *Government Finance Statistics Manual 2014 (GFSM 2014)* and the *Public Sector Debt Statistics Guide (PSDSG)*. A mechanism is needed to systematically collect data on arrears and floating debt of public enterprises.

Monetary and Financial Statistics: Monetary and financial statistics (MFS) are reported to STA on a regular monthly basis using the standardized report forms (SRFs) for the central bank, other depository corporations, and other financial corporations (OFCs). However, pension funds are excluded from the coverage of OFCs. The inclusion of pension funds, and cross-sectoral data consistency between MFS and other data sets are the major issues that should be addressed.	
Financial sector surveillance: The authorities report 11 out of 12 core financial soundness indicators and five of the encouraged set.	
External sector statistics: Honduras has achieved significant milestones in the context of the CAPTAC-DR's Regional Harmonization Project of External Sector Statistics (ESS), which ended in December 2015. The BCH disseminates quarterly Balance of Payments and International Investment Position (IIP) statistics, and monthly the Data Template on International Reserves and Foreign Currency Liquidity. Honduras also participates in the Coordinated Direct Investment Survey (CDIS) and the Coordinated Portfolio Investment Survey (CPIS). Work in progress at the BCH aims at improving the coverage of nonfinancial private sector transactions and positions included in balance of payments and IIP statistics, ensuring consistency between external debt statistics and IIP statistics, and completing the migration to a BPM6 basis of recording and dissemination of ESS.	
II. Data Standards and Quality	
Honduras is an e-GDDS participant. In June 2016, it implemented the e-GDDS recommendations—including the launch of a National Summary Data Page to serve as a one-stop portal for essential macroeconomic and financial data. We encourage the authorities to take steps toward SDDS subscription.	Data ROSC was published on July 29, 2005.

Table of Common Indicators Required for Surveillance
(As of April 23, 2018)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]	Memo Items:[8] Data Quality – Methodological soundness[9]	Memo Items:[8] Data Quality – Accuracy and reliability[10]
Exchange Rates	23/04/18	23/04/18	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	19/04/18	23/04/18	D	D	D		
Reserve/Base Money	28/02/18	09/03/18	D	M	D		
Broad Money	28/02/18	09/03/18	M	M	M		
Central Bank Balance Sheet	31/03/18	13/04/18	D	M	D		
Consolidated Balance Sheet of the Banking System	31/01/18	30/03/18	M	M	M		
Interest Rates[2]	28/02/18	09/03/18	W	M	M		
Consumer Price Index	31/03/18	6/04/18	M	M	M		
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	31/12/17	30/03/18	Q	Q	Q		
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	31/12/17	30/03/18	Q	Q	Q		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	31/12/17	30/03/18	Q	Q	Q		
External Current Account Balance	31/12/17	09/03/18	Q	Q	Q		
Exports and Imports of Goods and Services	31/12/17	09/03/18	Q	Q	Q		
GDP/GNP	31/12/17	09/03/18	Q	Q	Q		
Gross External Debt	30/01/18	30/03/18	M	M	M		
International Investment Position[6]	31/12/17	09/03/18	Q	Q	Q		

[1] Any reserve assets that are pledged or 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.

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

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

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

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[8] These columns should only be included for countries for which Data ROSC (or a Substantive Update) has been published.

[9] This reflects the assessment provided in the data ROSC or the Substantive Update (published on ..., and based on the findings of the mission that took place during...) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

[10] Same as footnote 7, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

INTERNATIONAL MONETARY FUND

HONDURAS

May 17, 2018

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION— DEBT SUSTAINABILITY ANALYSIS

Approved by:
Ana Corbacho (IMF) and Paloma Anos (IDA)

Prepared by staffs of the International Monetary Fund and the International Development Association

Risk of external debt distress:	Moderate
Augmented by significant risks stemming from domestic public and/or private external debt?	No

The debt sustainability analysis (DSA) shows some improvement relative to the previous review mainly due to better-than-expected outcomes in year 2017 and the revised profile of PPP operations.[1] Staff still assess the risk of debt distress as moderate.

[1] See *Annex II* of Honduras: Fifth and Sixth Reviews Under the Stand-By Arrangement-Press Release; Staff Report; and Statement by the Executive Director for Honduras (IMF Country Report No. 17/331).

BACKGROUND

1. **Honduras' public debt increased slightly in 2017**. After satisfactory completion of the IMF-supported program (December 2017), gross public debt stood at 40¾ percent of GDP in 2017, an increase of about ¼ percentage *point of GDP relative to 2016*.[2] In 2017, the NFPS posted a deficit of ¾ percent of GDP, and the sovereign placed international bonds for US$700 million at a historically low rate of 6¼ percent.

2. **External debt increased in 2017**. The increase in 2 percentage points of GDP (from 35½ percent of GDP in 2016 to 37½ percent of GDP in 2017) reflected the above-mentioned bond placement. The procedures from the placement were used to pay liabilities from the public electricity company ENEE. Consequently, the actual change in the stock of total external debt is larger than the implicit variation derived from identified debt-creating flows in the LIC-DSA template, thus causing a large residual in 2017. Total external debt figures are consistent with the standard BOP coverage including public banks and the monetary authority.

3. **Public debt is mostly with foreign creditors.** The share of public debt that is external rose from 72 percent in 2016 to about 77 percent in 2017 due mainly to the above-mentioned external bond issuance. The main external lenders to Honduras are the Inter-American Development Bank (IADB), the Central American Bank for Economic Integration (BCIE), and the World Bank. Debt to these institutions carries long maturities but only the IADB continues to provide loans on concessional terms (i.e., with a grant element of at least 35 percent). Domestic public debt is mainly with commercial banks, has a shorter—though rising—maturity (about 3 years), and carries a higher real interest rate. In March-2018, the authorities placed their first 15-year Lempira-denominated bond in the local market at a fixed interest rate of 11 percent.

UNDERLYING ASSUMPTIONS

4. **Economic growth.** The baseline scenario assumes that growth will decelerate to 3¾ percent in 2018, owing to less favorable conditions abroad and uncertainty affecting private consumption and investment. Private consumption and public investment will be the main drivers of growth. Over the medium term, it is expected that growth will converge towards potential (3¾ percent), a similar outlook as envisaged in the previous DSA

5. **Fiscal policy.** As in the previous DSA and consistent with the fiscal responsibility law (FRL) we expect the fiscal outlook continued to be anchored by the FRL, which sets a NFPS deficit ceiling of 1 percent of GDP from 2019 onwards and a limit of about 3 percent in the real increase for current spending. Additionally, the DSA is aligned with the authorities' priority to control the increase in public debt stated in their revised macroeconomic framework. In the baseline scenario,

[2] The NFPS public debt stock presented in this annex includes outstanding liabilities from the security trust fund (around ¼ percent of GDP). Additionally, the authorities adopted the IPSAS-32 standard for reporting PPP operations in the fiscal accounts; therefore, the net stock of liabilities stemming from PPPs is included as public debt stock (estimated at 1½ percent of GDP at end-2017).

the primary balance becomes consistently positive backed by fiscal reforms undertaken in 2013-2017. As part of these reforms, the gatekeeper role of the minister of finance has been strengthened with the requirement of a formal assessment on the size of fiscal liabilities (including contingencies) by the newly created contingency unit for all PPP operations. Thus far this new unit has resulted in a better prioritization of PPP projects. The baseline projection assumes that starting in 2021, the net flows from PPPs would be negative.

