IMF Country Report No. 23/337

HONDURAS

September 2023

2023 ARTICLE IV CONSULTATION AND REQUESTS FOR AN ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR HONDURAS

In the context of the Article IV Consultation and Requests Under the Extended Arrangement Under the Extended Fund Facility and an Arrangements Under the Extended Credit Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 21, 2023, following discussions that ended on June 16, 2023, 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 September 5, 2023.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF and the World Bank.
- 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.

IMF Executive Board Approves US$822 Million Arrangements Under the Extended Fund Facility and the Extended Credit Facility for Honduras and Concludes 2023 Article IV Consultation

FOR IMMEDIATE RELEASE

- The Executive Board of the International Monetary Fund (IMF) approved arrangements under the Extended Fund Facility (EFF) and the Extended Credit Facility (ECF) for Honduras for a total of US$822 million.
- These arrangements provide support for the Honduran government's economic and institutional reform agenda over the next three years. The program also aims to support the authorities' efforts to improve governance and transparency and fight corruption.
- The program will advance policies needed to strengthen economic resilience and address structural bottlenecks to boost inclusive growth, including by increasing public investment while safeguarding macroeconomic stability.

Washington, DC – **September 21, 2023:** The Executive Board of the International Monetary Fund (IMF) approved today an SDR 416.3 million (about US$548 million) arrangement under the Extended Fund Facility (EFF) and an SDR 208.2 million (about US$274 million) Extended Credit Facility (ECF) for Honduras for a combined SDR 624.5 million (equivalent to US$822 million[1] or 250 percent of quota) and concluded the 2023 Article IV consultation.[2] The Executive Board's decision allows the authorities an immediate disbursement of SDR 89 million, equivalent to about US$117 million. These arrangements will help address Honduras' balance of payments needs and provide support for the Honduran government's economic and institutional reform agenda over the next three years.

The authorities' IMF-supported program includes economic and institutional reforms to support macroeconomic stability on a sustainable basis while creating fiscal space for much-needed productive investment and social spending. The program also aims at fostering durable and inclusive growth and enhancing climate resilience, while supporting the authorities' efforts to improve governance and transparency.

Following the pandemic and tropical storms, the Honduran economy has rebounded, with economic output now around 6 percent above pre-pandemic levels. Economic growth is projected to moderate to around 3 percent in 2023, down from 4 percent in 2022. Over the medium term, growth is projected to increase to near 4 percent, supported by public investment and the authorities' reform agenda. After peaking near 11 percent in 2022 in the

[1] U.S. dollar amounts have been calculated using today's exchange rate: (SDR 0.759521/US$).

[2] 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.

aftermath of the global commodity price shock, inflation has declined significantly and is projected to moderate to near 5 percent by the end of 2023.

Following the Executive Board discussion, Mr. Kenji Okamura, Deputy Managing Director and Chair, made the following statement:

"The Honduran economy has shown remarkable resilience to recent domestic and external shocks. Still, Honduras faces long-standing social and structural challenges, including weak governance and limited economic opportunities, that hinder its development potential and fuel migration. Infrastructure and climate adaptation investment needs are also significant. The authorities' economic program supported by a Fund arrangement seeks to preserve macroeconomic stability and begin to address these challenges to foster more robust and inclusive growth.

At the core of the authorities' program is a medium-term fiscal framework that preserves debt sustainability while opening space to increase productive investment and social spending. Underpinning these efforts will be a far-reaching tax reform and measures to strengthen tax administration. The program will also support the authorities' efforts to build a well-targeted and wide-reaching social safety net to reach the most vulnerable groups. Importantly, the authorities are also working on diversifying financing sources, including by developing domestic debt markets, which will be bolstered by a zero limit on central bank financing of the budget.

The authorities are committed to strengthening the frameworks for monetary and foreign exchange policies, supported by Fund technical assistance, with a view to preserving competitiveness and creating the necessary conditions to transition to a balanced, competitive, and efficient foreign exchange allocation system. Monetary policy should support the ongoing disinflation process and ensure that they are no undue pressures on the exchange rate.

Reforms in the energy sector will be essential to limit fiscal risks and improve the business environment. The authorities are implementing a comprehensive loss reduction plan to strengthen the financial position of the public electricity company and enhance the provision of electricity. In this context, the program also aims to support the authorities' efforts to build resilience to climate change.

The authorities have prioritized enhancing governance and transparency and the fight against corruption. They have strengthened the Anti-Money Laundering framework and are eliminating trust funds, which created corruption risks in spending execution. To further strengthen governance, the authorities are taking steps to implement an electronic declaration system for public officials' finances, create a comprehensive beneficial ownership registry, and establish an anti-corruption commission."

Executive Board Assessment[3]

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities' implementation of prudent economic policies that underpinned macroeconomic

---

[3] 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 any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

stability and promoted resilience to recent shocks. Notwithstanding these achievements, Directors noted that poverty and inequality, corruption, and large investment needs remain major hindrances to sustained growth and development. In this context, they supported the new Fund arrangements to anchor the authorities' reform agenda and catalyze additional external financing. Directors stressed the importance of maintaining strong ownership and commitment to reforms, continued capacity development support by the Fund and other IFIs, and adequate contingency planning.

Directors welcomed the program's aim to create fiscal space for increased social spending and investment while preserving debt sustainability. To this end, they underscored the need to implement revenue mobilization policies, including the planned tax reform and strengthened tax administration. Directors noted the importance of mechanisms to enhance the targeting of social spending, including a planned social registry, and improvements to public investment efficiency, including through the upcoming PIMA. They also called for continued progress in the diversification of fiscal financing sources.

Directors emphasized the need to enhance monetary and exchange rate policies to support price stability and resilience to shocks. To this end, they underscored that the crawling band exchange rate regime should be managed with a view to preserving competitiveness, while the efficiency of foreign exchange market allocation should be improved. Directors also called for data-driven monetary policy, including active monitoring of developments in international interest rates. They also underscored the importance of enhancing the monetary policy framework and transmission and looked forward to the findings of the updated safeguards assessment.

Directors commended the authorities' efforts to strengthen transparency and governance and reduce corruption risks, including the elimination of trust funds and the strengthening of the AML/CFT framework. They supported the authorities' plans to increase financial transparency of public officials, simplify administrative procedures, and create an international corruption commission. Directors also stressed the need to accelerate energy sector reforms to limit fiscal risks, support growth, and improve the business environment.

Directors called on the authorities to increase preparedness and build resilience to the effects of climate change. In this context, they took note of the authorities' interest on Fund financing under the Resilience and Sustainability Facility.

Table 1. Honduras: Selected Economic Indicators, 2021–27

	2021	2022	2023	2024	2025	2026	2027
		Projections					
Activity and Prices							
GDP (change in percent)	12.5	4.0	2.9	3.2	3.5	3.7	3.8
Inflation (percent)							
Average	4.5	9.1	6.4	4.7	4.1	4.0	4.0
End of period	5.3	9.8	5.3	4.2	4.0	4.0	4.0
Public Finances (percent of GDP)							
Non-financial public sector overall balance	-3.7	-0.2	-2.0	-1.7	-1.4	-1.0	-0.9
Non-financial public sector primary balance	-2.3	1.2	-0.7	-0.2	0.0	0.4	0.4
Gross debt	51.6	52.3	51.9	51.3	50.4	49.1	47.8
Balance of Payments							
Current account balance, percent of GDP	-4.6	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1
Gross international reserves (billions of US$)	9.0	8.7	7.9	8.0	8.1	9.1	8.7
Memorandum item:							
Nominal GDP (billions of Lempiras)	684	777	850	919	990	1068	1153

Sources: Honduran authorities; and IMF staff calculations.

HONDURAS

September 5, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION AND REQUESTS FOR AN ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CRGEDIT FACILITY

EXECUTIVE SUMMARY

Context. The Honduran economy has shown remarkable resilience to various domestic and external shocks over 2020-22, and real GDP is now around 6 percent above pre-pandemic levels supported by the authorities' prudent policies. That said, Honduras faces long-standing social and structural challenges that hinder its development potential and stability. Under the previous Fund-supported program that expired in January 2022, Honduras succeeded in enhancing the quality of fiscal policy and implementing institutional reforms. The current authorities are committed to maintaining prudent macroeconomic policies and advancing structural reforms while fostering inclusive growth by creating space for critical social spending and infrastructure investment. In this context, the authorities have requested a new Fund arrangement to anchor their economic and institutional reform agenda.

Recent developments and outlook. Growth is projected to moderate this year to around 3 percent from 4 percent in 2022. Inflation has gradually declined close to the 3-5 percent reference range of the Central Bank after peaking last year at almost 11 percent in the aftermath of the global commodity price shock. Prudent fiscal policies have continued, with the fiscal deficit declining to near balance in 2022, reflecting robust revenues and slow spending execution, in particular capital investment. The current account deficit narrowed in 2022, buoyed by strong remittance flows, but is expected to widen this year largely due to a less supportive external environment. International reserves still remain at adequate levels. Over the medium term, growth is projected to increase to near 4 percent, supported by public investment and the impact of reforms.

Article IV discussions. There was broad agreement on the need to advance policies to strengthen economic resilience and address structural bottlenecks to boost inclusive growth. Policy priorities include (i) reducing poverty and social inequality, including through greater public investment and social spending; (ii) securing the financial sustainability of the electricity sector; (iii) strengthening the monetary and exchange rate policy frameworks; (iv) improving governance and transparency, and tackling corruption; and (iv) enhancing resilience to climate change. Decisive implementation of

policies and structural reforms will be essential to reduce poverty, promote investment, and raise potential growth.

Program objectives. The program will aim to entrench economic stability and begin to tackle Honduras' impediments to sustainable growth. The program will be anchored on (i) a gradual fiscal adjustment path and supportive fiscal structural policies that create space for much-needed capital and social spending while preserving debt sustainability; (ii) consistent monetary and exchange rate policies that support disinflation, strengthen external resilience, including by safeguarding reserves, and preserve macroeconomic stability; and (iii) structural reforms to strengthen governance and combat corruption while bolstering the energy sector and resilience to climate change.

Program risks. Risks to the program stem from a challenging global backdrop, including weaker-than-expected growth in key trading partners, and adverse weather events. On the domestic side, a complex political environment and policy implementation slippages could jeopardize program objectives. Program design and contingency planning would help to mitigate these risks.

Program modalities. In pursuit of their policy plans, the Honduran authorities are requesting a 36-month EFF/ECF with access of SDR 624.5 million, 250 percent of quota, split between the ECF arrangement (SDR 208.2 million, 83.3 percent of quota) and the EFF (SDR 416.3 million, 166.7 percent of quota) and equally phased across semi-annual reviews. The Fund-supported program aims to address the actual, prospective, and protracted BoP needs faced by the country and to play a catalytic role for additional official multilateral and bilateral external financing. The authorities intend to utilize the resources as indirect budget support, which will facilitate social spending and fill urgent infrastructure gaps, further exacerbated by the pandemic and climate shocks, and a more gradual fiscal adjustment, while safeguarding international reserves. Moreover, the authorities have expressed interest in Fund financing under the Resilience and Sustainability Facility (RSF), which could be considered in subsequent program reviews.

Approved By
Patricia Alonso-Gamo (WHD) and Natalia Tamirisa (SPR)

Discussions were held in Tegucigalpa during June 5-16, 2023, and continued remotely thereafter. The staff team comprised Ricardo Llaudes (head), Carlos Chaverri, William Lindquist (all WHD), Michal Andrle (ICD, formerly WHD), Hassan Adan (FAD), and Martha Woldemichael (SPR). Christian Henn (Resident Representative) and Mr. Guerra (Executive Director) also participated in the discussions. The mission met with senior economic officials, including Finance Minister Rixi Moncada and Central Bank of Honduras President Rebeca Santos, in addition to representatives of labor unions, the private sector, civil society, and the international community. Heidi Canelas and Justin Lesniak (both WHD) and Sonia Pavon Solis (Resident Representative Office) provided additional support.

CONTENTS

CONTEXT 5

RECENT ECONOMIC DEVELOPMENTS 6

OUTLOOK AND RISKS 10

POLICY DISCUSSIONS 12

A. Fiscal Policies: Creating Fiscal Space for Investment and Social Spending 13
B. Monetary, Exchange Rate, and Financial Sector Policies: Preserving Macroeconomic Stability 18
C. Energy Sector Reform and Building Resilience to Climate Change 22
D. Improving AML/CFT and Governance and Combatting Corruption 25

PROGRAM MODALITIES 27

STAFF APPRAISAL 28

BOXES

1. Poverty and Food Insecurity 55
2. Labor Markets and Education 56
3. Comprehensive Tax Reform to Support Development Needs 58
4. Neutral Interest Rate Estimates 60
5. Climate Change Adaptation Strategies 61

FIGURES

1. Long-Term Macroeconomic Trends, 2010-2022 31

2. Social Indicators 32
3. Key Recent Developments 33
4. Real Sector Developments 34
5. External Sector Developments 35
6. Fiscal Developments 36
7. Monetary and Financial Sector Developments 37

TABLES

1. Selected Economic Indicators 38
2. Statement of Operations of the Central Government, 2020-2028 (in millions of Lempiras) 39
3. Statement of Operations of the Central Government, 2020-2028 (in percent of GDP) 40
4. Statement of Operations of the Nonfinancial Public Sector (in millions of Lempiras) 41
5. Statement of Operations of the Nonfinancial Public Sector (in percent of GDP) 42
6. Summary Accounts of the Financial System 43
7. Balance of Payments (In millions of US Dollars) 44
8. Balance of Payments (In percent of GDP) 45
9. External Financing Needs and Sources 46
10. External Financing Gap 47
11. External Vulnerability Indicators 48
12. Decomposition of Public Debt and Debt Service by Creditor, 2022-24 49
13. Medium-Term Macroeconomic Framework 50
14. Structure and Performance of the Banking Sector 51
15. Proposed Disbursements, Purchases, and Timing of Reviews Under the ECF/EFF Arrangements, 2023-26 52
16. Indicators of Fund Credit 53
17. Sustainable Development Goals 54

ANNEXES

I. External Sector Assessment 62
II. Economic Impact of Climate Change and Natural Disasters 65
III. Risk Assessment Matrix 67
IV. Implementation of 2019 Article IV Recommendations 69
V. Implementation of 2016 FSSR Recommendations 71

APPENDIX

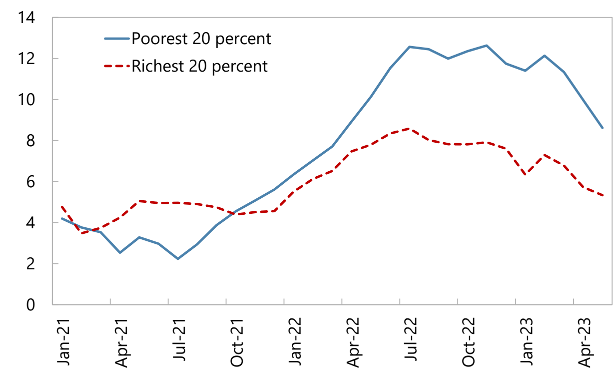
I. Letter of Intent 72
Attachment I. Memorandum of Economic and Financial Policies 75
Attachment II. Technical Memorandum of Understanding 96

CONTEXT

1. **Since the last Article IV consultation in July 2019, the Honduran economy has shown significant resilience to external and domestic shocks.** Economic activity has rebounded sharply from the pandemic and back-to-back tropical storms in 2020, which resulted in losses of around 7½ percent of GDP. After contracting by 9 percent in 2020, real GDP growth surged to 12.5 percent in 2021, making Honduras' recovery among the strongest in the region. Real GDP is now around 6 percent above pre-pandemic levels, driven by strong manufacturing activity and remittance-fueled domestic demand. This performance has been anchored by the authorities' prudent policies, which have supported macroeconomic stability. Honduras has also benefitted from close engagement with the IMF, including two SCF/SBA supported programs (2014-17 and 2019-22) and significant technical assistance and capacity development.

2. **The authorities are advancing policies to safeguard macroeconomic stability, protect the most vulnerable, and improve governance and transparency.** The government of President Xiomara Castro, who was inaugurated in January 2022, has been focused on addressing investment gaps and social challenges while improving governance and fighting corruption. The authorities' decisive response to recent shocks, including through the scaling up of targeted social assistance programs, was critical to protect the most vulnerable from higher inflation, which had an outsized impact on this group. Moreover, key reforms have already been adopted to bolster governance and transparency, including by (i) enhancing budgetary discipline and spending controls by eliminating trust funds and (ii) strengthening the anti-money laundering framework by repealing legislation that had previously weakened it. On the other hand, large public investment projects remain largely unexecuted—reconstruction after the tropical storms also remains incomplete—reflecting capacity limits and financing constraints.

Inflation by Income Quantiles
(Percent, year-on-year)



Sources: Central Bank of Honduras

3. **Honduras faces long-standing social and structural challenges that hinder its development potential and stability.** During the last decade, growth in real GDP per capita has significantly lagged regional peers (**Figure 1**), reflecting, *inter alia*, limited growth in investment and the impact of extreme weather events. As a result, Honduras remains one of the poorest and most unequal countries in the Western Hemisphere, with GDP per capita[1] of US$2,500 and poverty rates over 70 percent, with extreme poverty at over 50 percent.[2] The economy is heavily reliant on remittances (close to 27 percent of GDP in 2022) and a few exports including coffee, palm oil, bananas, and textiles (maquilas). Crime, weak governance and institutions, corruption vulnerabilities,

[1] Honduras is among the 60 poorest countries (of 193) by GDP (constant 2015 US$) per capita (World Bank, 2021).

[2] Data for 2021 from the *Instituto Nacional de Estadísticas* (INE).

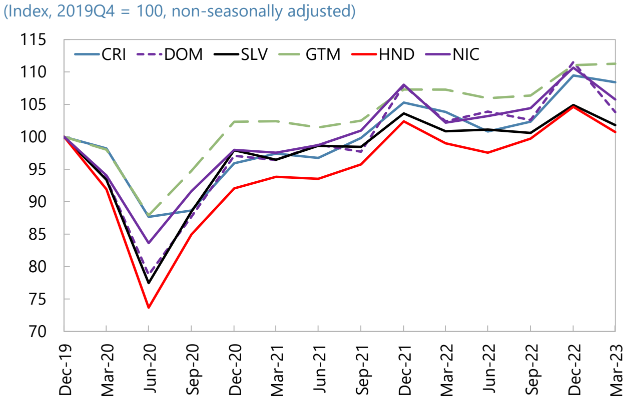
and limited formal economic opportunities—informal employment[3] is around 80 percent—fuel migration. Structural bottlenecks, including in the energy sector, stifle investment, with FDI inflows below regional averages. Moreover, Honduras remains one of the world's most vulnerable countries to climate disasters, with sizeable adaptation investment needs. Addressing these challenges will take time and require a comprehensive approach that promotes economic diversification and social inclusion.

4. The authorities have requested Fund financing to support their policies and reform agenda. Financing under the program is expected to be in the form of budget support and address actual, prospective, and protracted BoP needs faced by the country. Specifically, the authorities are seeking to decisively scale up capital investment projects (focusing on hospitals, schools, dams, and roads) while also creating space for priority social spending. To this end, they are seeking to mobilize IFI and bilateral financing.[4] Their Fund-supported agenda aims to create fiscal space for increased investment and social spending while maintaining fiscal discipline; strengthen the monetary and exchange rate policy frameworks, safeguard reserves, and preserve macroeconomic stability; enhance climate and energy sector resilience; and improve governance and transparency while combatting corruption.

RECENT ECONOMIC DEVELOPMENTS

5. Strong economic growth moderated in late 2022 and early 2023. After contracting by 9 percent in 2020, the economy expanded 12.5 and 4.0 percent in 2021 and 2022, respectively, driven by the gradual reopening of the economy after the pandemic, with strong domestic demand, robust remittance inflows (up 18 percent in 2022) and a resilient export sector, especially maquila-related. As in most countries in the region, growth moderated in 2023:Q1, down to 1.9 percent year-on-year, as both investment and exports slowed. High-frequency indicators through June—up 2.9 percent year-to-date—confirm the moderation in activity, manufacturing in particular, in the context of a less supportive external environment. Recent drought conditions have also impacted adversely agricultural output and contributed to energy supply problems, leading to the temporary introduction of rolling blackouts in June 2023.

Real GDP: Central America and Dominican Republic
(Index, 2019Q4 = 100, non-seasonally adjusted)



Sources: Central Bank of Honduras; and Haver.

6. The impact of the recent shocks, while mitigated by the authorities' swift response, has exacerbated already fragile social conditions. The COVID-19 pandemic, back-to-back tropical

[3] Latest International Labor Organization (ILO) estimate for 2017.

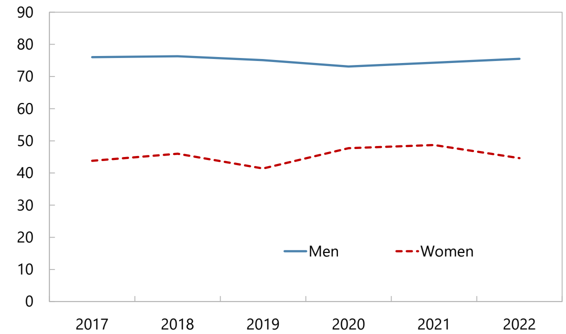
[4] In this context, diplomatic relations were recently established with China and membership in the Development Bank of Latin America and the Caribbean (CAF) was recently approved by Congress.

storms, and the global commodity price shock have exacerbated social conditions in Honduras, increasing poverty, inequality, and food insecurity (**Box 1**), with the number of Hondurans in need of humanitarian assistance more than doubling since 2020.[5] Importantly, the authorities' decisive and effective response was key to mitigating the impact of higher food and energy prices on the poor. Free electricity has been provided since May 2022 to poor households with consumption of less than 150 kWh/month (at an annual cost of around 0.3 percent of GDP),[6] and subsidies also continue for public transportation and for LPG gas (around 0.2 percent of GDP), which is mainly used for cooking by poor households.

7. Elevated levels of unemployment and informality continue, while the gender gap in the labor market has widened. While the unemployment rate declined to 8.9 percent in 2022 from 10.9 percent in 2020, it remains above pre-pandemic levels. The labor force participation rate is also low, especially for women, underscoring the gender gap that contributes to labor market informality (**Box 2**).

Labor Force Participation

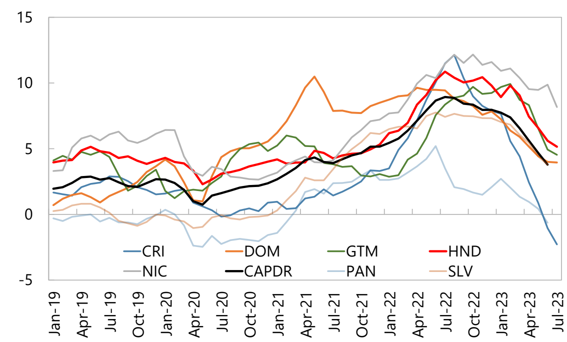
(Percent of working age population)



Sources: Honduras National Statistical Institute; and IMF staff calculations.

Headline Inflation

(Percent, year-on-year)



Sources: Central Bank of Honduras; and Haver.

8. Inflation has rapidly declined since early 2023. As in most other countries, inflation pressures rose sharply in Honduras in 2022—peaking at almost 11 percent (y/y) in July from 5.3 percent at end-2021—largely driven by food prices, and well above the Central Bank of Honduras (BCH) reference range of 3-5 percent. Headline inflation has since eased to 5.2 percent in July 2023, as prices for food and other commodities have stabilized and imported inflation has abated (**Text Figure 1**). Underlying inflationary pressures are easing more gradually, with core inflation declining to 5.8 percent, down from a peak of 9 percent. Importantly, inflation expectations are also sharply declining and converging toward the BCH reference range.[7] In response to elevated inflation, the BCH tightened

[5] IDA/IFC/MIGA Country Partnership Framework for Honduras for the period FY23-FY27.

[6] This has been financed by a government subsidy to the public utility company ENEE (60 percent) and a cross-subsidy of large consumers (40 percent). For all other consumers, tariffs are again reflecting cost recovery since January 2023 (after automatic tariff increases were halted during 2022H2 to cushion consumers from high fuel prices). The authorities have strengthened the targeting of this policy over time by increasingly limiting it to poor neighborhoods and thereby reducing the number of beneficiary households to around 900,000 from slightly above 1 million initially.

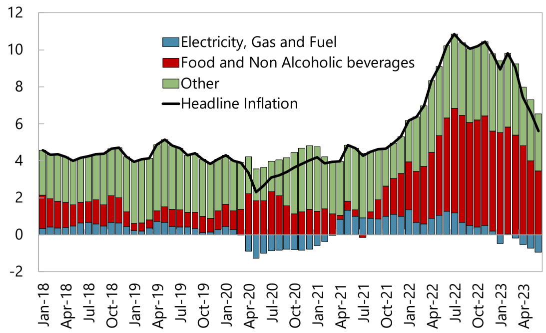
[7] In the July BCH survey, inflation expectations continued to decline, down to 5.6 percent and 5.2 percent 12 and 24 months ahead, respectively, the lowest readings since February 2022. Long-term Consensus inflation expectations are also well anchored at 4.1 percent in the July 2023 survey.

its policy stance by increasing open market operations (OMOs) to absorb liquidity, prompting the interbank rate to rise from around 1 percent in March 2022 to 3.5 percent in October 2022 (see ¶27).

Text Figure 1. Inflation and Monetary Policy Developments

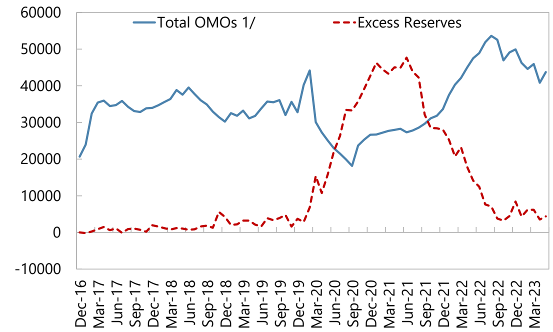
Inflation surged largely driven by food prices.

Contributions to Headline Inflation
(Percentage points)



In response, the BCH stepped up liquidity absorption.

Open Market Operations and Excess Reserves
(Millions of Lempiras)

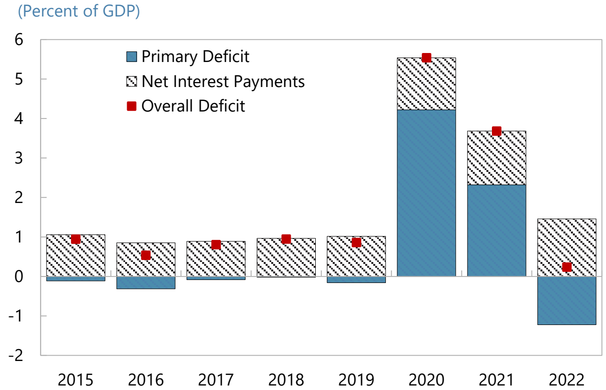


1/ Refers to the outstanding stock of BCH bills and bonds issued.

Sources: Central Bank of Honduras; and IMF staff calculations.

9. Fiscal policy has remained prudent, with the deficit declining to near balance in 2022. The non-financial public sector (NFPS) deficit narrowed to 0.2 percent of GDP in 2022 from an average of 4½ percent of GDP in 2020-21. The deficit reduction was driven by strong revenues, buoyed by the robust recovery and higher prices, and constrained expenditure execution capacity, including due to the closure of trust funds and restructuring of ministries. In 2023:H1, the NFPS registered a lower surplus of 1.2 percent of GDP—compared to a surplus of 2.6 percent of GDP in the same period in 2022—from somewhat lower tax revenues and greater capital expenditure execution (Text Table 1).[8] Despite the smaller fiscal deficit in

Non-Financial Public Sector Deficit
(Percent of GDP)



Sources: Honduras Ministry of Finance; and IMF staff calculations.

Text Table 1. NFPS Fiscal Execution
(Percent of GDP, through June)

	2022H1	2023H1 1/
Income and Grants	**14.8**	**14.0**
Current income	14.7	13.9
Tax income	*9.3*	*8.9*
Non-tax income	*0.6*	*0.7*
Contributions for pensions and social security	*1.5*	*1.5*
Sales of goods and services	*2.5*	*1.8*
Other current income	0.8	1.0
Grants	0.1	0.1
Capital income	0.0	0.0
Expenses	**12.2**	**12.9**
Current expenses	11.6	11.5
Wages and salaries	*5.2*	*5.2*
Purchases of goods and services	*3.5*	*3.3*
Interest paid	*1.2*	*1.4*
Current transfers	*1.7*	*1.6*
Other current expenses	*0.1*	*0.0*
Capital expenses	0.6	1.3
Fixed investment	*0.3*	*1.0*
Other capital expenditure	*0.2*	*0.3*
Overall Balance	2.6	1.2

Sources: Ministry of Finance, Haver Analytics, and IMF staff calculations.
1/ Preliminary.

[8] In 2022, tax revenues had been boosted by a one-off effect due to forbearance during the pandemic.

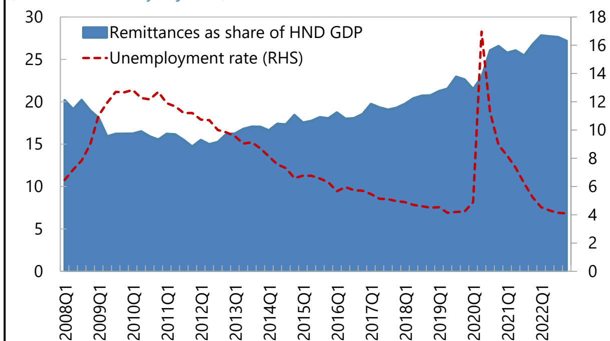
2022, gross public debt increased to 52.3 percent of GDP at end-2022 due to the recognition of previously unaccounted domestic debt (**DSA Annex**).

10. The external position strengthened in 2022 and international reserve buffers remain at adequate levels, although some strains in the FX market emerged. The external position in 2022 is assessed to be broadly in line with the level implied by fundamentals and desirable policies (**Annex I)**.

- The *current account* deficit narrowed to 3.2 percent of GDP in 2022 from 4.6 percent of GDP in 2021, driven by strong remittances, favorable prices for key export products (coffee, bananas, and palm oil), and a dynamic maquila sector. Net FDI inflows (2.2 percent of GDP) and official flows supported the external position in 2022. The current account reached a small surplus (US$70 million) in 2023:Q1 on the back of still robust remittances flows. That said, a less supportive external environment—softer growth in trading partners and worsening terms-of-trade—is weighing on trade dynamics, with goods exports through May declining by 4.3 percent (y/y), with maquila-sector exports (mainly textiles) down 11.2 percent, and non-maquila imports increasing by 0.2 percent (y/y).

U.S. Remittances to Honduras and U.S. Hispanic Unemployment Rate

(Percent; seasonally adjusted)



Sources: National authorities; and IMF staff calculations.

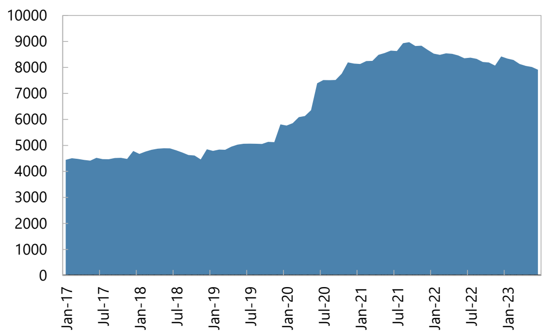
- *Gross international reserves* declined by about US$120 million in 2022 to US$8.7 billion (US$8.4 billion in net terms). The BCH sold US$336 million (net), mostly towards the end of the year as higher commodity prices increased demand for foreign exchange (FX). At 5.9 months of import cover and 137 percent of the IMF's Assessing Reserve Adequacy metric at end-2022, gross reserves remained at comfortable levels. Reserves have declined by a further US$730 million as of August 2023, mainly explained by significant net external repayments by the public sector (around $460 million) and increased FX sales to energy importers to compensate for lower domestic energy production in the context of the drought (Text Figure 2).
- In response to *declining volumes in the interbank FX market* the BCH reintroduced in April 2023 its own FX auction mechanism alongside 100 percent surrender requirements for foreign exchange agents, thereby shutting down the interbank FX market (see ¶29).[9]

[9] The system of auctions had been in place for more than two decades prior to 2017. Starting in the early 2010s, a process was established, supported by IMF technical assistance, to gradually wind down the auction system and introduce an interbank market for FX. This was a key objective of the two previous Fund-supported programs. The interbank market was launched in 2017, alongside a gradual process of lowering both surrender requirements for FX agents and the importance of BCH auctions, which had culminated in June 2021 in their complete elimination.

Text Figure 2. Recent Developments in Net International Reserves

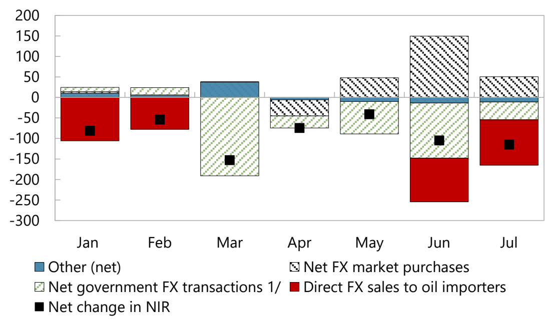
While remaining comfortable, net international reserves have declined since 2021….

Net International Reserves
(Millions of USD)



…with the decline in 2023 mostly driven by net government external payments and direct sales to oil importers.

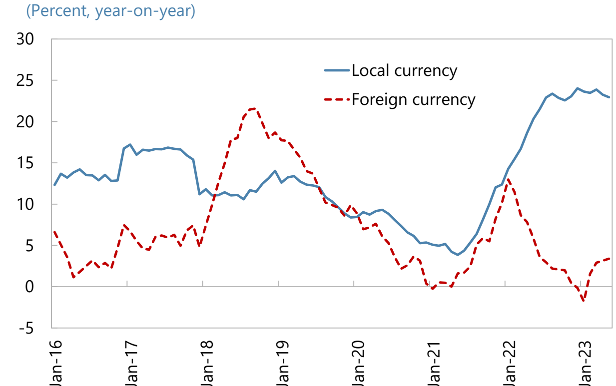
Monthly Change in Net International Reserves, 2023
(Millions of USD)



1/ Loan disbursements and grants minus debt service

Sources: Central Bank of Honduras; and IMF staff calculations.

Growth of Credit to the Private Sector
(Percent, year-on-year)



Sources: Central Bank of Honduras; and IMF staff calculations

11. The financial sector remains sound, underpinned by healthy bank balance sheets. The banking system remains well-capitalized, with the capital adequacy ratio at 13.8 percent in July 2023, well above the 10 percent requirement, and with solid levels of liquidity and profitability. Credit to the private sector in local currency has grown to around 20 percent while FX lending has markedly decelerated, reflecting increasing FX lending rates. Credit as a share of GDP stood at 67 percent at end-2022, compared to 64 percent in 2021. Importantly, non-performing loans (NPLs) remain low at 2.3 percent of total loans and provisioning remains strong at 137 percent of NPLs.

OUTLOOK AND RISKS

12. After a slowdown in 2023, growth is projected to recover, supported by program policies, while inflation is projected to subside (Text Table 2). In the near term, the economy faces headwinds from a less supportive external environment as public investment increases.

- *Real GDP growth* is projected to decelerate to around 3 percent in 2023—in line with lower U.S. and remittances growth—and to gradually converge toward potential (close to 4 percent),[10]

[10] This is consistent with Honduras' average growth over 2000-2019.

supported by stronger public investment, the implementation of reforms under the program, and strengthened economic resilience.

- *Inflation* is projected to return to the BCH reference range (of 3-5 percent) by early 2024 and to remain within that range thereafter, driven by a normalization of commodity prices and the strengthening of monetary and FX policies.
- *External balance.* The current account deficit is projected to widen to around 5 percent of GDP in 2023, consistent with the deceleration in the U.S. (affecting maquila exports and lowering remittances growth), worsening terms-of-trade, and the adverse ramifications of the energy crisis linked to the regional drought. Reserve adequacy is expected to remain within the recommended 100-150 percent range of the ARA metric and close to 5 months of import cover over the medium term.
- *The fiscal deficit of the NFPS* is expected to widen to 2 percent of GDP in 2023 as spending, including capital expenditure, begins to normalize following the restructuring of ministries and elimination of trust funds.[11] Thereafter, the planned gradual fiscal consolidation would return the NFPS deficit to 1 percent of GDP by 2026 underpinned by prudent expenditure policies, the revenue efforts expected during the program, and expected improvements in the energy sector.
- *Debt sustainability.* The baseline envisages a gradually declining public debt path—reaching 46.6 percent of GDP by 2028—underpinned by the fiscal reforms in the program, including greater spending efficiency, in line with a low risk of external debt distress and moderate risk of overall debt distress (**DSA Annex**).

Text Table 2. Medium-Term Economic Projections

(Percent of GDP, unless otherwise noted)

	Actual	Projections					
	2022	2023	2024	2025	2026	2027	2028
Real							
GDP growth, percent	4.0	2.9	3.2	3.5	3.7	3.8	3.8
Inflation (end of period, percent)	9.8	5.3	4.2	4.0	4.0	4.0	4.0
Fiscal							
Primary balance	1.2	-0.7	-0.2	0.0	0.4	0.4	0.5
Overall balance	-0.2	-2.0	-1.7	-1.4	-1.0	-0.9	-0.9
Public capital investment	2.8	3.0	3.8	4.0	4.0	4.0	4.0
Gross debt 1/	52.3	51.9	51.3	50.4	49.1	47.8	46.6
Balance of payments							
Current account balance	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1	-3.9
Gross international reserves (percent of ARA)	137	120	116	112	117	109	109

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

1/ Debt projections use the defintion from the DSA.

[11] The elimination of trust funds led to low execution in 2022 (and into 2023) given lacking implementation capacity in the public administration after years of execution through trust funds run by private sector entities.

13. Downside risks to the outlook are significant, largely driven by a challenging global backdrop and the impact of extreme weather events (RAM, Annex III).

- The *global outlook* is subject to downside risks related to (i) an intensification of the effects of Russia's protracted war in Ukraine that could further dampen the global outlook and growth in trading partners; (ii) an abrupt slowdown in trading partners, the U.S. in particular, that could trigger weaker-than-projected export and remittances growth; (iii) a monetary policy miscalibration that could increase risk aversion and external borrowing costs and create FX market pressures; and (iv) new commodity price volatility that could lead to higher inflation, pressure on FX reserves, and social instability. Adverse weather events (hurricanes/tropical storms, floods, and droughts), in addition to their human cost, could impact Honduras' fiscal position, inflation, and agricultural exports, and, in the long run, further erode Honduras' growth potential and aggravate emigration. On the upside, a stabilization of global commodity prices at lower levels would bring further relief regarding inflation, while a more resilient U.S. and global economy would support export and remittances growth.
- *Domestically*, risks to the reform agenda stem from limited implementation capacity and a complex political environment, including lack of a majority in Congress, while program implementation slippages may jeopardize program objectives and the availability of financing. Finally, in the near term, more severe weather conditions, including from the "*El Niño*" phenomenon, could lower growth further.
- Given significant downside risks to the outlook, contingency planning, including in the event external financing does not materialize, will be essential to preserve macroeconomic stability and ensure achievement of program objectives.

Authorities' Views

14. The authorities concurred with staff's assessment and were broadly aligned on growth and inflation projections. However, they also noted potential upsides from an improvement in budget execution that could lead to higher capital expenditure, boosting growth in the short term. The authorities also acknowledged the external pressures on the current account and reserves.

POLICY DISCUSSIONS

15. The authorities' economic program aims to safeguard macroeconomic stability while tackling Honduras' investment and social needs. Discussions with the authorities focused on: (i) maintaining fiscal discipline while opening fiscal space for investment and social spending needs; (ii) strengthening monetary and exchange rate policies to safeguard external resilience and macroeconomic stability; (iii) energy sector reform and building resilience to climate change; and (iv) improving governance and transparency.

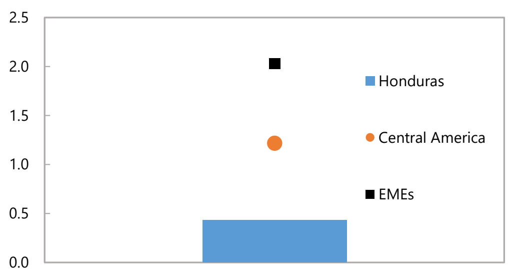
A. Fiscal Policies: Creating Fiscal Space for Investment and Social Spending

16. Honduras needs to scale up social and infrastructure investment expenditures to address poverty and promote economic development. Compared to peer countries, Honduras spends less on social assistance, while the overall perceived quality of infrastructure is lower (Text Figure 3). The authorities see such a scale up as key to reducing poverty, increasing employment, and strengthening economic resilience, including to climate change.