6. **Fiscal institutions.** Consolidating the role of the FRL as the cornerstone of macroeconomic policies continues to be the main challenge for the next years. On this front, the experience in Latin America with the adoption of a FRL is mixed. In some countries, a FRL failed to institutionalize fiscal prudence while in others it served to catalyze fiscal reforms and became the backbone of sound policy making. The implementation of the FRL in Honduras requires developing institutions, strengthening commitment, and fostering transparency and accountability across all levels of government. This process is off to a good start but it needs to be entrenched as a binding medium-term target.

7. **Public sector financing.** It is assumed that public financing will be contracted mainly from external sources. Financing conditions are expected to change toward less concessional terms compared to recent years, including with multilateral institutions and in line with Honduras increasing ability to tap international markets. Authorities have been targeting increased Lempiras-denominated debt issuance, with a longer maturity profile. Domestically, authorities target a minimum of 80 percent of the public debt portfolio be issued at fixed rates.

8. **External sector.** On the back of large remittances inflows, favorable terms of trade, and a recovery in coffee production, the current account deficit declined to 1¾ percent of GDP in 2017, its lowest level since 2001. The current account deficit is projected to hover around 4 percent over the medium term, and stabilize at around 3½ percent of GDP over the longer term. Slower growth in remittances, coupled with less favorable terms of trade, explain the move toward higher deficits, which is in line with fundamentals and desired policy settings (see Annex I). As in the previous DSA, the current account deficit continues to be financed primarily by foreign direct investment and, to a lesser extent, public sector borrowing, with small private sector flows. This outcome allows for international reserves to remain around 5 months of non-*maquila* imports throughout the projection period.

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

9. **Public and public guaranteed (PPG) of external debt is expected to start decreasing in the medium term** (Annex II. Table 1). PPG external debt is projected to peak at about 33 percent of GDP in 2022, from about 31 percent of GDP in 2017. The share of PPG external debt in total public debt rises slowly to about 82 percent by 2022. The increase takes place as total debt decreases substantially due to fiscal consolidation. Private external debt is projected to be around 4 percent of GDP through the period.

Selected Macroeconomic Indicators, Current vs. Previous DSA

	2016	2017	2018	2019	Long term 1/
Real GDP growth (percent)					
Current DSA	3.8	4.8	3.7	3.7	3.8
Previous DSA	3.6	4.0	3.6	3.8	3.8
GDP deflator growth (percent)					
Current DSA	3.5	4.2	4.2	4.3	4.0
Previous DSA	3.7	5.9	3.8	4.0	4.4
Primary balance (% of GDP)					
Current DSA	-0.7	-0.4	0.2	0.5	0.7
Previous DSA	-0.3	-0.1	-0.2	0.4	0.5
Current account balance (% of GDP)					
Current DSA	-2.7	-1.7	-3.8	-3.9	-3.5
Previous DSA	-3.8	-4.1	-4.3	-4.0	-3.7
Net FDI (% of GDP)					
Current DSA	4.5	4.2	4.4	4.2	4.3
Previous DSA	4.5	5.7	6.1	6.0	6.4

Source: IMF staff estimates.

1/ Defined as the last 15 years of the projection period. For the current DSA, the long term covers the period 2024-38, whereas for the previous DSA it covered 2023-37.

10. External debt ratios remain within indicative thresholds in all scenarios.[3] The ratios for the PV of PPG external debt and PPG debt service remain below their indicative thresholds in all scenarios throughout the projection period. PV of external PPG remains initially stable and starts to decline in 2023.

11. In the baseline scenario, debt indicators remain within indicative thresholds under the probability approach. All ratios remain within indicative thresholds under the baseline scenario (Figure 2). Under the most extreme shock (one-time 30 percent depreciation), the ratio for the PV of debt-to-GDP plus remittances ratio breaches the threshold in 2020 and only returns to levels below the threshold in the late 2026. The ratio of debt service to revenue is breached only in 2020 under the most extreme shock (a one-time 30 percent depreciation), reflecting the bullet payments of the 2013 bond issuance.

12. External debt indicators appear resilient to a customized scenario combining negative real, fiscal and financing shocks. The customized scenario aims at capturing possible downside risks and key vulnerabilities in Honduras. It includes negative shocks to GDP growth, which could arise from weaker external conditions; tighter external financing conditions that could be associated with negative developments in international financial markets; and a weaker fiscal position from possible slippages in the implementation of the fiscal responsibility law. In this scenario, the PV of PPG external debt-to-GDP plus remittances ratio rises initially up to 24 percent and starts to decline

[3] Honduras has large remittances inflows — about 18 percent of GDP on average in 2015-2017. Therefore, the indicative external DSA thresholds reported are remittances-adjusted as per the DSA template.

in 2023. The ratio of debt service-to-exports plus remittances and debt service to revenue also remain below their indicative thresholds throughout the projection.

Baseline vs. Customized Scenario 1/

	2018	2019	2020	Long term 2/
Real GDP growth (percent)				
Baseline	3.7	3.7	3.7	3.8
Customized	2.6	2.5	2.8	3.5
Average interest rate on new external debt				
Baseline	3.4	3.4	3.4	3.4
Customized	4.4	4.4	4.4	4.4
Fiscal balance				
Baseline	-0.8	-0.8	-0.7	-0.7
Customized	-2.8	-2.5	-2.2	-1.9

Source: IMF staff estimates.

1/ In the customized scenario, (i) real GDP growth is 2.5 percent in 2018 and 2.8 in 2019, and rises on average 0.25 percentage points per year to reach 3.5 percent in 2022, staying at this level for the remainder of the DSA period; (ii) financing conditions from external capital markets deteriorate permanently, raising the average interest rate on new external debt by 100 basis points; and (iii) the overall deficit increases by 2 percent of GDP in 2018 compared to the baseline and then fades out partially at a constant rate of 15 percent during the DSA period.

2/ Defined as the last 15 years of the projection period. For the current DSA, 2024-38.

PUBLIC DEBT SUSTAINABILITY ANALYSIS

13. Public debt ratios are expected to peak in 2021 and then start to decline subsequently (Table 3). Public debt is projected to peak at about 41½ percent of GDP in 2021 (up from 40¾ percent of GDP in 2017) and start falling slowly as fiscal consolidation proceeds and interest payments decline reaching 30 percent of GDP by 2028. In present value terms, the debt-to-GDP ratio is expected to peak at around 36¼ percent of GDP in 2021 and fall to about 25 percent of GDP by the late 2020s. Public debt dynamics remain somewhat vulnerable to both policy-related and exogenous shocks, especially to those related to economic growth and fiscal policy (Annex II. Table 4). However, under no scenario the PV of debt-to-GDP ratio breaches its benchmark.

14. The exposure to contingent liabilities is limited. Several measures recently taken by the authorities limit the exposure of public debt to fiscal risks. For instance, by doubling the contribution rate for the social security institute (IHSS), the authorities' have improved the IHSS actuarial position; the PPP framework law was amended to limit the provision of government guarantees for PPP operations; and by upgrading PPPs accounting rules to international standards the impact of PPP's operations is included into the regular spending or financing recording. The 2017 bond issuance was used to clear most of ENEE's liabilities, leaving an estimated of 1¼ percent of GDP under dispute (classified as either pending or contingent).

CONCLUSION

15. Despite marked improvements on public and external debt indicators the risk of external debt distress remains moderate. Stronger than expected fiscal consolidation, and a reduced current account deficit strengthen the resilience of Honduras external position. The FRL passed in 2016, and its fulfillment, is the foundation for continued structural fiscal reforms over the coming years. Against this backdrop, further revenue mobilization efforts and actions to ensure the sustainability of state-owned enterprises will be essential to guarantee fiscal sustainability. On the monetary front, the reform of the monetary policy framework has shown some progress but much more work is needed.