Text Figure 3. Social Spending and Infrastructure Quality

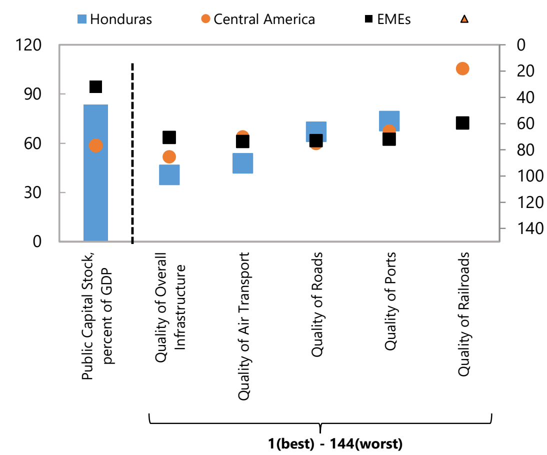
Honduras spends less on social assistance than peers….

Social Assistance Spending (in percent of GDP), Latest Value Available



… while perceived infrastructure quality in Honduras is one of the lowest in Central America.

Capital Stock and Infrastructure Quality, Latest Value Available (% of GDP and ranking)



Sources: IMF FAD Expenditure Assessment Tool (EAT), World Economic Outlook, ASPIRE, IMF investment and Capital Stock Dataset, and World Economic Forum.

17. The authorities' fiscal program aims at creating space for priority spending while preserving debt sustainability. The program targets a gradual reduction of the overall deficit of the NFPS from 2 percent of GDP in 2023 to around 1 percent by the end of the program, monitored through a *quantitative performance criterion (QPC)*, with a gross operating surplus of over 3 percent of GDP.

- The deficit is projected to initially increase in 2023 to 2 percent of GDP, up from 0.2 percent of GDP in 2022 (but significantly below the 4.4 percent deficit in the approved budget). Revenues are projected to remain robust, although to be impacted by lower inflation, with some moderation in tax performance and collections from sales of goods and services in the energy sector. The spending envelope accommodates a recovery of public sector employment towards pre-2022 levels[12] and some expected acceleration of still-low capital spending in 2023H2, in line with historical seasonal patterns.

- The reduction of the overall deficit under the program—narrowing to 1.7 percent of GDP in 2024 and to 1 percent of GDP in medium-term—will be underpinned by efforts on both the revenue and expenditure sides. The bulk of the reduction in the deficit comes from revenue increases, including through revenue administration reforms, that continue to drive revenue convergence towards pre-pandemic levels. The program monitors central government tax revenues through an ***indicative target (IT)***. On the spending side, prudent current spending—projected to decline relative to GDP—and the implementation of energy sector reforms should create space for increases in social and capital spending. The program includes a ceiling on current primary spending (excluding priority social spending) to monitor its execution ***(IT)***.

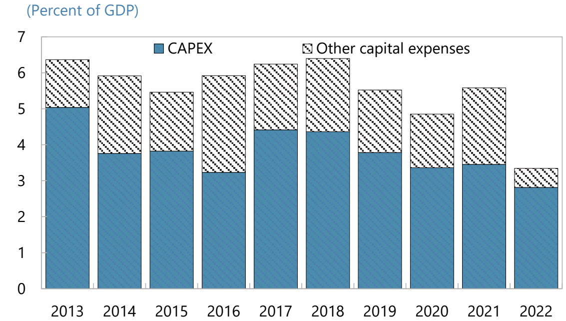
Medium-Term Fiscal Adjustment Measures, 2023-26

Fiscal Measure	Percent of GDP
Revenues	**0.8**
Income tax exemption reforms	0.3
Goods and service tax	0.4
Other revenue	0.1
Expenditures	**0.2**
Compensation of employees	0.2
Purchases of goods and services	0.6
Other expenditures	0.6
Increase in social benefits	(0.2)
Increase in capital spending	(1.0)
Total deficit reduction by 2026	1.0

Source: IMF staff calculations.

18. The program will support a scaling-up of productivity-enhancing public capital investment while safeguarding debt sustainability. Under the baseline, capital investment will be scaled up from 3 to over 4 percent of GDP by 2026—albeit still below the 2013-19 average of around 6 percent of GDP. An increase is warranted by Honduras' urgent need for public investment to reduce poverty, bolster resilience to climate change (especially through dams for flood control and investments in the energy sector), and increase the economy's growth potential. To this end, an adjustor under the program envisages that public investment (and therefore the fiscal deficit) in 2024 could be up to 1.3 percent of GDP higher than under the baseline should additional external financing (beyond that envisaged in the baseline) materialize for capital spending. The authorities are committed to safeguarding debt sustainability and will evaluate how any additional capital spending may impact debt levels and related risks, in consultation with Fund staff.[13]

Capital Expenditures and Other Capital Expenses[1/]
(Percent of GDP)



1/ Other capital expenses refer to transfers by the NFPS to other spending units (such as municipalities and SOEs) for capital investment projects.
Sources: Honduras Ministry of Finance; and IMF staff calculations.

19. Revisions to the FRL would support anchoring medium-term fiscal policies. While the Fund-supported program is expected to help guide policies in the short to medium term, it remains appropriate to revise the FRL with a view to strengthening its role as a medium-term policy anchor.

[12] The NFPS wage bill significantly declined in 2022 (down 0.7 p.p. from 2021) due to the restructuring of spending units, including ministries, and temporary reductions in headcount as rehiring started to take place only in late 2022 and 2023.

[13] Staff estimates that debt sustainability would be preserved even if the full 1.3 percent of GDP of additional capital spending were to materialize.

Such a revision should entrench a fiscal path that underpins debt sustainability while recognizing the country's development needs. It should also incorporate appropriate flexibility through well-defined escape clauses and corrective mechanisms and ensure their alignment with the budget calendar and the medium-term fiscal framework. The authorities have already made progress in this direction with support from Fund and IDB technical assistance.

20. Tax policy and administration reforms will support revenue mobilization (Box 3). The authorities, with support from the Fund and other IFIs, are advancing a multi-pronged strategy to broaden the tax base and strengthen the efficiency of revenue collection. In addition to these efforts, the authorities should consider reversing the reductions to gasoline and diesel taxes introduced in 2022—at an annual cost of 0.4 percent of GDP—once the social safety nets have been further strengthened.[14]

- *Tax policy*. A new tax reform bill (*Ley de Justicia Tributaria*, LJT), designed with IMF assistance and currently under Congressional discussion, aims to reduce widespread exemptions to the corporate income tax (CIT)[15]—gradually replacing numerous special CIT regimes with two new ones—while safeguarding competitiveness and acquired rights ***(end-December 2023, structural benchmark (SB))***. Staff estimates yields at upwards of 1 percent of GDP, although these are subject to uncertainty and are expected to accrue only very gradually, as firms' benefits under existing regimes expire. The reform also strengthens controls and enforcement, including by setting global income as the taxable basis and introducing a registry of beneficial ownership. A transparent and predictable implementation of the law, as would be set out in corresponding regulations, will be essential to protect competitiveness, including against regional peers, and strengthen the business environment while reducing the scope for corruption.
- *Tax administration*. The authorities have designed, with IMF assistance, a comprehensive inter-institutional action plan for tax administration reform involving the Ministry of Finance and tax and customs administrations, whose implementation would be buttressed by passage of the LJT. Some elements of the plan are already being implemented, e.g., improving inter-institutional collaboration, data sharing, and digitization. Other ongoing and planned reforms include:
    - Fostering tax compliance by developing a system of proportional penalties for delinquent taxpayers and strengthening the management of tax arrears;
    - Developing a system for VAT refunds, to eventually replace ex-ante VAT exemption orders that are often subject to fraud;
    - Approving the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters, expected to foster Honduras' international cooperation with tax administrations in other countries ***(end-December 2023, SB)***; and

[14] Reversing the reduction in fuel taxes would also be supportive of the authorities' climate policies.

[15] Tax expenditures reduce annual revenues by around 7 percent of GDP, compared to 3-5 percent of GDP among regional peers. CIT exemptions represent close to 40 percent, while most of the remainder is due to VAT exemptions.

   - Comprehensively reforming customs through a long-term project with IDB assistance with a focus on strengthening operational capacity and modernization of technological platforms.

21. Enhanced expenditure policies are essential to underpin consolidation and the targeting of spending. Fiscal consolidation, while creating room to expand social protection and investment needs, will require both careful targeting and discipline on spending.

- *Social protection.* In reaction to global commodity price shocks, social support has been provided through fiscal measures (¶6) and other programs, such as aid to small farmers by providing seeds and fertilizer (*bonos tecnológicos*) and subsidized loans. In parallel, expansion of the comprehensive flagship social assistance program *Red Solidaria* continues, expected to provide direct assistance to 350,000 of the poorest households in rural areas by end-2023, including through conditional cash transfers. Beneficiary selection has relied on a consistent methodology, implemented with IFI assistance. An analogue census of urban extreme poverty is currently underway to identify approximately 100,000 beneficiary households marginalized urban areas and expected to be concluded by September 2024 ***(SB)***. Together with other relevant information, these data will be organized into a comprehensive social sector information system, including a social registry, which is envisaged to be established by end-June 2024 ***(SB)*** as a repository to inform the country's social assistance strategy. A companion program, *PROASOL*, focuses on other groups at risk, including indigenous groups and the disabled. Staff underscored the need for continued work with other IFIs to strengthen the targeting, coverage, and effectiveness of social programs. As part of the program, priority social spending would be expanded ***(IT)*** and its quality should be subsequently evaluated in coordination with international partners.[16] The authorities plan to update their poverty reduction and growth strategy by the second review, and a new Social Protection Law would be submitted to Congress by end-June 2024.
- *Capital spending.* As public investment is scaled up, it will be essential to strengthen the planning, selection, and monitoring of infrastructure projects. This will be essential as public investment is scaled up. To this end, a Public Investment Management Assessment (PIMA), including a climate module, will be conducted in late 2023, with resulting recommendations to guide reforms and program conditionality going forward.

22. Strengthening budget credibility and transparency will also support fiscal management and program objectives. Considerable progress has been made in these areas.

- *Elimination of trust funds.* In 2022, the authorities passed legislation to close trust funds, a longstanding Fund recommendation. Trust funds had executed a sizeable share of public spending outside of budgetary controls, a poor public financial management practice also giving rise to corruption risks. Trust funds' current transactions have been largely integrated into the

[16] Social programs are being expanded mainly by adding beneficiaries and broadening their intervention beyond conditional cash transfers.

budget process, and the authorities aim to complete the full integration of their assets and liabilities into the public sector balance sheet by end-December 2024 **(*SB*)**, with Fund assistance.

- *Strengthening the Treasury Single Account (TSA) and cash management*. The implementation of the TSA should be strengthened to improve liquidity, including by enhancing its fungibility, and debt management. The authorities plan to submit a new Law on the TSA to Congress by March 2024 ***(SB)***, developed with technical assistance from the IMF and other IFIs, and operationalize this new TSA law by December 2025 ***(SB).*** With Fund assistance, work is underway to improve liquidity projections and link them to a debt issuance strategy to improve domestic debt markets (¶24).
- *Preparation of a new Procurement Law*. The existing procurement law is outdated and leads to lags in procurement, which also slows down investment project implementation. A new law is currently being prepared to address these shortcomings, and strengthen contracting processes, competitive bidding, and powers for fraud detection, while ensuring needed safeguards. Congressional approval of the new law is expected by end-2023.

23. The authorities plan to diversify financing sources to support their fiscal policies. Honduras has long relied on IFI support to meet its financing needs. In 2022, the authorities additionally resorted to $1.3 billion (4 percent of GDP) in monetary financing largely to address liquidity strains.[17] To develop new financing sources, the authorities will resume regular issuance of Treasury bonds at market rates after having halted such issuance since beginning of 2022. Financing needs are also expected to be covered by net positive IFI financing and a return to issuance in international capital markets, supported by the catalytic effect of the Fund arrangement ahead of the 2027 Eurobond repayment. To support disinflation, develop the domestic market, and reduce fiscal dominance, the program is underpinned by a zero limit on the use of central bank financing of the budget ***(continuous PC)***.

24. The authorities are taking steps to develop the local debt market and strengthen debt management practices. As an initial step, the public utility company ENEE placed government-guaranteed domestic bonds in December 2022 (0.8 percent of GDP). To strengthen predictability and coordination ahead of the domestic market issuances, the authorities will publish a schedule for 2024 Treasury bond auctions ***(end-January 2024, SB)***. To further support the development of domestic bond markets, the authorities will approve a Public Debt Policy ***(end-September 2023, SB)*** and a Medium-Term Debt Strategy ***(end-December 2023, SB)***, both to be published later this year as part of the 2024 budget framework. The authorities are committed to meeting their debt service obligations in a timely manner and not accumulate any external arrears ***(continuous QPC)***.

[17] While $300 million were repaid within the year, the remaining $1 billion—a 30-year loan with 5-year grace period at the overnight policy rate (TPM) plus a 100bps spread—became Treasury deposits, with about ⅓ of these used in 2022, mainly for servicing debt payments, and the remainder to be used for investment financing in 2023.

Authorities' Views

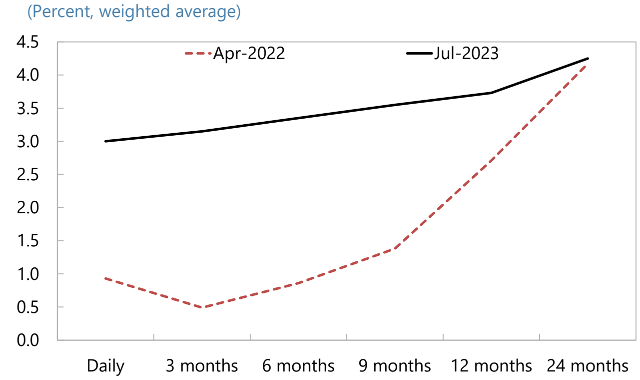
25. The authorities stressed their commitment to maintaining budgetary discipline and transparency while increasing spending on investment and social programs. The authorities share staff's view on the importance of prudent fiscal policies to maintain debt sustainability. Moreover, the authorities remain ambitious on their plans to mobilize external support to finance productive investment projects and adaptation to climate change. Importantly, they expressed their commitment to continue improving implementation capacity gradually through strengthened budget transparency and enhanced practices in public investment management. The authorities also stressed the importance of protecting and strengthening social spending, which is key to reducing poverty, while reforming the social safety net. They voiced their strong commitment to making the tax system more equitable, including through the tax reform bill. They recognized the need to further develop the domestic debt market and to diversify the sources and forms of financing. Finally, they also recognized the importance of advancing a reform of the FRL, when the political climate for achieving broad consensus for such a reform is more conducive.

B. Monetary, Exchange Rate, and Financial Sector Policies: Preserving Macroeconomic Stability

26. Sound management of the crawling band exchange rate regime—the nominal anchor for the Honduran economy—remains essential to safeguard economic stability and bolster resilience to shocks. As such, the nominal exchange rate should adjust in line with relative price differentials between Honduras and its trading partners to help maintain external competitiveness and support reserve accumulation. However, as a response to the commodity shock caused by Russia's war in Ukraine, the authorities focused strongly on containing inflation, using the exchange rate to limit the pass-through of global inflationary pressures. In addition to liquidity absorption and energy subsidies, and building on a comfortable international reserves position, the authorities have also limited movements in the Lempira, which remained broadly unchanged against the USD since 2020, despite Honduran inflation outpacing that of trading partners.

27. A proactive monetary policy remains essential to preserve stability and support the FX framework. Amid a weak transmission mechanism and limited informational content of the monetary policy rate (TPM), the BCH has conducted policy through OMOs and the interbank rate. The BCH's decisive liquidity absorption operations—raising the interbank interest rate and reducing excess reserves by 5 percent of GDP between June 2021 and September 2022—were fundamental in limiting inflationary pressures. Further

BCH Auction Interest Rates 1/
(Percent, weighted average)



1/ Refers to yields on BCH bills and bonds issued for liquidity absorption.
Sources: Central Bank of Honduras

supporting these efforts, the BCH modified the interbank interest rate corridor on August 24, 2023, increasing the Permanent Credit Facility (FPC) rate[18] by 50 bps to 4.0 percent ***(prior action)***. The BCH, however, has maintained the TPM at 3 percent since November 2020, remaining below staff's estimates of the medium-term neutral rate (**Box 4**), although these estimates are subject to uncertainty. Given ongoing upside risks to inflation, the authorities agreed on the need to continuously reevaluate the policy stance under the program and to maintain monetary policy proactive and data-driven, especially if inflation failed to decline as projected. Moreover, the authorities will monitor developments in international interest rates to maintain the consistency of monetary and exchange rate policies.

28. Further improvements to the monetary policy operational framework would strengthen its effectiveness. The BCH is committed to further enhancing the monetary policy framework and transmission. Staff and the authorities will evaluate how to integrate measures into the program in future reviews, possibly supported by Fund TA. Building on previous TA, measures could include:

- Strengthening the role of the TPM in monetary policy implementation, both in signaling the policy direction and transmitting the level of the TPM to other interest rates, including the interbank rate.
- Reviewing and enhancing liquidity management practices, including how the BCH currently withdraws liquidity through structural (medium-term) instruments—bills and bonds issued for up to two years—while managing the remaining excess liquidity by issuing one-day bills through OMOs. This could allow the interbank rate to more closely reflect the monetary policy rate.[19]
- Removing the cap on the size of daily OMOs while also reducing the amount and frequency of structural OMOs, with issuances at fixed pre-announced amounts to enable price discovery.
- Reducing the maturity profile for structural OMOs to facilitate government issuance earlier in the yield curve, supporting efforts to develop the local government bond market. Improved coordination between the Ministry of Finance and the BCH would help in this regard.
- Lengthening the maintenance period for reserve requirements to enhance the BCH's ability to forecast and manage liquidity.
- Implementing forthcoming recommendations from the Fund's Safeguards Assessment of the BCH (to be completed by the first program reviews).

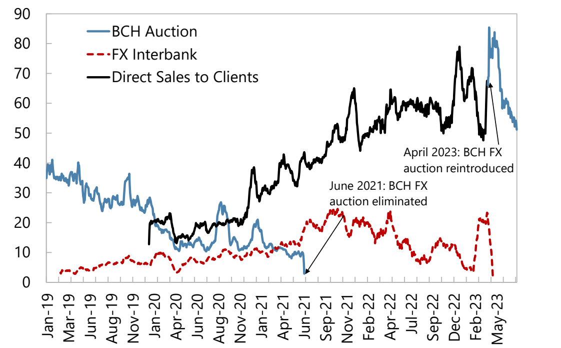
29. In response to strains in the FX market, the BCH ultimately returned to an auction system for the allocation of FX in April 2023. The interbank FX market started to experience declining turnover from late 2021. In staff's view, the declining turnover in the FX market resulted

[18] The FPC acts as a ceiling on the interbank rate, which has been the BCH's preferred instrument to guide liquidity absorption and signal the stance of monetary policy. Increasing the BCH's lending facility enables greater upward movement in the interbank rate and greater absorption/pass-through to other market rates.

[19] The latter could also allow the interbank rate to more closely reflect the monetary policy rate on an ongoing basis. Especially during the pandemic, the interbank rate deviated significantly from the policy rate, as the BCH stopped the absorption of excess liquidity.

from a combination of factors, including higher import prices, tighter global financial conditions combined with increased uncertainty over the direction of policies,[20] and the rising interest rate differential with trading partners in the context of a stable nominal exchange rate. As a result, FX supply into the market dried up and banks preferred to allocate the available FX inflows to their own (and preferred) customers rather than making them freely available, including through the interbank market. This led to an inequitable FX allocation, favoring especially large firms, prompting concern from the authorities. The BCH initially reacted through FX interventions in 2022Q4, and, in February 2023, by introducing a requirement for all banks to sell 25 percent of their FX receipts in the interbank market to increase access to FX for smaller banks with fewer exporter clients. In April 2023, the BCH reintroduced its own FX auction mechanism, thereby shutting down the interbank FX market.[21] Under this mechanism, banks and FX bureaus must surrender essentially all their FX receipts,[22] of which at least 80 percent are returned to economic agents the next business day through the BCH's FX auction.