Table 1. Honduras: External Debt Sustainability Framework, Baseline Scenario, 2015-38 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/	Standard 6/	Projections													
	2015	2016	2017	Average	Deviation	2018	2019	2020	2021	2022	2023	2018-2023 Average	2024	2025	2026	2027	2028	2038	2024-2038 Average
External debt (nominal) 1/	**36.1**	**35.5**	**37.6**			**36.8**	**36.8**	**36.8**	**37.1**	**37.1**	**34.9**		**32.8**	**30.9**	**29.3**	**27.9**	**25.7**	**17.3**	
of which: public and publicly guaranteed (PPG)	28.8	29.0	31.2			31.5	32.4	32.5	32.8	32.9	30.7		28.6	26.8	25.2	23.8	21.6	13.4	
Change in external debt	-1.0	-0.6	2.1			-0.8	0.0	0.1	0.2	0.1	-2.3		-2.1	-1.8	-1.6	-1.4	-2.3	0.3	
Identified net debt-creating flows	-2.0	-2.5	-4.8			-1.7	-1.6	-1.6	-1.7	-1.8	-1.8		-1.9	-1.9	-1.9	-1.9	-1.9	-2.0	
Non-interest current account deficit	**3.6**	**1.4**	**0.4**	**5.8**	**4.2**	**2.5**	**2.6**	**2.7**	**2.7**	**2.7**	**2.7**		**2.7**	**2.7**	**2.7**	**2.7**	**2.7**	**2.7**	2.7
Deficit in balance of goods and services	16.2	14.2	14.1			15.6	15.8	15.9	16.0	16.2	16.3		16.3	16.3	16.3	16.3	16.3	16.3	
Exports	45.0	42.5	43.5			42.6	42.9	43.5	43.6	43.8	43.8		43.8	43.8	43.8	43.8	43.8	43.8	
Imports	61.2	56.8	57.6			58.2	58.7	59.4	59.6	60.0	60.1		60.1	60.1	60.1	60.1	60.1	60.1	
Net current transfers (negative = inflow)	-18.3	-18.5	-19.6	-18.7	1.1	-19.2	-19.3	-19.3	-19.4	-19.6	-19.7		-19.7	-19.6	-19.6	-19.6	-19.6	-19.6	-19.6
of which: official	-0.4	-0.2	-0.8			-0.7	-0.7	-0.7	-0.7	-0.7	-0.7		-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	
Other current account flows (negative = net inflow)	5.7	5.7	5.8			6.1	6.1	6.1	6.1	6.1	6.1		6.1	6.1	6.1	6.1	6.1	6.1	
Net FDI (negative = inflow)	**-4.5**	**-4.2**	**-4.4**	**-5.2**	**1.2**	**-4.2**	**-4.2**	**-4.2**	**-4.3**	**-4.3**	**-4.3**		**-4.3**	**-4.4**	**-4.4**	**-4.4**	**-4.5**	**-4.6**	-4.5
Endogenous debt dynamics 2/	**-1.1**	**0.2**	**-0.7**			**-0.1**	**0.0**	**0.0**	**-0.1**	**-0.2**	**-0.2**		**-0.2**	**-0.2**	**-0.2**	**-0.2**	**-0.2**	**-0.1**	
Contribution from nominal interest rate	1.1	1.3	1.3			1.3	1.3	1.3	1.2	1.2	1.1		1.1	1.0	1.0	0.9	0.8	0.5	
Contribution from real GDP growth	-1.3	-1.3	-1.6			-1.3	-1.3	-1.3	-1.3	-1.4	-1.4		-1.3	-1.2	-1.1	-1.1	-1.0	-0.6	
Contribution from price and exchange rate changes	-0.8	0.2	-0.5			...	...	...	...	...	...		...	...	...	...	...	...	
Residual (3-4) 3/	**1.0**	**1.9**	**6.9**			**0.9**	**1.6**	**1.7**	**1.9**	**1.9**	**-0.4**		**-0.2**	**0.0**	**0.3**	**0.4**	**-0.3**	**2.3**	
of which: exceptional financing	-0.1	-0.1	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	
PV of external debt 4/	...	...	31.7			31.1	31.4	31.2	31.8	32.0	30.1		28.4	26.8	25.6	24.1	22.3	13.8	
In percent of exports	...	...	72.9			73.2	73.3	71.7	73.0	73.0	68.8		64.9	61.3	58.4	55.1	50.9	31.4	
PV of PPG external debt	**...**	**...**	**25.4**			**25.9**	**27.0**	**26.9**	**27.6**	**27.7**	**25.9**		**24.2**	**22.7**	**21.5**	**20.0**	**18.2**	**9.9**	
In percent of exports	**...**	**...**	**58.3**			**60.8**	**63.1**	**61.8**	**63.2**	**63.3**	**59.2**		**55.4**	**51.9**	**49.0**	**45.8**	**41.7**	**22.6**	
In percent of government revenues	**...**	**...**	**80.8**			**84.1**	**89.3**	**88.8**	**91.1**	**92.1**	**85.8**		**80.2**	**75.1**	**71.0**	**66.3**	**60.3**	**32.8**	
Debt service-to-exports ratio (in percent)	**20.5**	**30.7**	**15.7**			**16.2**	**14.5**	**17.3**	**12.3**	**13.6**	**13.3**		**13.1**	**13.4**	**11.3**	**16.1**	**11.1**	**9.7**	
PPG debt service-to-exports ratio (in percent)	**3.5**	**4.1**	**4.5**			**4.8**	**4.9**	**9.5**	**4.6**	**6.0**	**5.9**		**5.7**	**6.1**	**4.1**	**9.0**	**4.0**	**3.0**	
PPG debt service-to-revenue ratio (in percent)	**5.3**	**5.5**	**6.2**			**6.7**	**6.9**	**13.6**	**6.6**	**8.8**	**8.5**		**8.3**	**8.9**	**5.9**	**13.0**	**5.8**	**4.3**	
Total gross financing need (Billions of U.S. dollars)	2.1	2.6	0.9			1.6	1.4	1.8	1.2	1.4	1.5		1.5	1.6	1.4	2.2	1.5	2.0	
Non-interest current account deficit that stabilizes debt ratio	4.5	2.0	-1.7			3.3	2.6	2.6	2.5	2.6	5.0		4.8	4.5	4.3	4.2	5.0	2.5	
Key macroeconomic assumptions																			
Real GDP growth (in percent)	3.8	3.8	4.8	3.2	2.0	3.7	3.7	3.7	3.7	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8
GDP deflator in US dollar terms (change in percent)	2.3	-0.6	1.3	3.3	3.8	1.2	-0.7	-0.8	-0.3	0.2	0.7	0.1	1.2	1.5	1.5	1.5	1.5	1.5	1.4
Effective interest rate (percent) 5/	3.2	3.7	4.0	2.7	0.8	3.5	3.6	3.7	3.3	3.4	3.2	3.4	3.2	3.2	3.3	3.2	3.1	3.3	3.3
Growth of exports of G&S (US dollar terms, in percent)	1.2	-2.4	8.5	5.1	13.2	2.7	3.7	4.5	3.6	4.6	4.6	3.9	5.1	5.4	5.4	5.4	5.4	5.4	5.4
Growth of imports of G&S (US dollar terms, in percent)	0.8	-4.2	7.6	4.0	15.3	6.1	3.8	4.2	3.8	4.7	4.8	4.5	5.1	5.4	5.4	5.4	5.4	5.4	5.4
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	16.5	15.0	14.9	15.3	14.3	15.6	15.3	17.7	17.7	17.7	15.2	17.7	17.1	17.5
Government revenues (excluding grants, in percent of GDP)	30.1	31.6	31.4			30.8	30.3	30.3	30.3	30.1	30.2		30.2	30.2	30.2	30.2	30.2	30.2	30.2
Aid flows (in Billions of US dollars) 7/	0.3	0.3	0.3			0.2	0.2	0.2	0.2	0.2	0.2		0.2	0.2	0.2	0.3	0.2	0.4	
of which: Grants	0.2	0.2	0.1			0.2	0.2	0.2	0.2	0.2	0.2		0.2	0.2	0.2	0.2	0.2	0.4	
of which: Concessional loans	0.1	0.1	0.1			0.0	0.1	0.1	0.1	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			1.0	1.1	1.2	1.1	1.1	0.8		0.8	0.9	0.8	1.1	0.6	0.7	0.8
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			34.2	29.2	26.5	30.6	28.4	50.4		47.6	41.9	54.8	29.8	94.0	83.4	53.2
Memorandum items:																			
Nominal GDP (Billions of US dollars)	21.0	21.6	23.0			24.1	24.8	25.5	26.4	27.5	28.8		30.2	31.8	33.6	35.4	37.3	62.8	
Nominal dollar GDP growth	6.2	3.2	6.2			4.9	2.9	2.9	3.4	4.1	4.6	3.8	5.1	5.4	5.4	5.4	5.4	5.4	5.4
PV of PPG external debt (in Billions of US dollars)			5.8			6.1	6.6	6.7	7.1	7.5	7.3		7.2	7.1	7.1	7.0	6.7	6.2	
(PVt-PVt-1)/GDPt-1 (in percent)						1.2	1.9	0.6	1.7	1.4	-0.5	1.0	-0.4	-0.3	-0.1	-0.3	-0.8	-0.7	-0.2
Gross workers' remittances (Billions of US dollars)	3.7	3.8	4.3			4.5	4.6	4.8	5.0	5.2	5.5		5.7	6.0	6.4	6.7	7.1	11.9	
PV of PPG external debt (in percent of GDP + remittances)	...	...	21.4			21.8	22.8	22.6	23.2	23.3	21.8		20.4	19.1	18.0	16.8	15.3	8.3	
PV of PPG external debt (in percent of exports + remittances)	...	...	40.8			42.3	44.0	43.2	44.2	44.2	41.3		38.6	36.2	34.2	31.9	29.1	15.8	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	3.1			3.4	3.4	6.6	3.2	4.2	4.1		4.0	4.3	2.8	6.3	2.8	2.1	

Sources: Country authorities; and 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/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

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

8/ 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).

Table 2. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2018–38

(In percent)

	Projections							
	2018	2019	2020	2021	2022	2023	2028	2038
PV of debt-to-GDP+remittances ratio								
Baseline	22	23	23	23	23	22	**15**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2018-2038 1/	22	24	24	26	27	26	**26**	27
A2. New public sector loans on less favorable terms in 2017-2037 2/	22	23	23	24	25	24	**19**	13
A3. Customized 7/	21	23	24	25	26	25	**17**	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2019-2020	22	23	23	24	24	22	**16**	8
B2. Export value growth at historical average minus one standard deviation in 2019-2020 3/	22	25	32	32	33	31	**23**	11
B3. US dollar GDP deflator at historical average minus one standard deviation in 2019-2020	22	22	22	22	23	21	**15**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2019-2020 4/	22	24	25	25	26	24	**17**	9
B5. Combination of B1-B4 using one-half standard deviation shocks	22	24	26	27	27	25	**18**	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2019 5/	22	30	30	30	31	29	**20**	11
PV of debt-to-exports+remittances ratio								
Baseline	42	44	43	44	44	41	**29**	16
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2018-2038 1/	42	46	47	50	52	51	**50**	54
A2. New public sector loans on less favorable terms in 2017-2037 2/	42	44	45	47	48	45	**35**	25
A3. Customized 7/	50	54	55	57	59	56	39	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2019-2020	42	43	42	43	43	41	**28**	15
B2. Export value growth at historical average minus one standard deviation in 2019-2020 3/	42	53	71	72	72	69	**51**	24
B3. US dollar GDP deflator at historical average minus one standard deviation in 2019-2020	42	43	42	43	43	41	**28**	15
B4. Net non-debt creating flows at historical average minus one standard deviation in 2019-2020 4/	42	47	49	48	49	46	**33**	17
B5. Combination of B1-B4 using one-half standard deviation shocks	42	48	55	56	56	53	**38**	19
B6. One-time 30 percent nominal depreciation relative to the baseline in 2019 5/	42	43	42	43	43	41	**28**	15
PV of debt-to-revenue ratio								
Baseline	84	89	89	91	92	86	**60**	33
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2018-2038 1/	84	92	94	99	103	101	**97**	100
A2. New public sector loans on less favorable terms in 2017-2037 2/	84	89	92	96	99	94	**74**	53
A3. Customized 7/	82	77	79	83	85	81	57	14
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2019-2020	84	89	91	93	95	88	**62**	34
B2. Export value growth at historical average minus one standard deviation in 2019-2020 3/	84	100	124	127	129	122	**91**	43
B3. US dollar GDP deflator at historical average minus one standard deviation in 2019-2020	84	87	85	88	89	83	**58**	32
B4. Net non-debt creating flows at historical average minus one standard deviation in 2019-2020 4/	84	92	97	100	101	95	**68**	35
B5. Combination of B1-B4 using one-half standard deviation shocks	84	92	101	104	105	99	**72**	36
B6. One-time 30 percent nominal depreciation relative to the baseline in 2019 5/	84	125	124	128	129	121	**85**	46

Table 2. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2018–38 (concluded)