Foreign Exchange Market Daily Turnover
(Millions of US$, 14-day moving average)



Sources: Central Bank of Honduras

30. Consistent monetary and exchange rate policies are key to safeguarding internal and external stability. As inflation returns to the BCH's reference range, policies should prioritize preserving competitiveness and external stability, including through the management of the crawling band. Such efforts will also help protect Honduras' international reserve position. The BCH's recent increase in the FPC rate to 4 percent is a welcome step to narrow the interest rate differential with peer countries, given the importance of managing interest rates also with a view of supporting the maintenance of the crawling band. Importantly, the authorities remain committed to preserving the competitiveness of the real exchange rate. In this context, the authorities have also committed to work with Fund staff, supported by TA to (i) evaluate and strengthen the crawling band regime; and (ii) diagnose the measures necessary to improve the efficiency of FX allocation.[23] Staff will discuss TA findings with the authorities, with specific measures to be incorporated into the program. On these bases, the authorities are committed to implementing measures, during the time of the program, to allow for a gradual transition to a balanced, competitive, and efficient system for FX allocation that allows for price discovery and reflects FX supply and demand. This should enable an eventual unwinding of the FX surrender requirement. It will be also important to allow for any

[20] As in other countries in the region, EMBI spreads started to increase significantly in late 2021 (see Figure 6), with periods of volatility in Honduran spreads likely reflecting uncertainty about the authorities' policy direction.

[21] Requests for FX of less than US$10,000) may still be filled with commercial banks outside the BCH auction system.

[22] The reintroduction of the surrender requirement for exchange agents in April 2023 is currently under CFM assessment under the Fund's Institutional View.

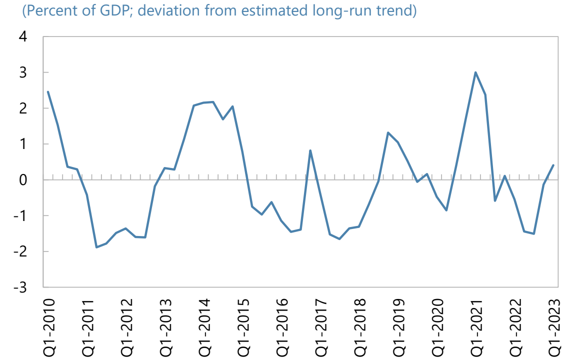
[23] Whereas past TA in these areas focused on an eventual transition to an inflation targeting regime with a more flexible exchange rate, the authorities in the current context have expressed a clear preference to maintain the crawling band, with TA focused on strengthening that regime.

necessary macroeconomic policy adjustments to preserve competitiveness and bolster resilience to shocks. The program monitors net international reserves and net domestic assets of the BCH through ***QPCs***. Reserve accumulation is projected to resume in 2024 supported by (i) the expected reduction in FX sales to oil importers; (ii) an increase in net disbursements to the public sector, mainly by official sources including the Fund; and (iii) net private capital inflows supported by strengthened market sentiment.

31. Honduras maintains two longstanding multiple currency practices and one exchange restriction subject to Fund jurisdiction. The first multiple currency practice (MCP) stems from a potential deviation of more than 2 percent between the exchange rate required to be used for certain FX transactions (the official exchange rate of the specified previous day) and the official exchange rate in force on the day on which these transactions occur. The second MCP arises from a similar potential deviation between the exchange rate at which agents purchase FX at the BCH auction and the official exchange rate in force on the day when the FX auction takes place. The authorities have requested temporary approval of these two MCPs, which are maintained for non-balance of payment reasons.[24] In addition, Honduras maintains one exchange restriction arising from restictions on the availability of FX for payments and transfers for current international transactions, as a law requires the BCH to reject participation in its FX auctions by exporters who have not duly repatriated export proceeds from two or more export transactions within required timeframes.

32. Continued close monitoring of the financial sector is warranted. Credit growth has been robust during the recovery from the pandemic, and the banking sector remains stable. Recent stress tests by the National Banking and Insurance Commission (CNBS) confirm the resilience of the sector to significant shocks. To foster more equitable and better access to credit, including for small entrepreneurs and farmers, the CNBS has recently taken various measures, including streamlining documentation requirements for loan applications from these segments. The authorities should proactively use macroprudential instruments as necessary, taking into consideration high credit growth, a credit gap that has turned positive, and high household debt. The authorities should carefully monitor the associated risks of an expansion of credit to underserved sectors such as farming and micro-enterprises. The authorities have implemented most of the recommendations of the 2016 Financial Sector Stability Review (**Annex V**).

Estimated Credit-to-GDP Gap
(Percent of GDP; deviation from estimated long-run trend)



Sources: Central Bank of Honduras; and IMF staff calculations.

Authorities' Views

33. The authorities reiterated their commitment to implementing policies that support the

[24] The authorities have also confirmed that exchange rate deviations have never surpassed the 2 percent threshold.

crawling band regime. The authorities emphasized the importance of their monetary and exchange rate policies in contributing to ongoing disinflation, while also allowing for more growth and financial inclusion. They considered that declines in inflation pressures reflect dissipating external supply shocks and that the measures they had adopted—including energy subsidies and liquidity absorption—were successful in containing the temporary impact of these shocks. They noted that the increase in interest rates brought about by the BCH's absorption of excess liquidity had struck a fine balance between containing inflation and supporting inclusive growth, which was much needed given the lingering impacts of the pandemic and 2020 tropical storms on the population. They emphasized their readiness to take necessary measures to ensure that inflation remained on a downward path. On the exchange rate regime, the authorities believed that exchange rate stability has helped to contain inflationary pressures and consider the Lempira to be fairly valued. They underscored that the decline in interbank FX market trading volumes from 2022 was associated with an inequitable allocation of FX, with smaller bidders finding it difficult to access FX. They emphasized that the reinstatement of BCH FX auctions and surrender requirements for exchange agents has stabilized the FX market and reduced speculative pressures, while improving equitable access to FX. There was agreement on the importance of bolstering financial inclusion, while safeguarding the stability of the banking sector.

C. Energy Sector Reform and Building Resilience to Climate Change

34. Energy sector reforms to ensure the financial viability of the sector and guarantee the reliable provision of electricity are essential to entrench fiscal sustainability and improve the business environment. The authorities' focus on reforming and strengthening the energy sector is a key step in this direction. The authorities aim to reduce losses in the sector through higher investment, improved enforcement and collection, and better management of electricity distribution. This will have important fiscal benefits—including greater government revenues through the sale of electricity and reduced fiscal outlays to cover losses—that would increase resources available for energy sector investment and, more broadly, for other needed infrastructure investment and social spending. Moreover, more reliable electricity supply would reduce economic uncertainty and improve the business environment.

35. The main player in Honduras' electricity sector is the state-owned electricity company (ENEE). After a decade of reforms and plans to reduce ENEE's electricity losses, challenges remain in the provision of electricity, which hinder medium-term economic growth. Moreover, ENEE remains a drain on fiscal resources. Although its operational financial losses were reduced in 2022, they remained equivalent to 0.8 percent of GDP, and its liabilities exceeded 12 percent of GDP at end-2022. Financial losses are driven by a significant share of electricity output not being collected from consumers. Technical losses—largely due to poor network infrastructure—account for 15 percent of the total electricity output and non-technical losses—stemming from weak management, low debt collection, fraud, and billing errors—account for another 23 percent.

36. A new energy law reflects the authorities' new vision for maintaining ENEE as an integrated monopoly while implementing reforms to increase its efficiency. The new law, approved in May 2022, reverses much of the 2014 General Electricity Law, which had envisaged an unbundling of ENEE into generation, transmission, and distribution functions and subsequent opening to private sector competition in each area. The new law also defines access to electricity as a human right and outlines its free provision to poor households (¶16). While maintaining an integrated ENEE, the authorities are starting to work towards implementing a strong administrative separation between its three functions, including their management as separate divisions, by implementing, as a first step, a more robust IT infrastructure. The transformation of ENEE into a viable public sector entity will require strong leadership from independent management, which the government has yet to appoint, together with professional oversight by its board. In this context, it will also be essential to ensure a smooth reintegration into ENEE of all distribution activities, which had been previously outsourced to a private company.[25]

37. A more decisive implementation of the National Loss Reduction Plan (NLRP) will be critical to making ENEE financially sustainable. Launched in 2022, the NLRP seeks to minimize losses and address inefficiencies through measures that include (i) upgrading the aging electricity distribution network; (ii) installing advanced metering systems; and (iii) preventing theft by deploying crews of workers for real-time theft monitoring. While there are tentative signs that ENEE's financial position (and consumers' payment discipline) is starting to improve, lasting change will depend on the steadfast implementation of the NLRP, which targets a reduction in total losses to under 20 percent (from 38 percent) over four years starting in 2023. To this end, the authorities are ramping up deployment of task forces to address technical losses by regularizing consumers and reducing fraud, including by installing new meters, starting with the circuits with highest losses and larger consumers. In this context, staff encouraged the authorities to work with international partners on assessing ways and designing measures to strengthen the NLRP. The program monitors the success of the NLRP through an ***IT*** on the percentage of energy lost by ENEE in energy distribution.

38. Swift progress should also be made on advancing other reforms to strengthen viability of the electricity sector and ENEE.

- Contracts with private electricity generators are being renegotiated to reduce costs and address irregularities. Agreement has been reached on ¾ of these contracts (23 of 32) and is expected to yield annual savings for consumers of around 0.2 percent of GDP.
- ENEE has adopted a bond issuance strategy to repay arrears to private generators. A first issuance of 0.8 percent of GDP of government-guaranteed ENEE bonds took place in December 2022, substantially reducing the arrears stock to 1.2 percent of GDP. Further issuances for a similar amount are planned for the remainder of 2023 to finance most of ENEE's operational

[25] In 2016, the Honduran government outsourced all distribution activity to a private company (*Empresa Energia Honduras*, EEH) under a contract set to expire in August 2023. The contract has been under intervention since 2019, with the authorities claiming a breach of contract. ENEE currently continues to prepare itself for reintegrating all distribution activities (including billing, customer service, etc.). Until this process is concluded, ENEE continues to collaborate with EEH in a transitional arrangement.

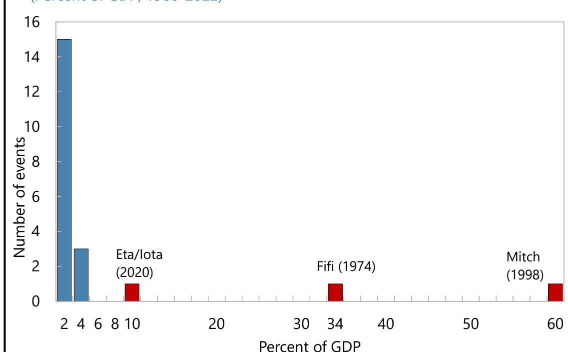
deficit for the ongoing year and thus forestall renewed arrears accumulation. The program will monitor the stock of ENEE's domestic arrears (***QPC***) to ensure a continued gradual decumulation.

- The authorities are working with banks to reduce the cost of servicing ENEE's domestic debt. This debt of 6.3 percent of GDP is largely in the form long-term bonds indexed to inflation.[26]
- Updating the value added in distribution (VAD) will ensure that tariffs better reflect the actual cost of distribution.[27]

39. The authorities should clarify the role of private investors to spur investment and thus ensure a sufficient supply of electricity and a modernization of the sector. While the authorities have stressed their interest in private investment in the sector, some private investors have interpreted the new energy law as allowing for the nationalization of plants and ruling out private investments in subsectors where public ownership is less than 50 percent. The law also removed the independence of the energy sector regulator and the system operator. Moreover, it increased uptake thresholds substantially so that now only very large firms are allowed to directly purchase electricity from private generators, which may hinder investment in other sectors and reduce growth, while electricity supply from ENEE remains prone to outages. A favorable and swift finalization of ongoing contract renegotiations with private generators together with the establishment of independent management at ENEE would also boost private investor confidence in the sector.

40. Swift and decisive actions are essential to tackle existing vulnerabilities to extreme weather and additional climate change challenges. Extreme climate events in Honduras have generated annual average losses equivalent to 6.3 percent of GDP during 1960-2022 (**Annex II**), highlighting the importance of strengthening disaster preparedness and resilience. Climate change also has negative implications for agricultural and energy production and increases risks of food insecurity. A Climate Public Investment Management Assessment (C-PIMA), planned for late 2023, will help the authorities establish a climate and disaster resilience strategy.

Extreme Climate Event Damages
(Percent of GDP, 1960-2022)



Source: EM-DAT; and IMF staff calculations.

41. The authorities approved a National Adaptation Plan (NAP) in 2018 and updated their Nationally Determined Contribution (NDC) plan in 2021. The NAP comprises 13 objectives and seeks to explore complementarities between mitigation, adaptation, and sustainable development goals, including poverty reduction, across multiple sectors including infrastructure, energy,

[26] This is included in SNPF domestic debt in the DSA.

[27] The tariff in Honduras already fully supports cost recovery, with the only limitation being that only 15 percent of technical and non-technical losses can be passed on to consumers via tariffs. The VAD study will update the cost of distribution, improving on previous estimates.

agriculture, and natural resources **(Box 5)**. Key targets of the NDC plan include reducing emissions by 16 percent relative to the business-as-usual (BAU) level by 2030 and restoring 1.3 million forest hectares (300,000 more than the previous target). However, these mitigation targets under the NDC would still need to be mapped onto a detailed mitigation plan that can be quantified and evaluated periodically. On the adaptation front, the NDC focuses on the creation and strengthening of institutions, strategies, plans, and policies in key sectors with a focus on social inclusion (e.g., increased labor force participation to find climate solutions for women, youth, and indigenous population).

42. The authorities are advancing in their climate agenda. The authorities have taken steps to integrate climate risks into fiscal planning, strengthen public investment and infrastructure resilience through the identification of priority projects in highly vulnerable areas, and establish committees for the analysis of climate vulnerabilities within the framework of the Climate Change Law approved in 2014, and the National Climate Change Strategy. Close cooperation with the IMF and other international partners is expected to broaden the scope and impact of this critical policy agenda.

Authorities' Views

43. The authorities concurred on the need to strengthen climate-related policies, enhance the resilience of the energy sector, and develop resilient infrastructure. The authorities viewed the previous administration's push for privatization in the energy sector as a cause for the deterioration of ENEE's financial position. They cited governance weaknesses which led to an unfavorable distribution contract with the company EEH and the approval of many generation contracts with irregularities and at above-market prices. They emphasized the need to renegotiate these contracts—to lower electricity prices for consumers as well as improve governance—and highlighted their determination to satisfactorily finalize these negotiations as soon as possible. They also emphasized the importance of developing infrastructure, such as the construction of dams for the Sula Valley, and implementing programs to mitigate the adverse effects of climate change on the most vulnerable. As a result, the energy sector features prominently in their public investment strategy with the ambition of starting to implement in the next years US$5.5 billion (16 percent of GDP) in priority investments identified in generation, transmission, and distribution. In line with these priorities, the authorities expressed interest in seeking additional Fund financing under the Resilience and Sustainability Fund (RSF) at a future program review.

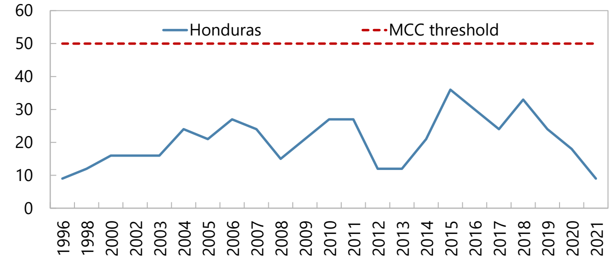
D. Improving AML/CFT and Governance and Combatting Corruption

44. Perception-based indicators suggest that corruption increased considerably in the last years of the previous administration. The current authorities are committed to improving transparency and governance and combatting corruption, including to qualify for the Millennium Challenge Account, a U.S. foreign assistance agency that provides grants to reduce poverty through sustainable economic growth. Honduras already meets all requirements to qualify for the

Millennium Challenge Account except for the perceptions-based control of corruption indicator, whose last available 2021 value, however, does not yet reflect the achievements under the current government.[28]

Control of Corruption Indicator 1/

(Percentile in relevant Millennium Challenge Corporation (MCC) comparator group)



1/ Index captures perceptions of the extent to which public power is exercised for private gain. Rankings are subject to uncertainty around point estimate. Ranking reflects relative performance of HND against other countries with similar GNI per capita, not HND's absolute performance.
Sources: Worldwide Governance Indicators (WGI), which summarizes views on governance according to surveys of enterprises, citizens, and experts.

45. In line with their policy agenda, the authorities have taken important actions to fight corruption and improve transparency. They abolished in early 2022 a secrecy law which had restricted access to many public documents and, in August 2023, abolished Decree 116-2019 on the departmental fund through which Congress members have been directing budgetary resources, creating corruption risks, and which limited the investigative power of the attorney general. Also, they have implemented an internal results-based management system for the entire government and are considering making a version of it publicly available. An executive decree has been adopted to increase financial transparency among public officials and combat illicit enrichment.

46. Congress approved unanimously in July 2023 key legislation to strengthen the AML/CFT framework. This legislation eliminated Decree 57-2020 and modified Decree 93-2021, which had diluted the penal code and its AML/CFT safeguards and made prosecution of corruption-related crimes difficult. Inter alia, the new legislation revises the definitions of money-laundering and politically-exposed persons to make them more consistent with international standards by aligning them with the FATF and UN Conventions, and reverts previous reductions in sentences for some corruption-related crimes.

47. Gradual progress has continued in the establishment of an anti-corruption commission (CICIH, The International Commission Against Impunity in Honduras) since the authorities started engaging with the UN on this process in February 2022. Building on the December 2022 memorandum of understanding (MoU) between the authorities and the UN to agree on the preparatory process, a UN expert group has been engaging with the authorities to produce a diagnostics report, which would form the basis for negotiations to formally establish the CICIH. Such an agreement could require certain further legislative changes to ensure that the CICIH can assist effectively in prosecuting corruption and strengthening the judicial system. This will, in turn, require continued work to build broad support in Congress. Support for an independent CICIH remains strong, including from Honduran civil society.

[28] The requirements that Honduras already meets relate to democratic rights indicators and ranking sufficiently highly on 11 of 20 indicators (with a minimum of 10 required). On the control of corruption indicator, Honduras needs to rank above the median of its comparator group of countries with a similar GNI per capita.

48. Looking ahead, the authorities' program features a strong agenda on transparency, governance, and AML/CFT. The nationwide implementation of an electronic asset declaration system for public officials will start early next year ***(end-February 2024, SB)***; a pilot has already been successfully implemented. The authorities have also submitted to Congress legislation to create a comprehensive beneficial ownership registry, which is expected to be approved by December 2023 and made operational by December 2024 ***(SBs)***. The authorities also plan to submit to Congress a Law on Simplification of Administrative Procedures by June 2024 ***(SB)*** and have already identified several administrative processes to digitize. This should help improve the business environment alongside ongoing work towards modernizing the legal frameworks governing digital signatures, telework, cybersecurity, and data protection. Building on the improvement to the AML/CFT framework from July, the authorities are working on further legislation to implement additional FATF recommendations. Finally, the Council of Ministers is considering adopting a National Transparency and Anti-Corruption Strategy.

Authorities' Views

49. The authorities underscored their steadfast commitment to transparency and good governance. The authorities are firmly committed to the reforms described above, highlighting the deterioration during the previous government and representing a break with past practices. They reiterated their interest in TA from the Fund and other organizations to achieve their ambitious reform agenda in this area. Finally, they expressed hope that their actions would not go unrecognized in their pursuit of reestablishing access to the U.S. Millennium Challenge Account, which requires improvement in a control of corruption indicator.

PROGRAM MODALITIES

50. Blended Fund support under a 36-month EFF and a 36-month ECF arrangements is appropriate to help meet Honduras' balance of payments (BoP) needs. Staff proposes an access level of 250 percent of quota, or SDR 624.5 million, split between the ECF arrangement (SDR 208.2 million, 83.3 percent of quota) and the EFF (SDR 416.3 million, 166.7 percent of quota) and equally phased across semi-annual reviews. Fund financing will be used for indirect budget support, and staff will ensure that the required MoU or loan agreement between the BCH and Ministry of Finance is in place. Staff will monitor the program through QPCs and ITs, standard continuous PCs (MEFP (Appendix I, Attachment 1) and TMU (Appendix I, Attachment II), as well as SBs (MEFP, Table AI.1) to support reforms in key areas, consistent with implementation capacity.

51. The level of access is justified by the actual, prospective, and protracted BOP needs. The program will support front-loading social spending and filling urgent infrastructure gaps, further exacerbated by the pandemic and climate shocks, while seeking to address distortive income tax exemptions, in the context of a more gradual fiscal adjustment. Without IMF financing, staff projects international reserves to fall below adequate levels. The proposed level of access is commensurate with the projected remaining BoP financing need, and further justified by the strength of the program, the authorities' commitment to reforms and capacity to repay the Fund (see also ¶53).

52. Financing assurances. The program is fully financed for the first 12 months, with good prospects of full financing for the remainder of the program. The program is expected to support access to international capital markets and to catalyze donor financing, including from multilaterals such as CABEI, IADB, and the World Bank, with IMF financing projected to fill 18 percent of the external financing gap over 2023-26 (Table 10).