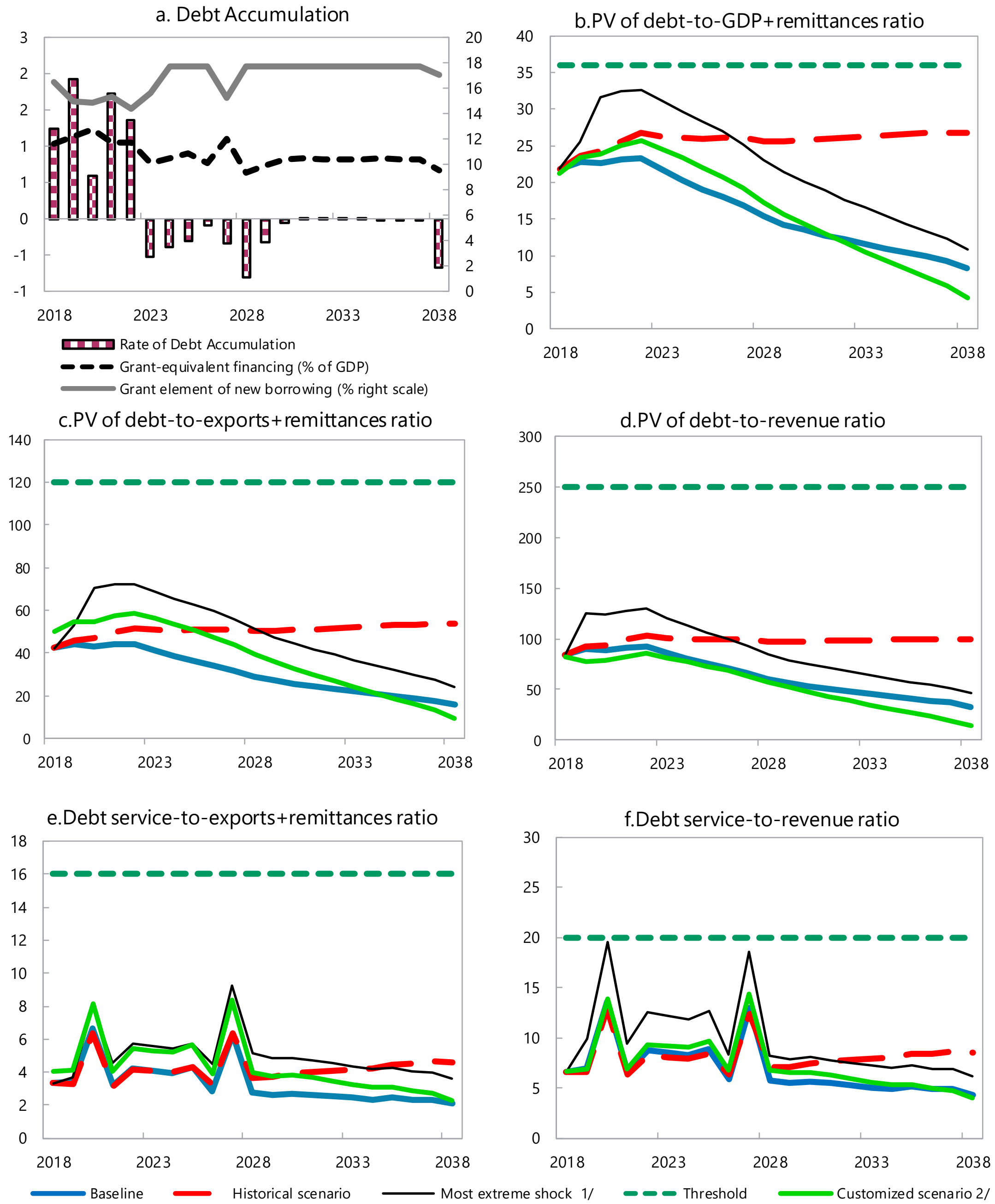
(In percent)

	Projections							
	2018	2019	2020	2021	2022	2023	2028	2038
Debt service-to-exports+remittances ratio								
Baseline	3	3	7	3	4	4	**3**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2018-2038 1/	3	3	6	3	4	4	**4**	5
A2. New public sector loans on less favorable terms in 2017-2037 2/	3	3	6	3	4	4	**4**	3
A3. Customized 7/	4	4	8	4	5	5	4	2
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2019-2020	3	3	7	3	4	4	**3**	2
B2. Export value growth at historical average minus one standard deviation in 2019-2020 3/	3	4	8	5	6	6	**5**	4
B3. US dollar GDP deflator at historical average minus one standard deviation in 2019-2020	3	3	7	3	4	4	**3**	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2019-2020 4/	3	4	7	3	4	4	**3**	2
B5. Combination of B1-B4 using one-half standard deviation shocks	3	4	7	4	5	5	**4**	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2019 5/	3	3	7	3	4	4	**3**	2
Debt service-to-revenue ratio								
Baseline	7	7	14	7	9	8	**6**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2018-2038 1/	7	7	13	6	8	8	**7**	9
A2. New public sector loans on less favorable terms in 2017-2037 2/	7	7	13	7	9	9	**7**	6
A3. Customized 7/	7	7	14	7	9	9	7	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2019-2020	7	7	14	7	9	9	**6**	4
B2. Export value growth at historical average minus one standard deviation in 2019-2020 3/	7	7	14	8	10	10	**9**	6
B3. US dollar GDP deflator at historical average minus one standard deviation in 2019-2020	7	7	13	7	9	8	**6**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2019-2020 4/	7	7	14	7	9	9	**7**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	7	7	14	7	9	9	**7**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2019 5/	7	10	20	9	13	12	**8**	6
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	15	15	15	15	15	15	**15**	15

Sources: Country authorities; and 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 2.6 percent in 2016 and 2.5 in 2017, and rises on average 0.25 percentage points per year to reach 3.5 percent in 2021, staying at this level for the remainder of the DSA period; (ii) financing conditions from external capital markets deteriorate permanently, raising the average interest rate on new external debt by 100 basis points; and (iii) the overall deficit of the CPS increases by 2 percent of GDP in 2015 compared to the baseline and then fades out partially at a constant rate of 15 percent during the DSA period.

Figure 1. Honduras: Indicators of Public and Publicly Guaranteed External Debt 1/

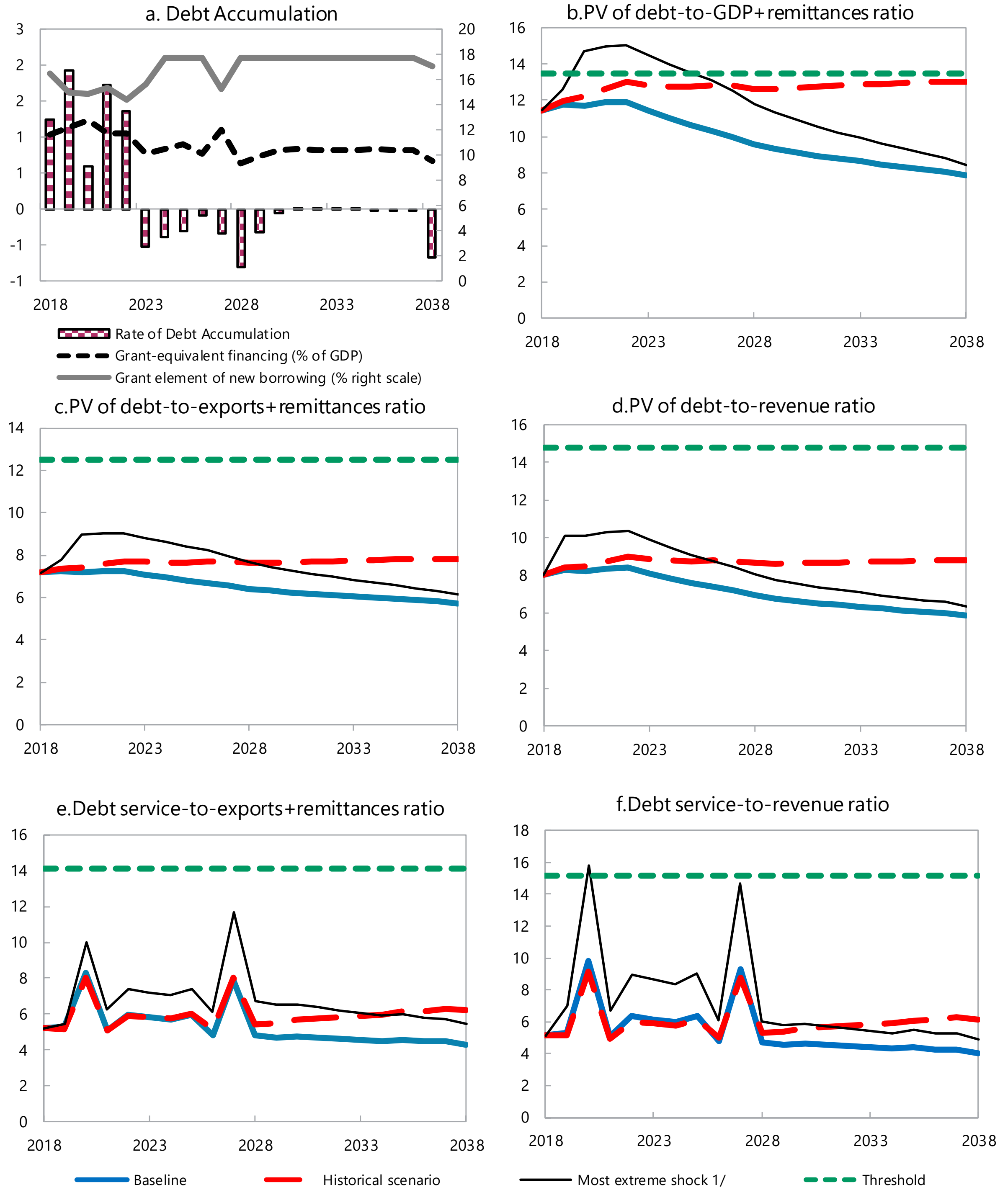


Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2028. In figure b. it corresponds to a Exports shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