53. Honduras' capacity to repay the Fund remains adequate. Existing and prospective Fund credit outstanding is expected to reach 273.9 percent of quota by end-2026, before declining to 155.6 percent of quota by 2031. Repayments to the Fund increase during 2024-25 and are projected to peak at 1.7 percent of exports and 2.9 percent of gross reserves in 2024, before declining to 0.6 percent and 1.1 percent respectively by 2028.

54. Risks to the program. Program implementation challenges are significant, largely stemming from the identified risks to the baseline (¶13). In addition, policy slippages and the complex domestic political environment, including potential difficulties in shoring up sufficient support in Congress, could impact the adoption of important legislation, such as the LJT (¶20). Still limited budget execution capacity could lead to delays in the authorities' ambitious public investment plans and to the emergence of domestic arrears. Strengthening the monetary and foreign exchange policy frameworks may take longer than anticipated, delaying the expected further enhancements of the country's resilience to shocks. Finally, and recognizing their inherent complexity, energy sector reforms, including the loss reduction plan, could fall short of the anticipated outcomes. Mitigating these risks are the strength of program conditionality, the authorities' strong ownership of reforms, an adequate level of international reserves, prudent phasing of purchases, strong support from the international community, and the country's track record under previous arrangements.

55. Safeguards Assessment. An updated assessment will need to be completed prior to the first review of the program. Progress in implementing the 2019 safeguards recommendations has been considerable, including to strengthen the BCH's financial reporting and internal audit mechanism. On the other hand, progress in legal reforms to strengthen the BCH governance framework has been limited. Staff will follow up on this issue in the updated assessment.

STAFF APPRAISAL

56. Honduras has shown resilience to a series of external and domestic shocks. Following the pandemic and tropical storms in 2020, the economy has rebounded strongly, supported by domestic demand, remittances, and a resilient export sector. Elevated inflation, driven in large part by external shocks, is now abating. The authorities' prudent policies, including the maintenance of public debt on a downward path and efforts to contain inflation, have underpinned Honduras' macroeconomic stability. The authorities have taken important steps to improve the AML/CFT, governance, and transparency frameworks, including through the elimination of trust funds and amending relevant AML/CFT legislation.

57. Nevertheless, the Honduran economy faces significant social and structural challenges. Honduras remains one of the poorest countries in the Western Hemisphere, reflecting limited investment, a narrow export base, structural bottlenecks in the energy sector, and weak governance and institutions. Poverty also remains pervasive. These challenges are further exacerbated by Honduras' vulnerability to extreme climate events.

58. Strengthened revenue mobilization and continued prudent spending policies are necessary to create space for additional social and infrastructure investment, while preserving debt sustainability. While maintaining public debt on a downward path and gradually reducing the fiscal deficit, the authorities' program aims to create additional fiscal space for increased social spending and investment. To this end, the authorities have prepared an ambitious tax reform to support revenue mobilization and reduce distortive tax exemptions. A wide-ranging agenda to strengthen tax administration will also continue to be implemented. A planned social registry will be essential to expand social assistance in a targeted manner. To increase the efficiency of public investment, the authorities aim to improve the planning, selection, and monitoring of public investment projects.

59. Enhancements to monetary and exchange rate policies will support price stability, maintain external competitiveness, and bolster resilience to shocks. Consistent monetary and exchange rate policies are necessary to support the crawling band exchange rate regime. To this end, the authorities are committed to maintaining a proactive and data-driven monetary policy and to monitoring developments in international interest rates. To support these effects, the authorities should take steps to enhance monetary policy transmission. The implementation of the crawling band regime should be enhanced, and the efficiency of FX market allocation should be improved. The authorities plan to work with staff to identify such measures. The authorities' program will also help maintain an adequate international reserve position.

60. Accelerating energy sector reforms will be essential to preserve macroeconomic stability, limit fiscal risks, and improve the business environment. Difficulties in the reliable provision of electricity are an impediment to investment and economic growth, while financial losses in the state-owned electricity company are a fiscal drain. The authorities are working to reduce losses in the provision of electricity and reduce ENEE's debt service costs and arrears. The authorities should also take steps to clarify the role of private investment in the energy sector, including through renegotiations of contracts with private generators. The authorities should also further their efforts to increase preparedness and build resilience to the effects of climate change.

61. Continued improvements to AML/CFT, governance, and transparency are needed, including to reduce corruption risks. While progress in establishing the anti-corruption commission CICIH has been slow, the authorities remain steadfast in their commitment to strengthening governance and transparency and combat corruption. In addition to the elimination of fiscal trust funds, the authorities have taken steps to realign the AML/CFT framework with international standards, improve access to public documents and increase financial transparency among public officials. The authorities plan to further increase transparency on the assets of public officials while creating a comprehensive beneficial ownership registry. To improve governance, the authorities plan to simplify administrative procedures and increase digitalization.

62. Given the strength of the authorities' program, staff fully supports the request for an arrangement under the EFF and ECF for SDR 624.5 million. The program will support critical social spending and infrastructure investment needs, while underlying fiscal reforms will reinforce prudent fiscal policies that maintain public debt on a downward path. The authorities' structural agenda will also make significant progress on improving governance and transparency. While policy implementation risks exist, the authorities have already made significant progress on their fiscal and structural reform agenda, underscoring their commitment to program objectives.

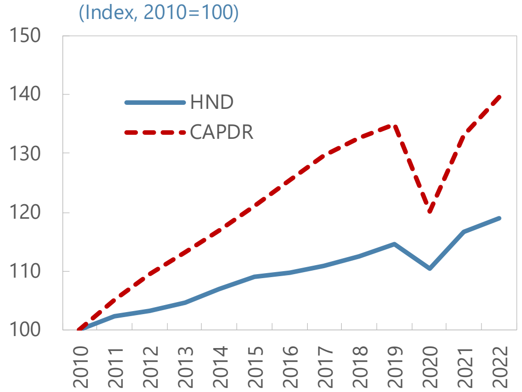
63. Staff supports the authorities' request for temporary approval of multiple currency practices subject to Fund jurisdiction under Article VIII, Section 3. The authorities have requested temporary Fund approval of the two existing MCPs. Staff supports the request, as the measures are imposed for non-BoP reasons and do not materially impede BoP adjustments, harm the interest of other members, or discriminate between Fund members. The authorities have also committed to removing the exchange restriction during the course of the program within the ambit of their planned reforms to the FX system.

64. It is recommended that the next Article IV consultation take place in accordance with the Decision on Article IV Consultation Cycles (Decision No. 14747(10/96), as amended).

Figure 1. Honduras: Long-Term Macroeconomic Trends, 2010-2022

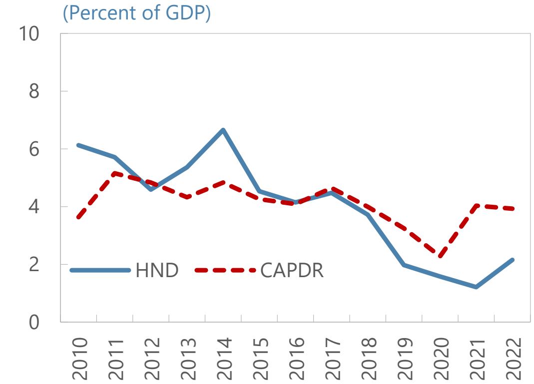
Income growth has lagged peers…

GDP per Capita, PPP
(Index, 2010=100)



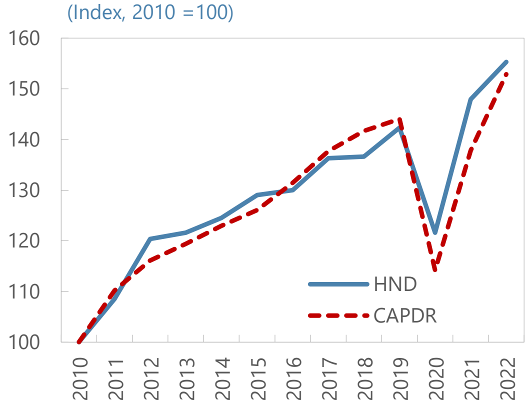
…and FDI inflows have largely remained on a downward trend…

Foreign Direct Investment
(Percent of GDP)



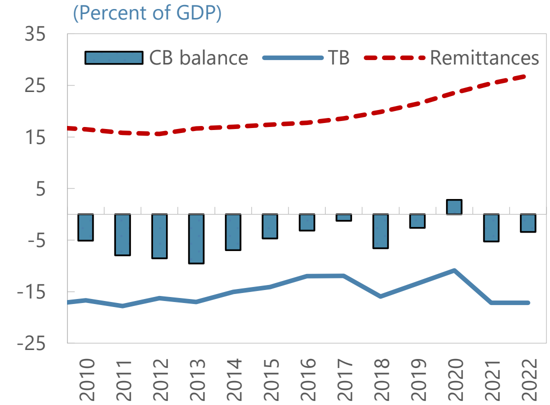
…and while export performance has rebounded sharply…

Export Volumes
(Index, 2010 =100)



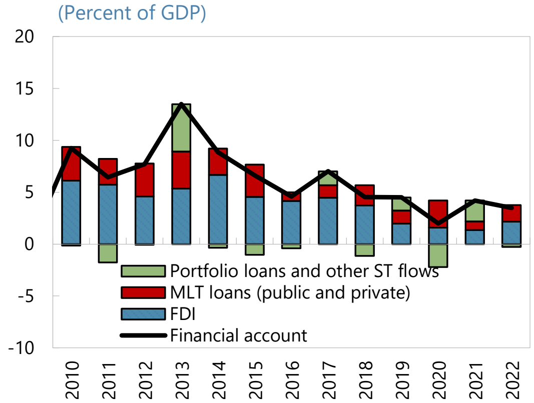
…heavy reliance on remittances has continued in the context of persistent trade deficits.

Current Account Balance
(Percent of GDP)



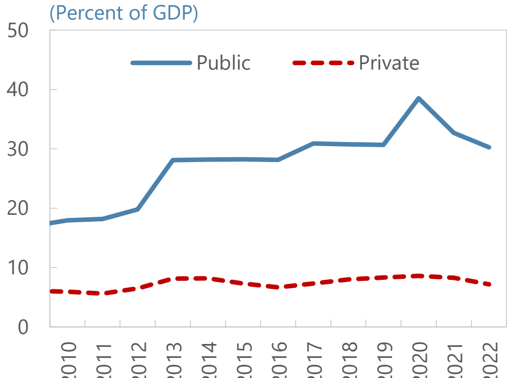
The lack of non-debt external financing constrains economic activity.

Financial Account
(Percent of GDP)



The government has turned to external borrowing, mostly from multilateral sources.

External Debt
(Percent of GDP)

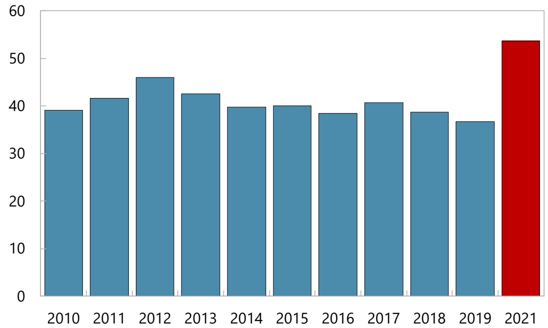


Sources: Central Bank of Honduras, IMF WEO database, IMF BOP database, and IMF staff calculations.

Figure 2. Honduras: Social Indicators

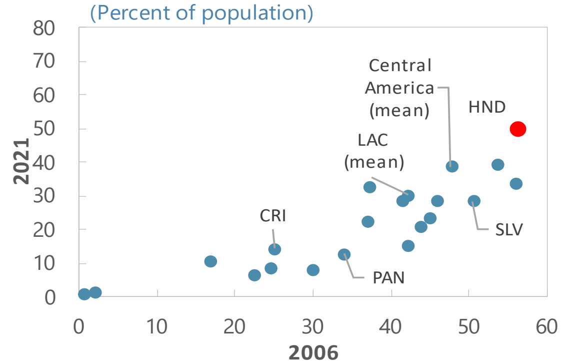
The pandemic reversed a small downward trend in poverty indicators…

Extreme Poverty 1/
(Percent of households)



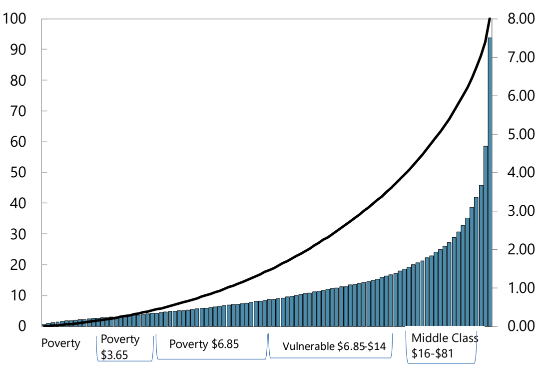
…and Honduras remains one of the poorest countries in LAC…

Poverty Headcount Ratio at $6.85 a Day (2017 PPP)
(Percent of population)



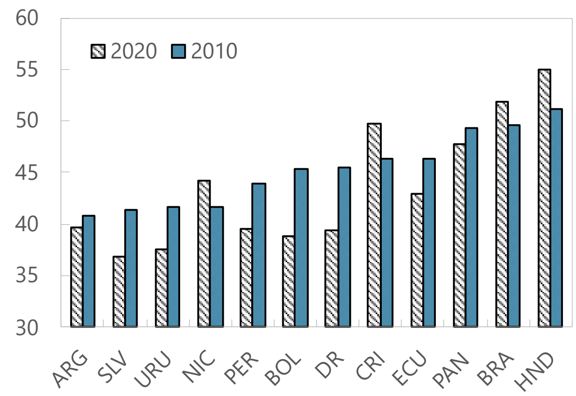
…with those living in poverty receiving a very low share of income…

Income Distribution, 2019
(Cumulative distribution, LHS; Income share, RHS)



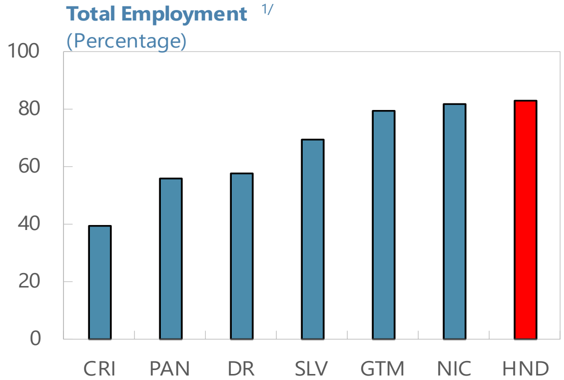
…making Honduras one of the most unequal countries in the Western Hemisphere.

GINI Index
(From 0 to 100, where 0= perfect equality)



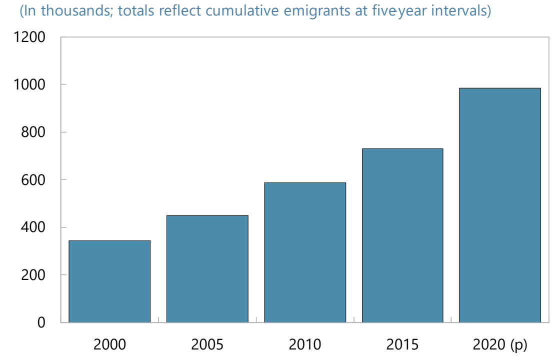
Most people work outside of formal employment…

Proportion of Informal Employment in Total Employment 1/
(Percentage)



…while poverty, high crime, and limited opportunities have been factors driving large migration.

Total Number of Emigrants at Mid-Year
(In thousands; totals reflect cumulative emigrants at fiveyear intervals)

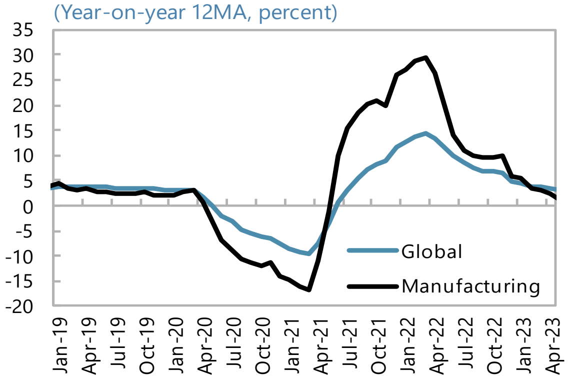


1/ Based on national definition. No data are available for 2020, after which there was a methodological change.
Sources: INE Honduras, WB WDI database, WB LAC Equity Lab, and Migration Data Portal; and IMF staff calculations.

Figure 3. Honduras: Key Recent Developments, 2019-2023

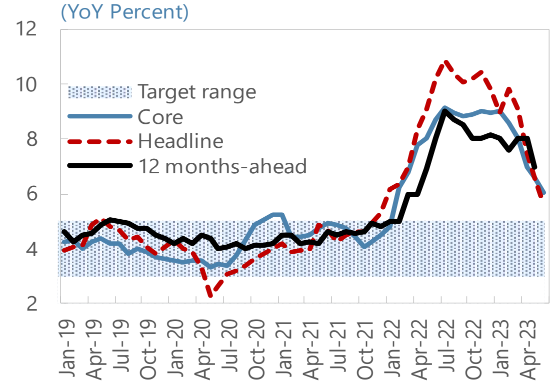
After a sharp post-Covid rebound, growth has moderated…

Monthly Economic Activity Index
(Year-on-year 12MA, percent)



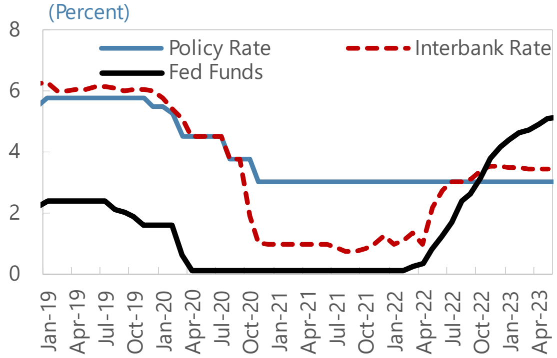
…while the global commodity price shock led to a surge in inflation, now abating.

Inflation and Inflation Expectations
(YoY Percent)



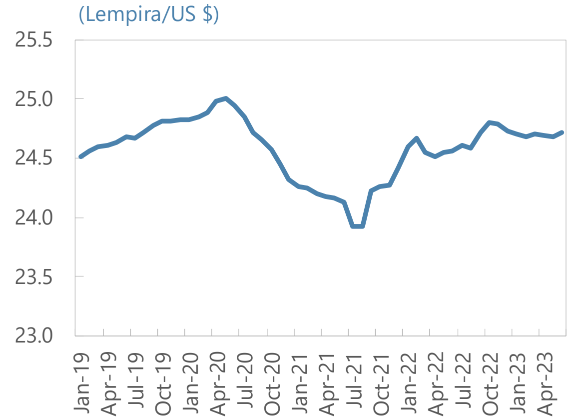
Monetary policy tightened only through interbank rates, and less than in the U.S. and peers, …

Policy and Interbank Rates
(Percent)



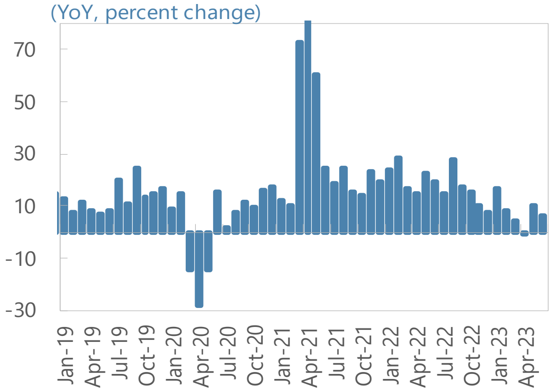
…and a stable exchange rate has limited pass-through but has also led to strains in the FX market.

Nominal Exchange Rate
(Lempira/US $)



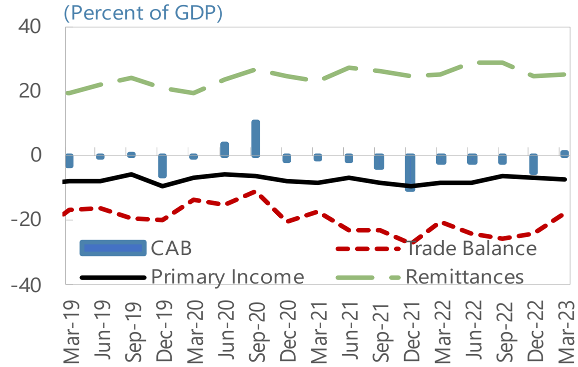
Strong remittance inflows have been critical to support domestic incomes…

Remittances
(YoY, percent change)



…but have also fueled strong domestic demand and imports, leading to a deterioration in the trade deficit.