2/ In the customized scenario, (i) real GDP growth is 2.5 percent in 2018 and 2.8 in 2019, and rises on average 0.25 percentage points per year to reach 3.5 percent in 2022, staying at this level for the remainder of the DSA period; (ii) financing conditions from external capital markets deteriorate permanently, raising the average interest rate on new external debt by 100 basis points; and (iii) the overall deficit of the CPS increases by 2 percent of GDP in 2018 compared to the baseline and then fades out partially at a constant rate of 15 percent during the DSA period.

Figure 2. Honduras: Probability of Debt Distress of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2018-38 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2028. In figure b. it corresponds to a Exports shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Table 3. Honduras: Public Sector Debt Sustainability Framework, Baseline Scenario, 2015-38

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate						Projections							
	2015	2016	2017	Average 5/	Standard Deviation 5/	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2018-23 Average	2028	2038	2024-38 Average
Public sector debt 1/	39.6	40.5	40.8			41.3	41.7	41.5	41.5	39.9	38.2	36.5	34.7	33.1	31.5		30.0	18.2	
of which: foreign-currency denominated	28.1	28.6	31.0			31.5	32.4	32.5	32.8	32.9	30.7	28.6	26.8	25.2	23.8		21.6	13.4	
Change in public sector debt	0.7	0.9	0.3			0.5	0.3	-0.1	0.0	-1.6	-1.7	-1.7	-1.7	-1.6	-1.6		-1.6	-1.0	
Identified debt-creating flows	0.6	2.5	-0.3			0.8	0.6	0.5	0.1	-0.1	-0.2	-0.3	-0.3	-0.3	-0.3		-0.3	-0.3	
Primary deficit 2/	0.5	0.7	0.4	3.1	2.2	-0.2	-0.5	-0.7	-0.6	-0.5	-0.6	-0.6	-0.7	-0.7	-0.7	-0.5	-0.7	-0.7	-0.7
Revenue and grants	29.8	30.5	30.5			29.9	29.5	29.5	29.6	29.5	29.7	29.7	29.8	29.8	29.9		29.9	30.4	
of which: grants	0.9	0.8	0.6			0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6		0.6	0.6	
Primary (noninterest) expenditure	30.3	31.2	30.9			29.7	29.0	28.9	29.0	29.0	29.1	29.2	29.1	29.1	29.2		29.2	29.7	
Automatic debt dynamics	-0.5	1.4	-0.9			0.9	1.1	1.2	0.7	0.4	0.4	0.3	0.4	0.5	0.5		0.4	0.5	
Contribution from interest rate/growth differential	-0.1	0.6	-0.3			0.1	0.2	0.2	0.1	0.0	0.1	0.2	0.3	0.3	0.3		0.3	0.4	
of which: contribution from average real interest rate	1.4	2.0	1.5			1.6	1.7	1.7	1.6	1.5	1.5	1.6	1.6	1.6	1.6		1.5	1.1	
of which: contribution from real GDP growth	-1.4	-1.4	-1.9			-1.5	-1.5	-1.5	-1.5	-1.5	-1.5	-1.4	-1.4	-1.3	-1.2		-1.2	-0.7	
Contribution from real exchange rate depreciation	-0.5	0.8	-0.6			0.8	0.9	0.9	0.6	0.5	0.3	0.1	0.1	0.1	0.1		...	...	
Other identified debt-creating flows	0.7	0.4	0.2			0.0	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)	0.7	0.4	0.2			0.0	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	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	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	0.0	0.0		0.0	0.0	
Residual, including asset changes	0.0	-1.6	0.6			-0.2	-0.2	-0.7	-0.1	-1.5	-1.5	-1.5	-1.4	-1.4	-1.3		-1.3	-0.8	
Other Sustainability Indicators																			
PV of public sector debt	...	...	35.0			35.7	36.3	35.9	36.3	34.8	33.5	32.1	30.6	29.3	27.7		26.6	14.7	
of which: foreign-currency denominated	...	...	25.2			25.9	27.0	26.9	27.6	27.7	25.9	24.2	22.7	21.5	20.0		18.2	9.9	
of which: external	...	...	25.4			25.9	27.0	26.9	27.6	27.7	25.9	24.2	22.7	21.5	20.0		18.2	9.9	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...	...	...	...	...		...	...	
Gross financing need 3/	3.7	3.1	6.9			3.4	3.8	5.9	3.9	4.1	4.2	4.3	4.5	3.6	5.8		3.8	2.5	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	114.6			119.3	122.9	121.4	122.7	117.8	112.7	108.1	102.9	98.3	92.8		88.8	48.3	
PV of public sector debt-to-revenue ratio (in percent)	...	...	117.0			121.9	125.7	124.1	125.3	120.2	115.1	110.4	105.1	100.5	94.8		90.7	49.4	
of which: external 4/	...	...	84.9			88.4	93.7	93.0	95.1	95.9	89.2	83.4	77.9	73.6	68.6		62.3	33.3	
Debt service-to-revenue and grants ratio (in percent) 5/	17.2	13.4	25.0			16.1	18.7	25.7	18.8	19.1	19.2	19.6	20.4	17.5	24.2		17.6	12.1	
Debt service-to-revenue ratio (in percent) 6/	17.7	13.7	25.5			16.4	19.1	26.3	19.2	19.5	19.6	20.0	20.9	17.8	24.7		18.0	12.4	
Primary deficit that stabilizes the debt-to-GDP ratio	-0.1	-0.2	0.1			-0.7	-0.9	-0.5	-0.6	1.1	1.1	1.2	1.0	0.9	0.9		0.9	0.3	
Key macroeconomic and fiscal assumptions																			
Real GDP growth (in percent)	3.8	3.8	4.8	3.2	2.0	3.7	3.7	3.7	3.7	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8
Average nominal interest rate on forex debt (in percent)	3.6	3.4	4.0	2.6	0.8	3.4	3.5	3.6	3.2	3.3	3.1	3.1	3.1	3.2	3.1	3.4	3.0	3.1	3.1
Average real interest rate on domestic debt (in percent)	6.6	12.8	8.1	7.2	4.0	11.8	13.5	14.4	14.1	12.9	17.1	17.1	17.1	17.0	17.0	14.0	16.9	16.5	16.8
Inflation rate (GDP deflator, in percent)	6.9	3.5	4.2	5.4	2.3	4.2	4.3	4.1	4.1	4.0	4.0	4.0	4.0	4.0	4.0	4.1	4.0	4.0	4.0
Growth of real primary spending (deflated by GDP deflator, in percent)	-5.7	6.9	3.9	0.6	3.2	-0.3	1.0	3.4	4.1	3.9	4.4	3.9	3.5	4.0	4.0	2.7	4.0	4.1	4.0
Grant element of new external borrowing (in percent)	...	...	...	...	...	16.5	15.0	14.9	15.3	14.3	15.6	17.7	17.7	17.7	15.2	15.3	17.7	17.1	17.5

Sources: Country authorities; and staff estimates and projections.
1/ Gross debt of the Combined Public Sector
2/ As defined in the fiscal accounts
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 4. Honduras: Sensitivity Analysis for Key Indicators of Public Debt 2018–38

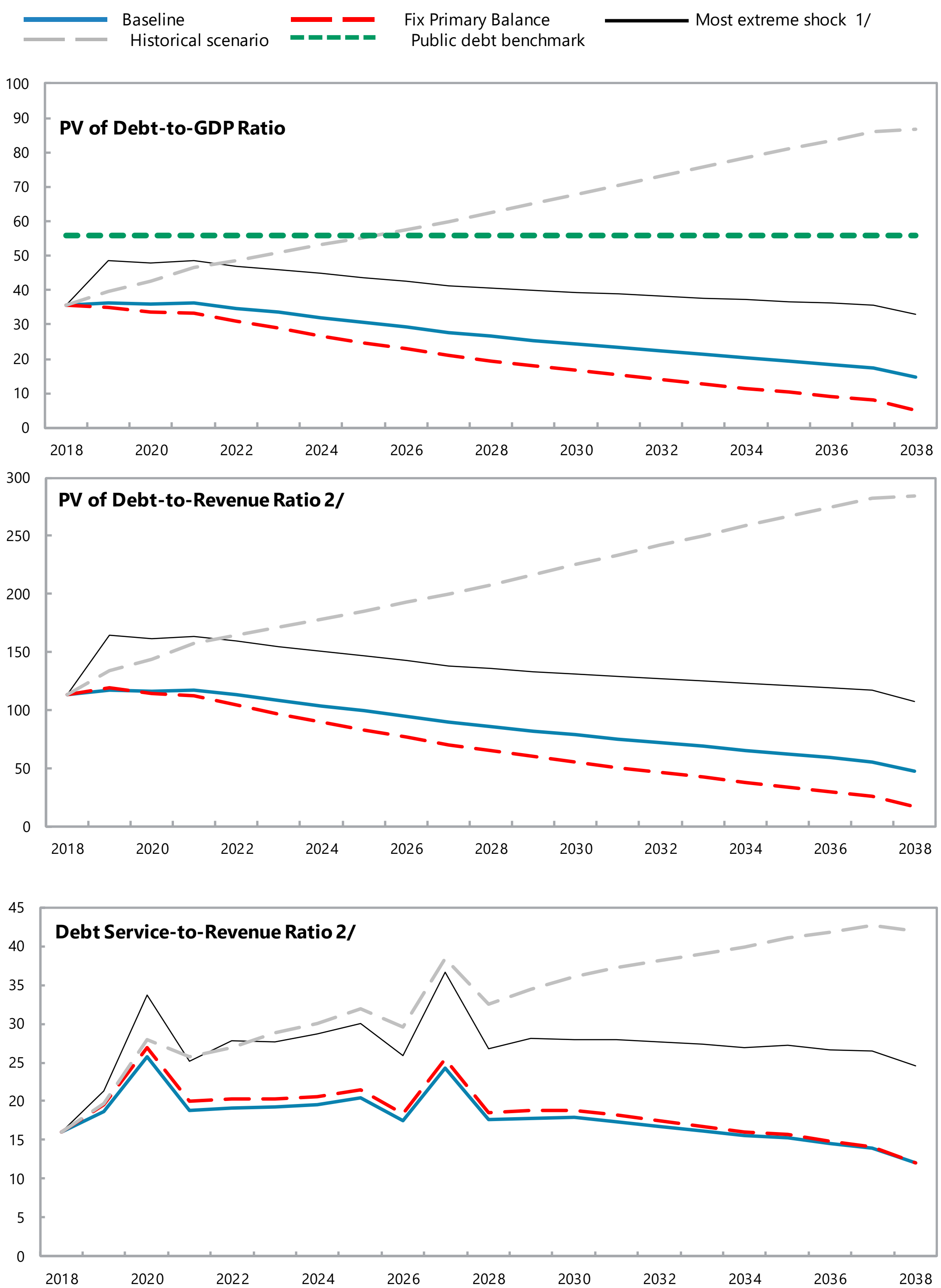
		Projections						
	2018	2019	2020	2021	2022	2023	2028	2038
PV of Debt-to-GDP Ratio								
Baseline	36	36	36	36	35	33	27	15
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	36	39	43	47	49	51	62	87
A2. Primary balance is unchanged from 2018	36	35	34	33	31	29	19	5
A3. Permanently lower GDP growth 1/	36	36	36	37	36	36	36	46
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2019-2020	36	38	39	41	41	41	41	44
B2. Primary balance is at historical average minus one standard deviations in 2019-2020	36	41	46	47	45	44	38	29
B3. Combination of B1-B2 using one half standard deviation shocks	36	41	45	47	46	45	43	40
B4. One-time 30 percent real depreciation in 2019	36	48	48	48	47	46	41	33
B5. 10 percent of GDP increase in other debt-creating flows in 2019	36	45	45	45	43	42	36	27
PV of Debt-to-Revenue Ratio 2/								
Baseline	114	117	116	118	113	108	86	48
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	114	134	144	157	164	171	208	285
A2. Primary balance is unchanged from 2018	114	119	114	113	105	97	65	17
A3. Permanently lower GDP growth 1/	114	123	123	126	123	121	119	150
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2019-2020	114	128	133	139	139	138	138	145
B2. Primary balance is at historical average minus one standard deviations in 2019-2020	114	140	157	157	152	147	126	94
B3. Combination of B1-B2 using one half standard deviation shocks	114	138	154	157	155	152	143	133
B4. One-time 30 percent real depreciation in 2019	114	164	162	164	159	155	136	108
B5. 10 percent of GDP increase in other debt-creating flows in 2019	114	152	151	152	147	142	121	90
Debt Service-to-Revenue Ratio 2/								
Baseline	16	19	26	19	19	19	18	12
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	16	20	28	26	27	29	33	42
A2. Primary balance is unchanged from 2018	16	20	27	20	20	20	19	12
A3. Permanently lower GDP growth 1/	16	20	27	22	22	23	24	27
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2019-2020	16	20	29	23	24	25	26	26
B2. Primary balance is at historical average minus one standard deviations in 2019-2020	16	20	28	28	28	25	24	21
B3. Combination of B1-B2 using one half standard deviation shocks	16	20	29	27	28	26	26	25
B4. One-time 30 percent real depreciation in 2019	16	21	34	25	28	28	27	25
B5. 10 percent of GDP increase in other debt-creating flows in 2019	16	20	29	31	23	26	24	20

Sources: Country authorities; and 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 3. Honduras: Indicators of Public Debt under Alternative Scenarios, 2018–38 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2028.
2/ Revenues are defined inclusive of grants.

Statement by Mr. Carlos Hurtado, Executive Director for Honduras
May 30, 2018

The Honduran authorities want to thank the IMF team for their well-informed policy advice as well as for a very constructive and candid dialogue.

In the last four years, supported by a Fund program, the Honduran authorities have made immense strides in stabilizing the economy and reducing criminality while at the same time fostering poverty reduction policies. It is important to remember where Honduras stood four years ago, with wide fiscal and external imbalances (non-financial public sector deficit of 7.5 percent of GDP and a current account deficit of 9.5 percent) and a very challenging security situation ranking as the country with the highest homicide rate in the world.