Current Account Developments
(Percent of GDP)

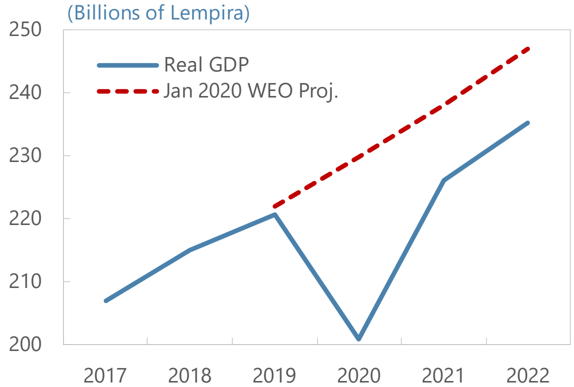


Sources: Central Bank of Honduras, Haver Analytics, and IMF staff calculations.

Figure 4. Honduras: Real Sector Developments

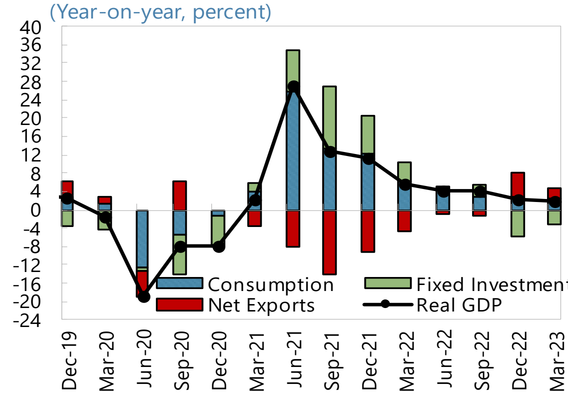
Real GDP has surpassed pre-COVID levels but remains below the prior trend.

Real GDP
(Billions of Lempira)



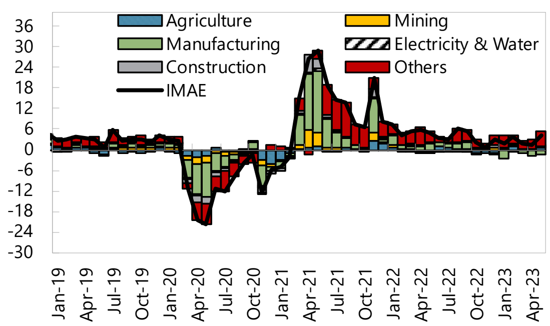
Strong consumption has remained a key driver of growth…

Contributions to Growth
(Year-on-year, percent)



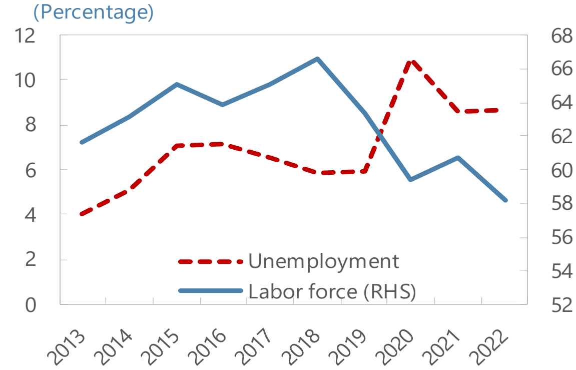
…and activity has been led by manufacturing, the maquila sector in particular, but which has slowed since late 2022.

Contributions to Index of Monthly Economic Activity
(Percent)



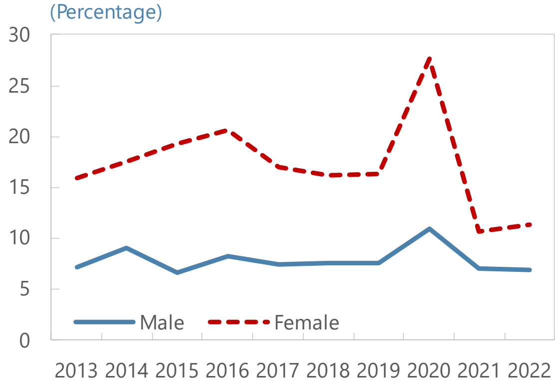
The labor market has not fully recovered from a sequence of shocks…

Unemployment and Labor Force Participation
(Percentage)



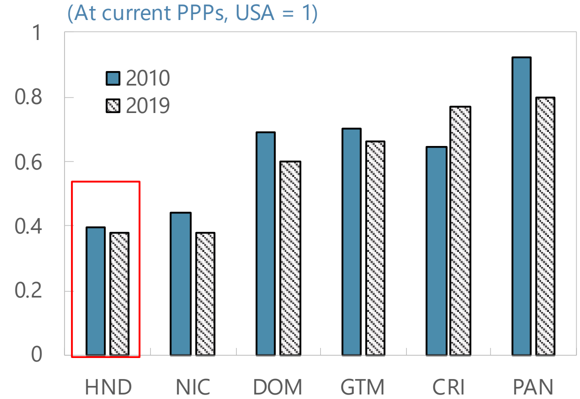
…and female unemployment remains high.

Unemployment Rate by Gender
(Percentage)



Improving productivity will be critical to boost potential growth.

Total Factor Productivity
(At current PPPs, USA = 1)

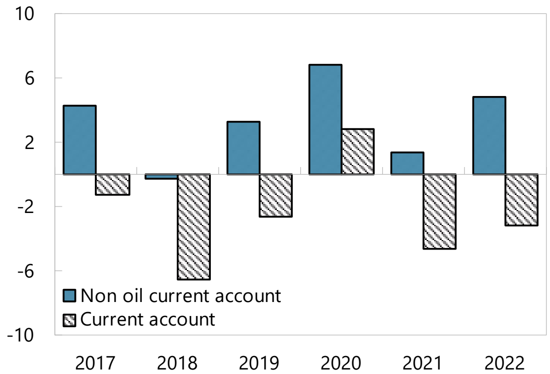


Sources: Central Bank of Honduras, IMF WEO, Haver Analytics, , and IMF staff calculations.

Figure 5. Honduras: External Sector Developments

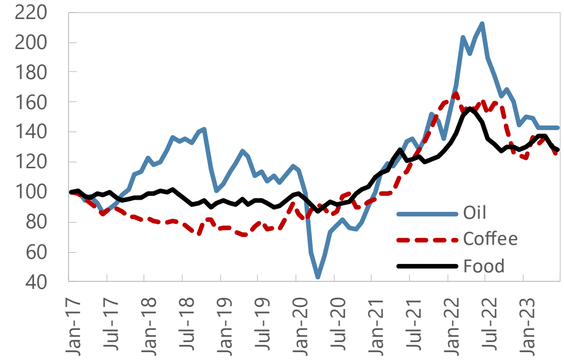
While narrowing in 2022, current account deficits persist…

Current Account Balance
(In percent of GDP)



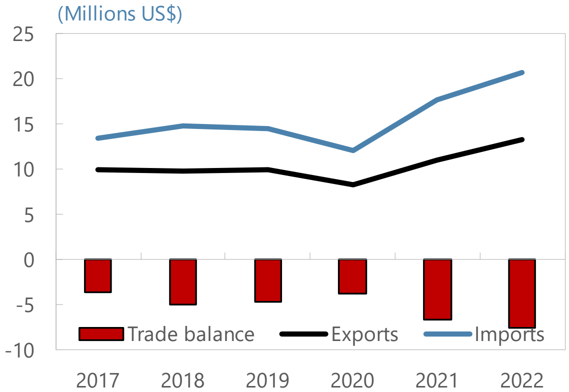
…driven recently by the surge in global commodity prices, food and energy in particular…

Prices of Coffee, Oil & Food
(Index, 2017=100)



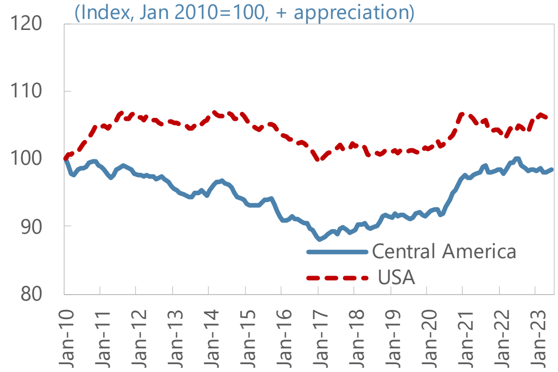
…leading to widening trade deficits…

Evolution of Trade Flows
(Millions US$)



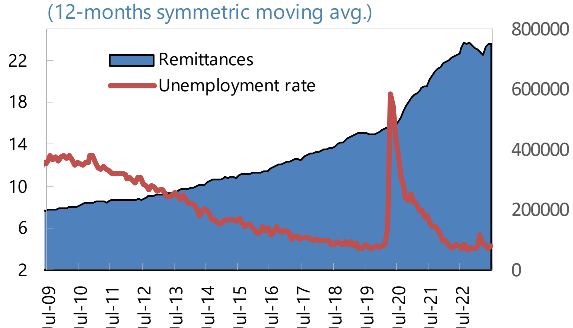
…in the context of some real appreciation from higher domestic prices.

Real Effective Exchange Rate
(Index, Jan 2010=100, + appreciation)



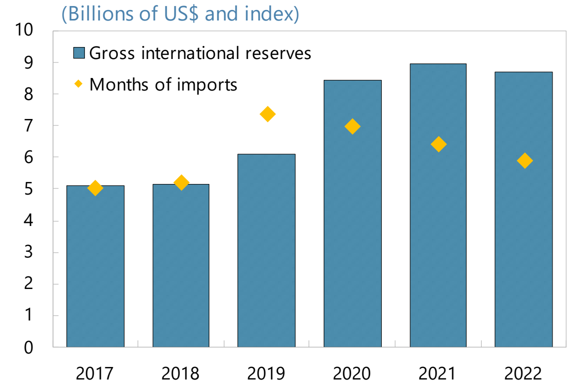
A strong U.S. labor market has supported the flow of remittances.

U.S. Remittances to Honduras and U.S. Hispanic Unemployment Rate
(12-months symmetric moving avg.)



Despite the recent FX market pressures, the FX reserve position remains comfortable.

Gross International Reserves
(Billions of US$ and index)

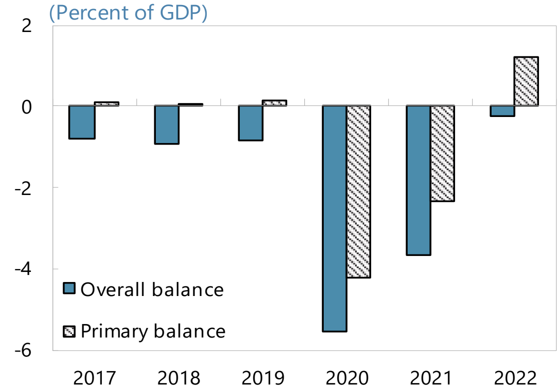


Sources: Central Bank of Honduras, Haver Analytics, IMF WEO; and IMF staff estimates and projections.

Figure 6. Honduras: Fiscal Developments, 2017-2023

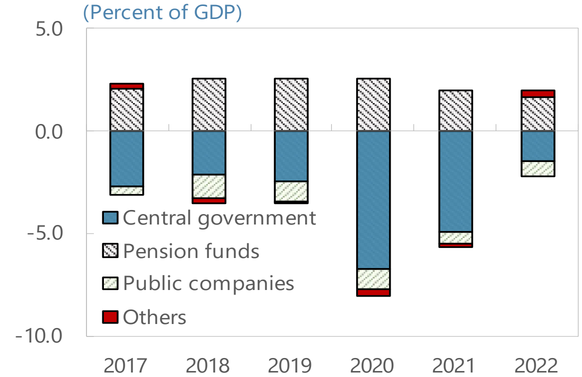
Post-pandemic fiscal deficits are shrinking supported by the economy recovery...

Nonfinancial Public Sector
(Percent of GDP)



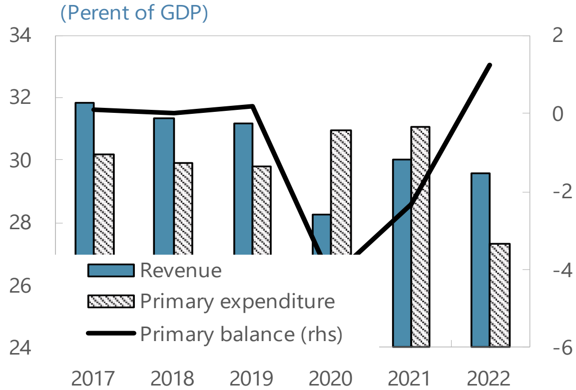
...and largely driven by consolidation of the central government.

NFPS Balance, by Sector
(Percent of GDP)



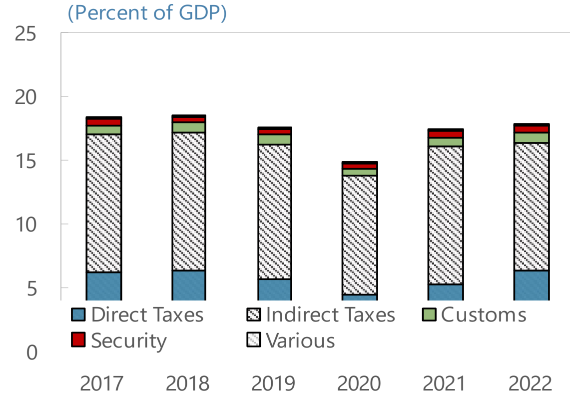
The primary balance reached a surplus in 2022 from a continued decline in post-COVID spending ...

NFPS: Revenue and Expenditures
(Perent of GDP)



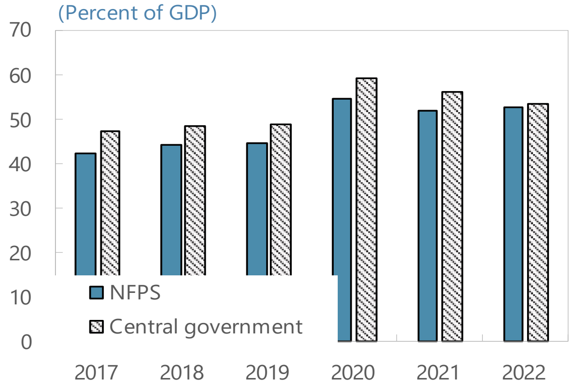
...and a broad-based recovery in revenues....

Central Governmemnt Tax Revenue
(Percent of GDP)



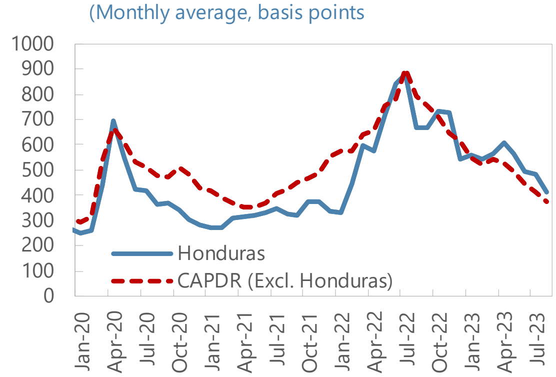
...contributing to declining debt levels...

Public Debt
(Percent of GDP)



...and a gradual decline in external bond spreads.

EMBI Spreads
(Monthly average, basis points)

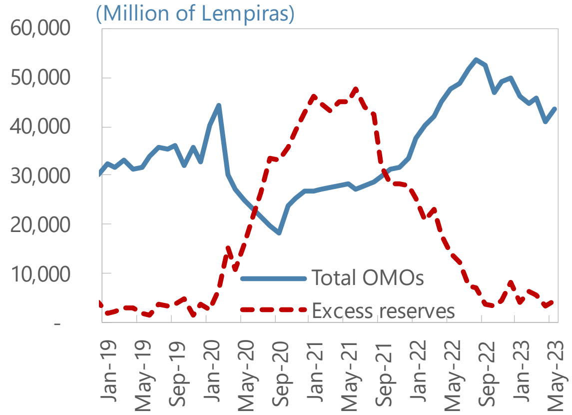


Sources: Authorties data, Bloomberg, and IMF staff calculations and projections.

Figure 7. Honduras: Monetary and Financial Sector Developments, 2019-2023

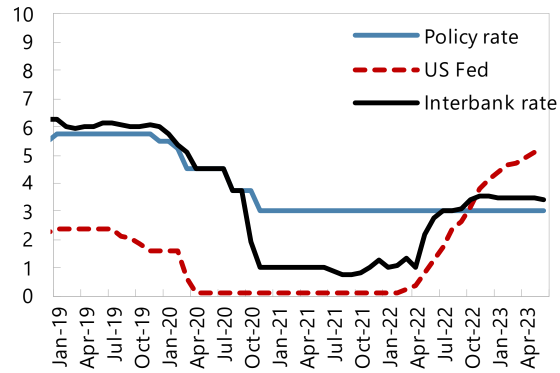
Stepped-up open market operations to absorb excess liquidity …

Open Market Operations and Reserves
(Million of Lempiras)



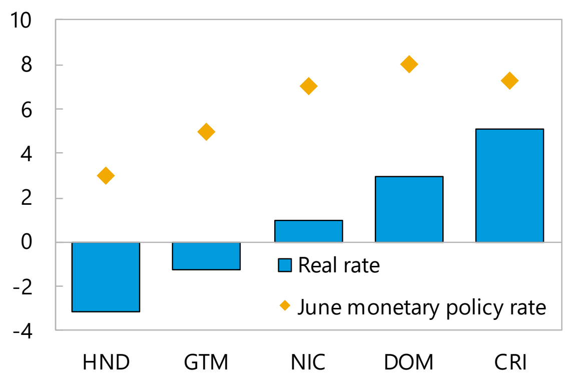
…have resulted in an increase in the interbank borrowing rate…

Policy and Interbank Rates
(Percent)



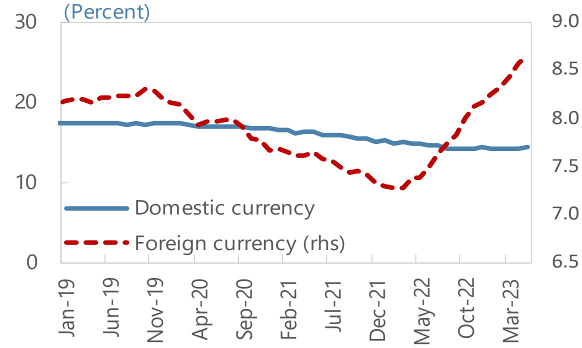
…but real interest rates remain below the U.S. and peers.

Real Interest Rate, End 2023 Projection
(Percent)



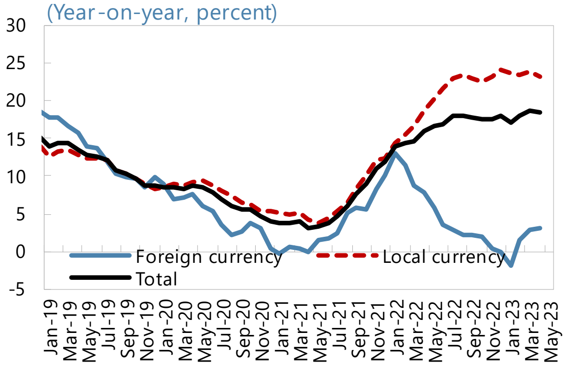
The gap between FX and domestic lending rates has reversed…

Lending Rate in Domestic and Foreign Currency
(Percent)



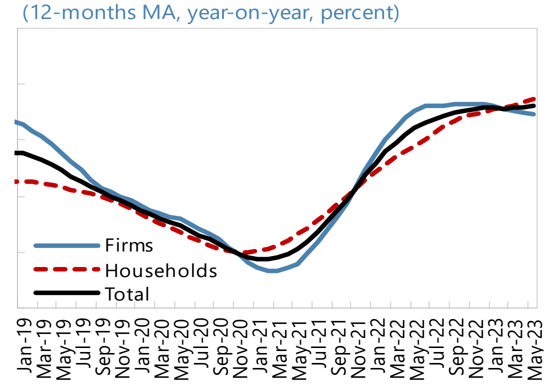
…making borrowing in FX become much less attractive…

Credit to Private Sector Growth
(Year-on-year, percent)



…as the cyclical recovery in credit has continued.

Credit to Firms and Households
(12-months MA, year-on-year, percent)



Sources: Central Bank of Honduras, Haver Analyics, and IMF staff calculations.