Now, economic fundamentals are strong with an economic growth rate in 2017 of 4.8 percent, the highest in a decade, non-financial public sector (NFPS) deficit of 0.8 percent of GDP, below the Fiscal Responsibility Law (FRL) ceiling of 1.5 percent of GDP and historically low for an election year. In the external sector, a combination of export growth and increased inflows of remittances narrowed the current account deficit to 1.7 percent of GDP and international reserves are equivalent to more than 5.3 months of non-maquila imports cover. Furthermore, a remarkable decline in violence was reached by more than 50 points with respect to 2013, a trend which has continued to date. The authorities' vast reform agenda and the resulting stabilization of the economy have helped boost investor confidence, which gave rise to the historic improvement of Honduras' international debt credit rating.

The government remains committed to safeguard the advances achieved and retain fiscal discipline while continue working at a gradual and timely pace, towards placing Honduras on a higher-potential growth path. To this end, our authorities will seek a new program with the Fund, cognizant of the valuable role the IMF has played and recognizing that there is still more to be done as well as challenges ahead due in part to the less- favorable external conditions.

For the next four years, the government is optimistic that it will achieve ambitious goals on economic growth, employment creation and poverty reduction. These goals will require progress on seven strategic priorities: boosting innovation, deepening financial inclusion, enhancing the country's role as Central America's logistics hub, improving education and health (including investing in bilingual English-Spanish public education), strengthening security, preserving macroeconomic stability, and reducing corruption. To make progress on these areas, and with the U.N. support, the government has initiated a national dialogue with all political parties.

Governance and Transparency

One of the first outcomes of the national dialogue is the creation of a new framework to enhance government transparency. The new framework includes the recent creation of the Inter-

Institutional Table for Transparency, comprised by the heads of the three branches of government – civil society, comptrollers and municipalities – which were installed recently, as well as electoral reforms including a new ID (last updated 20 years ago) with modern technology which will result in the added benefits of enhanced security and aid in doing business. Additionally, the government has reaffirmed its backing of the special anti-corruption[1] entity, created with the support of the Organization of American States (OAS), per the country's request in 2016. Through this alliance and as a key component towards achieving transparency, a special anticorruption unit within the public prosecutor's office was created in October 2017, backed by the MACCIH, which has generated the prosecution of high profile cases in 2018.

As highlighted in the staff's report, Honduras has greatly improved budget transparency since 2008, as evidenced in the survey-based Open Budget Index[2] which has improved from 12 in 2008 to 54 in 2017. Also, in the last four years, the country has improved the transparency indicator in the execution of public infrastructure from 74 percent in 2014, to 85 percent in 2017.

Moreover, a few days ago the SISOCS-APP – an integral framework for the disclosure of public-private partnership projects – was launched, Honduras thus becoming the first country in the world to implement a project of its kind. We also remain the only country in the world whose Government signed with Transparency International an agreement to work to improve transparency in a pilot project of five ministries of state. It is important to emphasize the valuable support of the Fund's technical assistance in these attainments.

To further enhance transparency, authorities have agreed to undergo a Fiscal Transparency Evaluation, led by FAD, which will assess the country's compliance with the basic requirements for fiscal risk disclosure under the new IMF Fiscal Transparency Code.

Monetary and Exchange Rate Policy

Throughout the duration of the program and in 2018, inflation remained within target reaching 4.2 percent in April 2018[3] (similar to the 4.1 percent of the year before). Based on assessment of external and domestic economic conditions, the central bank will stand ready to take the necessary measures to keep inflation within target.

According to the Central Bank of Honduras (BCH)'s strategic plan to modernize monetary policy and adopt an inflation-forecast targeting framework, approved in October 2016, new regulations for the interbank money market and FX market were approved in 2017, which have contributed to bolstering the monetary transmission mechanism and supporting de-dollarization.

---

[1] Misión de Apoyo Contra La Corrupción y Impunidad en Honduras (MACCIH).

[2] Measures the amount and timeliness of publicly available standard budget information.

[3] 4±1 percent tolerance range.

Furthermore, the monetary authority updated its organizational structure and strengthened its staffs' macroeconomic modeling capacity with the aid of technical assistance from the Fund.

In January 2018, an additional 10 percent of FX surrender requirements were decreased (for a total reduction of 20 percent) with the goal of creating a more dynamic FX market and, going forward, gradually increasing exchange rate flexibility to strengthen the country's capacity to absorb economic shocks. BCH is committed to making further advances in the planned transition to full inflation targeting, including the development of the secondary securities market, backed by the adoption of a new securities market law as well as enacting a central bank law with a clear mandate to control inflation. To accomplish these, they have requested a follow up TA to aid in the transition process.

Fiscal Policy

The Honduran government has pledged to maintain the NFPS deficit unchanged from last year (expenditures have been cut back to counteract the revision in the minimum income tax reform) and to sustain a prudent fiscal stance, with main spending priorities being in social spending, infrastructure and security. It is also committed to containing the wage bill. The authorities are receiving valuable technical assistance from the World Bank in civil service reform and from the Fund in performance-based budgeting, which will contribute to the above-mentioned goals.

The customs authority has achieved concrete progress in improving revenue collection and in generating efficiency throughout the customs clearance process. The advances achieved have contributed significantly to reduce costs for the private sector and to foster a positive investment environment. The transition to a fully independent and functioning customs authority is expected by August 2018.

Statistics

The current reference year for the Honduran National Accounts and Consumer Price Index (CPI) is based on the 1998-99 survey. Conscious of the importance of these in the economic and social policy decision process, as well as their significance in the transition to an inflation targeting regime, the authorities of the BCH and the National Institute of Statistics, signed recently in May 14, 2018 an inter-institutional technical cooperation agreement for the planning, formulation and execution of a new household survey. The new survey will consider the statistical and technical requirements necessary for updating the basket of goods and services and their weight for a new CPI database and will strengthen household estimates for the National Accounts. This project is planned to be finalized in the first quarter of 2021.

Energy Company (ENEE)

In the last four years, authorities reached significant progress in solidifying ENEE's financial position. The ongoing actions toward that end have included reductions in non-technical losses, a rightsizing program which attained a 60 percent reduction in the workforce, quarterly tariffs adjustments based on a cost-recovery formula, and the creation of a new Secretary of Energy to support the implementation of the electricity sector's reform.

Going forward, the authorities are committed to ensuring ENEE's financial sustainability by implementing a holistic plan and assessing a scope of wide-ranging actions including faster reduction in non-technical electricity losses as well as generating income through the charge for ancillary services to electricity generators.

Results of the Social Welfare Programs

Alleviating poverty has been and remains a key priority for the Honduran authorities. To that end, social spending was safeguarded and increased, even throughout the challenging fiscal consolidation process. Social spending has consisted mainly of social benefits such as conditional cash transfers. Results indicate that these programs have been effective in improving education, health and nutrition indicators, widely accepted as mechanisms to break the intergenerational transmission of poverty.

Structural Reforms

The country's medium-term development strives to attain inclusive export-led growth of the tourism, textiles, intermediate-goods, back office support, and agro-industrial sectors. The achievements in macroeconomic stability, crime reduction, coupled with ongoing efforts to enhance the country's internal and regional connectivity and ease of doing business will help the continued expansion of the tourism sector.

The afore-mentioned reduction of cargo backlog by the customs authority increased corporate sector profitability and will provide incentives for private sector investment. The customs union signed in June 2017 with Guatemala has enhanced trade, and the addition of El Salvador -later this year- will further boost growth in the region. Trade and tourism will also be enhanced by the construction of a bigger airport (projected to be finalized at the end of 2019).

Authorities have agreed to the publication of the Staff Report for the 2018 Article IV Consultation.