Table 1. Honduras: Selected Economic Indicators, 2020-2028

I. Social Indicators

Population (million, 2022)	10.4	Life expectancy at birth in years (2021)	70
Per capita income in U.S. dollars (2022)	3,040	Adult literacy (percent of ages 15 and above, 2019)	89
Rank in UNDP Development Index (2022)	137	Percent of pop. under moderate poverty (2019)	48.0
Unemployment rate (2022)	8.7	Gini index (2019)	48
Net FDI (as percent of GDP, 2022)	2.2	Oil imports (2022)	U.S. $2.8 billion

II. Economic Indicators

	Actual		Estimate	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
National Income and Prices				*(Annual percentage changes unless otherwise indicated)*					
Real GDP	**-9.0**	**12.5**	**4.0**	**2.9**	**3.2**	**3.5**	**3.7**	**3.8**	**3.8**
Domestic demand	-8.6	19.3	3.7	6.4	3.8	4.2	4.0	4.2	4.7
Consumption	-5.0	14.1	4.4	4.5	3.4	3.5	3.7	3.4	3.7
Investment	-23.8	33.3	-0.7	23.7	5.4	7.3	5.6	7.5	8.5
Exports	-20.8	21.5	6.1	7.0	4.9	5.9	6.8	6.1	5.9
Imports	-18.5	33.0	4.8	12.4	5.4	6.4	6.4	6.1	6.6
Net exports (percentage contribution to real GDP)	0.5	-8.7	-0.1	-4.8	-1.3	-1.6	-1.2	-1.3	-1.9
Output gap (percentage of potential GDP)	-7.5	-1.9	-0.5	-0.2	0.0	0.0	0.0	0.0	0.0
Inflation (eop)	4.0	5.3	9.8	5.3	4.2	4.0	4.0	4.0	4.0
Inflation (average)	3.5	4.5	9.1	6.4	4.7	4.1	4.0	4.0	4.0
GDP deflator	4.6	3.8	9.1	6.4	4.7	4.1	4.0	4.0	4.0
Saving and Investment				*(Percentage of GDP unless otherwise indicated)*					
Gross domestic investment	**18.7**	**25.5**	**25.2**	**24.3**	**23.9**	**23.4**	**22.7**	**22.4**	**22.0**
Private sector	16.1	21.1	21.0	20.9	19.8	19.2	18.4	18.0	17.6
Public sector	2.6	4.4	4.2	3.4	4.1	4.3	4.3	4.3	4.4
Gross national savings	21.6	19.3	20.3	18.4	18.3	18.2	17.8	17.7	17.6
Private sector	18.9	16.4	17.8	15.7	14.8	14.5	14.1	13.9	13.7
Public sector	2.7	2.9	2.6	2.7	3.5	3.6	3.7	3.8	3.9
Nonfinancial public sector									
Tax revenues	15.5	18.0	19.0	18.0	18.3	18.6	18.7	18.7	18.7
Public investment	3.4	3.5	2.8	3.0	3.8	4.0	4.0	4.0	4.0
Primary balance	-4.2	-2.3	1.2	-0.7	-0.2	0.0	0.4	0.4	0.5
Overall balance	-5.5	-3.7	-0.2	-2.0	-1.7	-1.4	-1.0	-0.9	-0.9
Gross debt	54.1	51.6	52.3	51.9	51.3	50.4	49.1	47.8	46.6
Balance of payments									
Current account balance	2.8	-4.6	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1	-3.9
Trade balance	-10.8	-17.1	-17.1	-19.2	-19.2	-19.0	-18.3	-17.8	-17.3
Worker's Remittances	23.4	25.3	26.7	26.1	26.0	25.8	25.4	25.0	24.6
Net FDI	1.6	1.8	2.0	2.1	2.2	2.3	2.4	2.5	2.6
Net International Reserves (billions of US$) 1/	8.1	8.7	8.4	7.6	7.7	7.8	8.8	8.4	8.8
Gross International Reserves (billions of US$)	8.5	9.0	8.7	7.9	8.0	8.1	9.1	8.7	9.1
GIR (In months of imports) 2/	7.0	6.4	5.9	5.2	5.0	4.8	5.2	4.8	4.7
GIR (in percent of ARA)	161	152	137	120	116	112	117	109	109
Terms of Trade (annual percent change)	10.7	-8.9	2.2	0.0	-0.6	1.4	0.9	0.5	0.2
Real effective exchange rate (eop, depreciation -)	3.7	1.2	4.0	... .	...	...	...	...	...
Money and Credit									
Broad money (percentage change)	18.6	11.6	12.9	11.4	7.1	7.0	6.5	6.4	6.3
Private sector credit (percentage change)	3.2	12.0	18.9	15.4	8.3	7.5	6.9	6.5	6.4
Private sector credit (percent of GDP)	67.1	64.4	67.4	71.1	71.2	71.1	70.5	69.5	68.5

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

1/ NIR (BCH) corresponds to reserves assets minus obligations with the IMF.

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

Table 2. Honduras: Statement of Operations of the Central Government, 2020-2028
(In millions of Lempiras)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue	**98,674**	**130,673**	**151,413**	**161,866**	**177,490**	**194,153**	**210,422**	**226,824**	**244,824**
Taxes	86,486	118,360	137,519	146,097	160,809	176,421	191,603	206,927	223,425
Taxes on income	25,893	35,660	48,703	48,883	53,893	59,220	65,165	70,377	75,988
Taxes on property	282	586	720	788	852	918	990	1,070	1,155
Taxes on goods and services	54,603	73,612	77,771	85,125	93,849	103,125	111,252	120,150	129,730
Taxes on foreign trade	3,282	5,288	6,501	7,115	7,691	8,285	8,938	9,653	10,423
Other taxes	2,425	3,214	3,823	4,185	4,523	4,873	5,257	5,678	6,130
Social contributions	0	0	0	0	0	0	0	0	0
Grants	3,542	3,741	2,723	3,474	3,386	3,406	3,360	3,310	3,310
Other revenue	8,647	8,573	11,170	12,296	13,295	14,326	15,458	16,587	18,088
Expenditure	**138,047**	**164,630**	**162,576**	**187,205**	**203,708**	**222,868**	**234,051**	**246,640**	**262,979**
Expense	**126,869**	**150,561**	**153,441**	**165,528**	**176,474**	**189,610**	**204,152**	**214,349**	**228,114**
Compensation of employees	52,221	59,485	63,951	69,997	75,658	81,506	85,930	90,802	96,042
Purchases of goods and services 1/	19,209	23,768	24,415	26,723	28,885	31,117	33,569	36,254	39,145
Interest	18,907	20,343	22,074	25,134	26,527	28,236	32,239	30,880	32,218
Domestic	12,437	14,724	16,103	17,717	19,970	21,664	21,665	21,666	21,667
Foreign	6,470	5,619	5,971	7,417	6,557	6,572	10,574	9,214	10,550
Subsidies	1,546	812	4,057	6,981	4,464	4,647	4,833	5,026	5,227
Grants	15,336	18,708	18,237	17,375	17,862	19,242	20,759	22,419	24,206
Current	10,356	11,985	12,768	13,975	15,105	16,273	17,555	18,959	20,471
Capital	4,980	6,723	5,469	3,400	2,756	2,969	3,204	3,460	3,736
Social benefits	6,958	10,309	10,042	10,991	14,078	15,166	16,361	17,670	19,079
Other expense	12,692	17,136	10,665	8,327	9,000	9,696	10,460	11,296	12,197
Current	4,164	2,556	2,171	2,376	2,568	2,767	2,985	3,224	3,481
Capital	8,528	14,580	8,494	5,950	6,432	6,929	7,475	8,073	8,716
Net acquisition of nonfinancial assets	**11,178**	**14,069**	**9,135**	**21,677**	**27,234**	**33,258**	**29,899**	**32,291**	**34,865**
Gross Operating Balance	**-28,194**	**-19,888**	**-2,028**	**-3,662**	**1,016**	**4,543**	**6,270**	**12,475**	**16,710**
Net lending (+)/borrowing (-)	**-39,372**	**-33,957**	**-11,164**	**-25,339**	**-26,218**	**-28,715**	**-23,629**	**-19,816**	**-18,156**
Net financial transactions	**-39,372**	**-33,957**	**-11,164**	**-25,339**	**-26,218**	**-28,715**	**-23,629**	**-19,816**	**-18,156**
Net acquisition of financial assets	**-3,136**	**-4,250**	**19,929**	**12,095**	**8,774**	**8,764**	**17,738**	**18,210**	**21,775**
Foreign	0	0	0	0	0	0	0	0	0
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	0	0	0	0	0	0	0	0	0
Other accounts receivable	0	0	0	0	0	0	0	0	0
Domestic	-3,136	-4,250	19,929	12,095	8,774	8,764	17,738	18,210	21,775
Currency and deposits	-14,671	-6,750	17,429	12,095	8,774	8,764	17,738	18,210	21,775
Debt securities	0	0	0	0	0	0	0	0	0
Loans	11,535	2,500	2,500	0	0	0	0	0	0
Other accounts receivable	0	0	0	0	0	0	0	0	0
Net incurrence of liabilities	**36,236**	**29,706**	**31,093**	**37,434**	**34,991**	**37,480**	**41,367**	**38,026**	**39,930**
Foreign	9,062	-732	9,874	3,512	11,794	4,380	34,032	-11,772	5,082
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	9,226	-549	10,057	3,696	11,977	4,564	34,215	-11,589	5,266
Disbursment	28,125	6,423	21,597	18,822	31,115	25,884	47,021	19,785	16,788
Amortizations	-18,900	-6,972	-11,540	-15,126	-19,139	-21,320	-12,806	-31,374	-11,523
Other accounts payable	0	0	0	0	0	0	0	0	0
Exceptional financing 2/	110	110	110	110	110	110	110	110	110
Other external	-274	-293	-293	-293	-293	-293	-293	-293	-293
Domestic	27,174	30,439	21,219	33,921	23,197	33,099	7,335	49,798	34,848
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	26,246	32,710	20,531	35,392	24,521	34,315	8,447	50,812	35,769
o/w IMF disbursements 3/	11,332	3,027	0	3,030	6,236	6,394	6,547	0	0
Other accounts payable	2,000	-2,000	2,000	0	0	0	0	0	0
PPPs/other	1,163	1,913	936	767	803	805	807	809	811
Adjustment for HIPC debt relief 4/	-2,235	-2,185	-2,248	-2,238	-2,126	-2,020	-1,919	-1,823	-1,732
Memorandum items:									
Net lending minus interest payments	-20,466	-13,614	10,910	-204	310	-479	8,610	11,065	14,062
Nominal GDP (in billions of Lempiras)	586	684	777	850	919	990	1,068	1,153	1,245

Sources: Honduran authorities, IMF staff estimates and projections.

1/ As recommended by the GFSM-2014, since 2019 debt service commissions are reported as goods and services (previously included in the interest bill).

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

3/ Reflects Fund purchases by the central bank to finance the budget

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

Table 3. Honduras: Statement of Operations of the Central Government, 2020-2028
(In percent of GDP)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue	**16.8**	**19.1**	**19.5**	**19.0**	**19.3**	**19.6**	**19.7**	**19.7**	**19.7**
Taxes	14.8	17.3	17.7	17.2	17.5	17.8	17.9	17.9	17.9
Taxes on income	4.4	5.2	6.3	5.8	5.9	6.0	6.1	6.1	6.1
Taxes on property	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Taxes on goods and services	9.3	10.8	10.0	10.0	10.2	10.4	10.4	10.4	10.4
Taxes on foreign trade	0.6	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Other taxes	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Grants	0.6	0.5	0.4	0.4	0.4	0.3	0.3	0.3	0.3
Other revenue	1.5	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.5
Expenditure	**23.6**	**24.1**	**20.9**	**22.0**	**22.2**	**22.5**	**21.9**	**21.4**	**21.1**
Expense	**21.7**	**22.0**	**19.8**	**19.5**	**19.2**	**19.2**	**19.1**	**18.6**	**18.3**
Compensation of employees	8.9	8.7	8.2	8.2	8.2	8.2	8.0	7.9	7.7
Purchases of goods and services 1/	3.3	3.5	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Interest	3.2	3.0	2.8	3.0	2.9	2.9	3.0	2.7	2.6
Domestic	2.1	2.2	2.1	2.1	2.2	2.2	2.0	1.9	1.7
Foreign	1.1	0.8	0.8	0.9	0.7	0.7	1.0	0.8	0.8
Subsidies	0.3	0.1	0.5	0.8	0.5	0.5	0.5	0.4	0.4
Grants	2.6	2.7	2.3	2.0	1.9	1.9	1.9	1.9	1.9
Current	1.8	1.8	1.6	1.6	1.6	1.6	1.6	1.6	1.6
Capital	0.9	1.0	0.7	0.4	0.3	0.3	0.3	0.3	0.3
Social benefits	1.2	1.5	1.3	1.3	1.5	1.5	1.5	1.5	1.5
Other expense	2.2	2.5	1.4	1.0	1.0	1.0	1.0	1.0	1.0
Current	0.7	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Capital	1.5	2.1	1.1	0.7	0.7	0.7	0.7	0.7	0.7
Net acquisition of nonfinancial assets	**1.9**	**2.1**	**1.2**	**2.6**	**3.0**	**3.4**	**2.8**	**2.8**	**2.8**
Gross Operating Balance	**-4.8**	**-2.9**	**-0.3**	**-0.4**	**0.1**	**0.5**	**0.6**	**1.1**	**1.3**
Net lending (+)/borrowing (-)	**-6.7**	**-5.0**	**-1.4**	**-3.0**	**-2.9**	**-2.9**	**-2.2**	**-1.7**	**-1.5**
Net financial transactions	**-6.7**	**-5.0**	**-1.4**	**-3.0**	**-2.9**	**-2.9**	**-2.2**	**-1.7**	**-1.5**
Net acquisition of financial assets	**-0.5**	**-0.6**	**2.6**	**1.4**	**1.0**	**0.9**	**1.7**	**1.6**	**1.7**
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	-0.6	2.6	1.4	1.0	0.9	1.7	1.6	1.7
Currency and deposits	-2.5	-1.0	2.2	1.4	1.0	0.9	1.7	1.6	1.7
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	2.0	0.4	0.3	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	**6.2**	**4.3**	**4.0**	**4.4**	**3.8**	**3.8**	**3.9**	**3.3**	**3.2**
Foreign	1.5	-0.1	1.3	0.4	1.3	0.4	3.2	-1.0	0.4
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	1.6	-0.1	1.3	0.4	1.3	0.5	3.2	-1.0	0.4
Disbursment	4.8	0.9	2.8	2.2	3.4	2.6	4.4	1.7	1.3
Amortizations	-3.2	-1.0	-1.5	-1.8	-2.1	-2.2	-1.2	-2.7	-0.9
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing 2/	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	4.6	4.4	2.7	4.0	2.5	3.3	0.7	4.3	2.8
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	4.5	4.8	2.6	4.2	2.7	3.5	0.8	4.4	2.9
o/w IMF disbursements 3/	*1.9*	*0.4*	*0.0*	*0.4*	*0.7*	*0.6*	*0.6*	*0.0*	*0.0*
Other accounts payable	0.3	-0.3	0.3	0.0	0.0	0.0	0.0	0.0	0.0
PPPs/other	0.2	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Adjustment for HIPC debt relief 4/	-0.4	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.1
Memorandum items:									
Net lending minus interest payments	-3.5	-2.0	1.4	0.0	0.0	0.0	0.8	1.0	1.1
Nominal GDP (in billions of Lempiras)	586	684	777	850	919	990	1,068	1,153	1,245

Sources: Honduran authorities, IMF staff estimates and projections.

1/ As recommended by the GFSM-2014, since 2019 debt service commissions are reported as goods and services (previously included in the interest bill).

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

3/ Reflects Fund purchases by the central bank to finance the budget

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

Table 4. Honduras: Statement of Operations of the Nonfinancial Public Sector, 2020-2028

(In millions of Lempiras)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue	**165,462**	**205,302**	**229,910**	**240,580**	**266,295**	**289,347**	**311,918**	**336,584**	**363,149**
Taxes	90,792	122,999	147,247	152,963	168,230	184,416	199,160	215,089	232,237
Taxes on income	25,893	35,660	48,703	48,883	53,893	59,220	65,165	70,377	75,988
Taxes on property	282	586	720	788	852	918	990	1,070	1,155
Taxes on goods and services	54,603	73,612	77,771	85,125	93,849	103,125	111,252	120,150	129,730
Taxes on foreign trade	3,282	5,288	6,501	7,115	7,691	8,285	8,938	9,653	10,423
Other taxes	6,731	7,854	13,552	11,051	11,945	12,868	12,814	13,839	14,942
Social contributions	22,032	23,452	24,723	26,519	29,238	31,497	33,980	36,697	39,623
Grants	3,620	3,743	2,998	2,790	3,424	3,460	3,397	3,387	3,387
Other revenue	49,019	55,107	54,941	58,308	65,403	69,973	75,381	81,410	87,901
Sales of goods and services	30,230	34,635	34,288	35,703	40,970	43,651	46,985	50,743	54,788
Interest earnings	8,726	8,600	8,403	9,198	9,942	10,710	11,554	12,478	13,473
Capital revenue	47	132	127	139	150	162	175	189	204
Nontax revenue	10,016	11,739	12,122	13,269	14,342	15,450	16,668	18,001	19,436
Expenditure	**197,909**	**230,502**	**231,739**	**257,318**	**281,610**	**302,962**	**322,816**	**346,729**	**373,737**
Expense	**178,207**	**206,869**	**209,888**	**231,816**	**246,696**	**263,369**	**280,102**	**300,600**	**323,930**
Compensation of employees	71,480	80,043	85,353	97,691	104,535	111,488	119,073	128,596	138,849
Purchases of goods and services	54,022	63,349	68,669	73,106	77,180	82,156	85,427	92,259	98,370
Interest	16,454	17,910	19,729	20,213	22,971	24,355	26,408	26,797	29,800
Domestic	9,658	12,063	13,497	12,746	14,850	15,888	17,428	16,335	19,248
Foreign	6,796	5,848	6,232	7,467	8,121	8,467	8,980	10,462	10,551
Social benefits	22,402	28,081	29,244	32,932	36,813	40,586	44,160	47,640	51,450
Other expense	13,827	17,423	6,831	7,856	5,176	4,762	5,012	5,282	5,436
Current	5,107	2,878	2,702	3,788	2,978	3,104	3,223	3,350	3,350
Capital	8,720	14,545	4,130	4,068	2,199	1,658	1,789	1,932	2,086
Net acquisition of nonfinancial assets	**19,701**	**23,633**	**21,850**	**25,502**	**34,915**	**39,593**	**42,714**	**46,130**	**49,808**
Gross Operating Balance	**-12,745**	**-1,567**	**20,021**	**8,764**	**19,600**	**25,978**	**31,816**	**35,984**	**39,219**
Net lending (+)/borrowing (-)	**-32,446**	**-25,200**	**-1,829**	**-16,738**	**-15,315**	**-13,615**	**-10,898**	**-10,146**	**-10,589**
Net financial transactions	**-32,446**	**-25,200**	**-1,829**	**-16,738**	**-15,315**	**-13,615**	**-10,898**	**-10,146**	**-10,589**
Net acquisition of financial assets	**-7,981**	**-7,101**	**48,840**	**27,314**	**29,545**	**32,919**	**33,340**	**34,052**	**45,729**
Foreign	0	0	0	0	0	0	0	0	0
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	0	0	0	0	0	0	0	0	0
Other accounts receivable	0	0	0	0	0	0	0	0	0
Domestic	-7,981	-7,101	48,840	20,674	11,564	16,357	29,564	14,407	15,719
Currency and deposits	-13,781	-12,903	48,840	20,674	11,564	16,357	29,564	14,407	15,719
Debt securities	0	1	0	0	0	0	0	0	0
Loans	3,300	3,300	0	0	0	0	0	0	0
Other accounts receivable	2,500	2,501	0	0	0	0	0	0	0
Net incurrence of liabilities	**24,465**	**18,099**	**50,669**	**44,052**	**44,860**	**46,534**	**44,237**	**44,197**	**56,318**
Foreign	9,063	-730	10,168	3,807	12,088	4,675	34,326	-11,478	5,377
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	9,226	-549	10,057	3,696	11,977	4,564	34,215	-11,589	5,266
Disbursment	28,125	6,423	21,597	18,822	31,115	25,884	47,021	19,785	16,788
Amorizations	-18,900	-6,972	-11,540	-15,126	-19,139	-21,320	-12,806	-31,374	-11,523
Other accounts payable	0	1	0	0	0	0	0	0	0
Exceptional financing 1/	111	111	111	111	111	111	111	111	111
Other external	-274	-293	0	0	0	0	0	0	0
Domestic	17,637	21,014	42,749	42,483	34,898	43,879	11,830	57,498	52,673
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	29,241	35,719	41,813	41,716	34,096	43,075	11,024	56,689	51,862
o/w IMF disbursements 2/	11,332	3,027	0	3,030	6,236	6,394	6,547	0	0
Other accounts payable	-13,000	-17,000	0	0	0	0	0	0	0
PPPs/other	1,396	2,295	936	767	803	805	807	809	811
Adjustment for HIPC debt relief 3/	-2,235	-2,185	-2,248	-2,238	-2,126	-2,020	-1,919	-1,823	-1,732
Memorandum items:									
Net lending minus net interest payments	-24,719	-15,890	9,497	-5,722	-2,286	30	3,956	4,173	5,738
Gross NFPS debt	319,246	355,179	408,729	441,387	470,954	498,533	524,841	551,825	580,411
Nominal GDP (in billions of Lempiras)	586	684	777	850	919	990	1,068	1,153	1,245

Sources: Honduran authorities, IMF staff estimates and projections.

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

2/ Reflects Fund purchases by the central bank to finance the budget.

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

Table 5. Honduras: Statement of Operations of the Nonfinancial Public Sector, 2020-2028

(In percent of GDP)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue	**28.2**	**30.0**	**29.6**	**28.3**	**29.0**	**29.2**	**29.2**	**29.2**	**29.2**
Taxes	15.5	18.0	19.0	18.0	18.3	18.6	18.7	18.7	18.7
Taxes on income	4.4	5.2	6.3	5.8	5.9	6.0	6.1	6.1	6.1
Taxes on property	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Taxes on goods and services	9.3	10.8	10.0	10.0	10.2	10.4	10.4	10.4	10.4
Taxes on foreign trade	0.6	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Other taxes	1.1	1.1	1.7	1.3	1.3	1.3	1.2	1.2	1.2
Social contributions	3.8	3.4	3.2	3.1	3.2	3.2	3.2	3.2	3.2
Grants	0.6	0.5	0.4	0.3	0.4	0.3	0.3	0.3	0.3
Other revenue	8.4	8.1	7.1	6.9	7.1	7.1	7.1	7.1	7.1
Expenditure	**33.8**	**33.7**	**29.8**	**30.3**	**30.6**	**30.6**	**30.2**	**30.1**	**30.0**
Expense	**30.4**	**30.2**	**27.0**	**27.3**	**26.8**	**26.6**	**26.2**	**26.1**	**26.0**
Compensation of employees	12.2	11.7	11.0	11.5	11.4	11.3	11.2	11.2	11.2
Purchases of goods and services	9.2	9.3	8.8	8.6	8.4	8.3	8.0	8.0	7.9
Interest	2.8	2.6	2.5	2.4	2.5	2.5	2.5	2.3	2.4
Domestic	1.6	1.8	1.7	1.5	1.6	1.6	1.6	1.4	1.5
Foreign	1.2	0.9	0.8	0.9	0.9	0.9	0.8	0.9	0.8
Social benefits	3.8	4.1	3.8	3.9	4.0	4.1	4.1	4.1	4.1
Other expense	2.4	2.5	0.9	0.9	0.6	0.5	0.5	0.5	0.4
Current	0.9	0.4	0.3	0.4	0.3	0.3	0.3	0.3	0.3
Capital	1.5	2.1	0.5	0.5	0.2	0.2	0.2	0.2	0.2
Net acquisition of nonfinancial assets	**3.4**	**3.5**	**2.8**	**3.0**	**3.8**	**4.0**	**4.0**	**4.0**	**4.0**
Gross Operating Balance	**-2.2**	**-0.2**	**2.6**	**1.0**	**2.1**	**2.6**	**3.0**	**3.1**	**3.1**
Net lending (+)/borrowing (-)	**-5.5**	**-3.7**	**-0.2**	**-2.0**	**-1.7**	**-1.4**	**-1.0**	**-0.9**	**-0.9**
Net financial transactions	**-5.5**	**-3.7**	**-0.2**	**-2.0**	**-1.7**	**-1.4**	**-1.0**	**-0.9**	**-0.9**
Net acquisition of financial assets	-1.4	-1.0	6.3	3.2	3.2	3.3	3.1	3.0	3.7
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	-1.4	-1.0	6.3	2.4	1.3	1.7	2.8	1.2	1.3
Currency and deposits	-2.4	-1.9	6.3	2.4	1.3	1.7	2.8	1.2	1.3
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	0.6	0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	0.4	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	**4.2**	**2.6**	**6.5**	**5.2**	**4.9**	**4.7**	**4.1**	**3.8**	**4.5**
Foreign	1.5	-0.1	1.3	0.4	1.3	0.5	3.2	-1.0	0.4
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	1.6	-0.1	1.3	0.4	1.3	0.5	3.2	-1.0	0.4
Disbursment	4.8	0.9	2.8	2.2	3.4	2.6	4.4	1.7	1.3
Amorizations	-3.2	-1.0	-1.5	-1.8	-2.1	-2.2	-1.2	-2.7	-0.9
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	3.0	3.1	5.5	5.0	3.8	4.4	1.1	5.0	4.2
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	5.0	5.2	5.4	4.9	3.7	4.4	1.0	4.9	4.2
o/w IMF disbursements 2/	1.9	0.4	0.0	0.4	0.7	0.6	0.6	0.0	0.0
Other accounts payable	-2.2	-2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PPPs/other	0.2	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Adjustment for HIPC debt relief 3/	-0.4	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.1
Memorandum items:									
Net lending minus net interest payments	-4.2	-2.3	1.2	-0.7	-0.2	0.0	0.4	0.4	0.5
Gross NFPS debt	54.1	51.6	52.3	51.9	51.3	50.4	49.1	47.8	46.6
Nominal GDP (in billions of Lempiras)	586	684	777	850	919	990	1,068	1,153	1,245

Sources: Honduran authorities, IMF staff estimates and projections.

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

2/ Reflects Fund purchases by the central bank to finance the budget.

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

Table 6. Honduras: Summary Accounts of the Financial System, 2020-2028 [1/]
(In millions of Lempiras; end-December)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
				I. Central Bank					
Net International Reserves 2/	**196,501**	**211,259**	**207,150**	**192,167**	**199,624**	**205,111**	**236,529**	**229,981**	**245,804**
(In millions of US$)	8,081	8,653	8,375	7,601	7,698	7,756	8,770	8,360	8,760
Net Domestic Assets	**-143,002**	**-148,713**	**-140,061**	**-120,716**	**-124,244**	**-125,925**	**-153,772**	**-143,487**	**-155,528**
Credit to the public sector (net)	12,961	16,957	12,480	2,327	2,327	2,327	2,327	2,479	2,633
Other depository institutions (net)	-135,435	-135,862	-117,733	-81,074	-80,723	-78,477	-94,918	-73,509	-71,379
Other financial institutions	3,840	6,058	2,056	810	-378	-1,605	-10,066	-18,139	-29,027
Nonfinancial private sector	-324	-273	-1,617	-1,763	-1,939	-2,133	-2,346	-2,581	-2,839
Medium and long-term net foreign assets	-9,708	-11,937	-11,072	-14,557	-14,931	-15,227	-15,529	-15,840	-16,157
Other items net	-14,336	-23,654	-24,175	-26,461	-28,601	-30,811	-33,240	-35,898	-38,760
Currency issued	**53,499**	**62,546**	**67,090**	**71,451**	**75,380**	**79,186**	**82,758**	**86,493**	**90,276**
				II. Other Depository Institutions					
Net Foreign Assets	**-23,394**	**-29,714**	**-30,724**	**-23,156**	**-24,842**	**-26,570**	**-28,455**	**-30,503**	**-32,691**
(In millions of US$)	-970	-1,221	-1,249	-916	-958	-1,005	-1,055	-1,109	-1,165
Foreign assets (in million of US$)	675	708	633	1,071	1,120	1,175	1,234	1,296	1,362
Net Domestic Assets	**418,251**	**471,049**	**527,805**	**567,236**	**612,923**	**652,876**	**695,470**	**750,866**	**810,488**
Credit to the monetary authority (net)	147,464	149,179	140,117	95,737	96,206	94,829	112,191	91,759	90,664
Credit to other financial institutions (net)	-39,209	-40,727	-38,776	-38,637	-38,509	-38,375	-38,225	-38,056	-37,871
Credit to the nonfinancial public sector (net)	1,549	8,631	9,925	9,697	11,297	13,043	15,395	17,849	20,409
Central government	-16,296	-9,166	-12,392	-9,489	-8,270	-7,027	-5,758	-4,464	-3,145
Other nonfinancial public sector	8,657	7,427	12,638	13,522	14,469	15,482	16,565	17,725	18,966
Local governments	9,188	10,369	9,679	5,664	5,098	4,588	4,588	4,588	4,588
Credit to the private sector	393,205	440,316	523,500	604,207	654,556	703,722	752,361	801,177	852,410
Local currency	289,852	327,188	410,286	487,520	534,629	580,360	625,219	670,564	718,212
Foreign currency	103,353	113,128	113,214	116,687	119,927	123,362	127,142	130,613	134,197
Other items net	-84,758	-86,348	-106,961	-103,770	-110,627	-120,343	-146,253	-121,862	-115,124
Liabilities	**394,856**	**441,336**	**497,081**	**544,079**	**588,081**	**626,306**	**667,016**	**720,363**	**777,796**
Of which: Deposits in domestic currency	301,072	341,259	389,637	434,719	474,581	507,308	540,283	583,494	630,015
Of which: Deposits in foreign currency	93,784	100,077	107,444	109,360	113,500	118,998	126,733	136,869	147,781
				III. Financial Systems					
Net Foreign Assets	**171,789**	**169,607**	**165,349**	**169,010**	**174,153**	**178,542**	**208,075**	**199,478**	**213,113**
(In millions of US$)	7,064	6,947	6,685	6,685	6,716	6,751	7,715	7,251	7,595
Net Domestic Assets	**277,577**	**331,943**	**400,992**	**461,967**	**501,917**	**544,903**	**562,657**	**620,377**	**659,601**
Credit to the nonfinancial public sector	14,573	25,663	22,578	12,025	13,624	15,370	17,722	20,327	23,042
Credit to the private sector	393,205	440,316	523,500	604,207	654,556	703,722	752,361	801,177	852,410
Local currency	289,852	327,188	410,286	487,520	534,629	580,360	625,219	670,564	718,212
Foreign currency	103,353	113,128	113,214	116,687	119,927	123,362	127,142	130,613	134,197
Other items net 3/	-130,201	-134,036	-145,086	-154,265	-166,262	-174,189	-207,427	-201,127	-215,851
Broad Money (M4)	**449,366**	**501,550**	**566,341**	**630,977**	**676,070**	**723,445**	**770,731**	**819,855**	**872,714**
				(Rate of growth 12 months)					
Currency issued	22.6	16.9	7.3	6.5	5.5	5.0	4.5	4.5	4.4
Currency in circulation	27.1	18.7	7.2	6.9	5.4	4.8	4.2	4.2	4.0
Broad money	18.6	11.6	12.9	11.4	7.1	7.0	6.5	6.4	6.3
Credit to the private sector	3.2	12.0	18.9	15.4	8.3	7.5	6.9	6.5	6.4
o/w foreign currency	10.8	9.5	0.1	3.1	2.8	2.9	3.1	2.7	2.7
M1	29.9	15.9	11.2	9.5	7.6	7.2	5.4	5.3	4.9

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

1/ The central government in the monetary accounts is defined as the budgetary central government plus any NPIs under its control, in particular, pension funds while the central government in Table 2 mainly comprises the budgetary central government (Administración central in the authorities' sectorization).

2/ NIR (BCH) corresponds to reserves assets minus obligations with the IMF. Includes allocation of SDR 104.8 million in August, 2009.

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

Table 7. Honduras: Balance of Payments, 2020-2028

(In millions of US Dollars)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
				(In millions of U.S. dollars; unless otherwise indicated)					
Current account	**666**	**-1,318**	**-1,015**	**-1,770**	**-1,775**	**-1,762**	**-1,712**	**-1,738**	**-1,736**
Trade Account	-2,569	-4,857	-5,411	-6,543	-6,881	-7,171	-7,307	-7,524	-7,751
Exports f.o.b.	5,563	7,088	8,144	8,022	8,118	8,522	8,952	9,340	9,763
Maquila (net)	1,272	1,852	2,009	1,986	2,021	2,133	2,274	2,387	2,520
Coffee	870	1,244	1,405	1,248	1,115	1,204	1,271	1,334	1,401
Other	3,422	3,993	4,730	4,789	4,982	5,185	5,407	5,620	5,842
Imports f.o.b.	-8,133	-11,945	-13,555	-14,565	-14,999	-15,692	-16,259	-16,864	-17,514
Petroleum products	-953	-1,719	-2,551	-2,399	-2,402	-2,465	-2,592	-2,690	-2,824
Other	-7,180	-10,226	-11,004	-12,166	-12,597	-13,227	-13,666	-14,174	-14,690
Services (net)	-1,102	-1,729	-2,122	-2,021	-2,112	-2,163	-2,256	-2,298	-2,441
Of which: tourism receipts	155	303	540	555	579	670	851	991	1,102
Income (net)	-1,646	-2,352	-2,421	-2,373	-2,400	-2,469	-2,622	-2,827	-2,913
Of which: public sector interest payments	-281	-244	-255	-299	-317	-323	-336	-384	-380
Transfers (net)	5,983	7,621	8,939	9,166	9,618	10,041	10,472	10,910	11,369
Of which: Remittances	5,573	7,184	8,465	8,888	9,333	9,740	10,154	10,574	11,013
Capital and Financial account	**1,025**	**1,589**	**1,586**	**873**	**1,799**	**1,757**	**2,556**	**1,372**	**2,185**
Capital account	**551**	**301**	**279**	**315**	**339**	**357**	**378**	**400**	**424**
Financial account	**474**	**1,288**	**1,307**	**558**	**1,460**	**1,400**	**2,178**	**972**	**1,762**
Direct investment (net)	373	513	640	700	777	858	940	1,066	1,152
Other capital flows (net)	-765	646	230	-259	236	427	99	260	343
General government (net)	867	129	436	117	447	115	1,139	-354	267
Disbursements	1,602	390	877	633	975	747	1,518	726	604
Amortization	-736	-260	-440	-516	-528	-631	-378	-1,080	-337
Errors and omissions	**220**	**188**	**-698**	**0**	**0**	**0**	**0**	**0**	**0**
Overall balance	**1,911**	**459**	**-127**	**-898**	**24**	**-5**	**844**	**-367**	**450**
Financing	**-1,911**	**-459**	**127**	**898**	**-24**	**5**	**-844**	**367**	**-450**
Change in central bank reserves (- increase)	-2,381	-587	122	796	-73	-82	-1,014	410	-400
Use of Fund credit (net)	466	124	0	59	49	87	170	-43	-50
Purchases				120	240	242	243	0	0
Repurchases				61	191	155	73	43	50
Exceptional financing	4	4	5	42	0	0	0	0	0
Residual financing	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Memorandum items:									
Terms of trade (percent change)	10.7	-8.9	2.2	0.0	-0.6	1.4	0.9	0.5	0.2
Exports of goods (percent change)	-12.6	33.0	19.1	-0.3	2.2	4.5	4.5	4.0	4.4
Goods exports volume (percent change)	-14.6	21.7	0.1	5.3	2.3	3.0	3.6	3.2	3.2
Imports of goods (percent change)	-15.6	47.0	16.7	6.2	3.2	4.4	3.6	3.7	3.9
Goods imports volume (percent change)	-8.8	22.5	0.2	12.2	2.8	4.3	3.6	3.4	3.0
Gross reserves (end of period, millions of U.S. dollars)	8,454	8,973	8,703	7,907	7,980	8,062	9,076	8,666	9,066
In months of next year imports (excluding maquila)	7.0	6.4	5.9	5.2	5.0	4.8	5.2	4.8	4.7
in percent of ARA	161	152	137	120	116	112	117	109	109
Total external debt (percent of GDP)	45.6	40.7	37.2	35.9	35.8	34.8	36.6	34.0	33.0
Nominal GDP (millions of U.S. dollars)	23,845	28,451	31,698	33,992	35,882	37,796	39,982	42,336	44,815

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

Table 8. Honduras: Balance of Payments, 2020-2028
(In percent of GDP)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
				(In percent of GDP; unless otherwise indicated)					
Current account	**2.8**	**-4.6**	**-3.2**	**-5.2**	**-4.9**	**-4.7**	**-4.3**	**-4.1**	**-3.9**
Trade Account	-10.8	-17.1	-17.1	-19.2	-19.2	-19.0	-18.3	-17.8	-17.3
Exports f.o.b.	23.3	24.9	25.7	23.6	22.6	22.5	22.4	22.1	21.8
Maquila net (exports-imports)	5.3	6.5	6.3	5.8	5.6	5.6	5.7	5.6	5.6
Coffee	3.6	4.4	4.4	3.7	3.1	3.2	3.2	3.2	3.1
Others	14.4	14.0	14.9	14.1	13.9	13.7	13.5	13.3	13.0
Imports f.o.b.	-34.1	-42.0	-42.8	-42.8	-41.8	-41.5	-40.7	-39.8	-39.1
Petroleum products	-4.0	-6.0	-8.0	-7.1	-6.7	-6.5	-6.5	-6.4	-6.3
Other	-30.1	-35.9	-34.7	-35.8	-35.1	-35.0	-34.2	-33.5	-32.8
Services (net)	-4.6	-6.1	-6.7	-5.9	-5.9	-5.7	-5.6	-5.4	-5.4
Of which: tourism receipts	0.6	1.1	1.7	1.6	1.6	1.8	2.1	2.3	2.5
Income (net)	-6.9	-8.3	-7.6	-7.0	-6.7	-6.5	-6.6	-6.7	-6.5
Of which: public sector interest payments	-1.2	-0.9	-0.8	-0.9	-0.9	-0.9	-0.8	-0.9	-0.8
Transfers (net)	25.1	26.8	28.2	27.0	26.8	26.6	26.2	25.8	25.4
Of which: Remittances	23.4	25.3	26.7	26.1	26.0	25.8	25.4	25.0	24.6
Capital and Financial account	**4.3**	**5.6**	**5.0**	**2.6**	**5.0**	**4.6**	**6.4**	**3.2**	**4.9**
Capital account	**2.3**	**1.1**	**0.9**	**0.9**	**0.9**	**0.9**	**0.9**	**0.9**	**0.9**
Financial account	**2.0**	**4.5**	**4.1**	**1.6**	**4.1**	**3.7**	**5.4**	**2.3**	**3.9**
Direct investment (net)	1.6	1.8	2.0	2.1	2.2	2.3	2.4	2.5	2.6
Other capital flows (net)	-3.2	2.3	0.7	-0.8	0.7	1.1	0.2	0.6	0.8
General government (net)	3.6	0.5	1.4	0.3	1.2	0.3	2.8	-0.8	0.6
Disbursements	6.7	1.4	2.8	1.9	2.7	2.0	3.8	1.7	1.3
Amortization	-3.1	-0.9	-1.4	-1.5	-1.5	-1.7	-0.9	-2.6	-0.8
Errors and omissions	**0.9**	**0.7**	**-2.2**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**8.0**	**1.6**	**-0.4**	**-2.6**	**0.1**	**0.0**	**2.1**	**-0.9**	**1.0**
Financing	**-8.0**	**-1.6**	**0.4**	**2.6**	**-0.1**	**0.0**	**-2.1**	**0.9**	**-1.0**
Change in central bank reserves (- increase)	-10.0	-2.1	0.4	2.3	-0.2	-0.2	-2.5	1.0	-0.9
Use of Fund credit (net)	2.0	0.4	0.0	0.2	0.1	0.2	0.4	-0.1	-0.1
Purchases				0.4	0.7	0.6	0.6	0.0	0.0
Repurchases				0.2	0.5	0.4	0.2	0.1	0.1
Exceptional financing	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Residual financing	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:									
Terms of trade (percent change)	10.7	-8.9	2.2	0.0	-0.6	1.4	0.9	0.5	0.2
Exports of goods (percent change)	-12.6	33.0	19.1	-0.3	2.2	4.5	4.5	4.0	4.4
Goods exports volume (percent change)	-14.6	21.7	0.1	5.3	2.3	3.0	3.6	3.2	3.2
Imports of goods (percent change)	-15.6	47.0	16.7	6.2	3.2	4.4	3.6	3.7	3.9
Goods imports volume (percent change)	-8.8	22.5	0.2	12.2	2.8	4.3	3.6	3.4	3.0
Gross reserves (end of period, millions of U.S. dollars)	8,454	8,973	8,703	7,907	7,980	8,062	9,076	8,666	9,066
In months of next year imports (excluding maquila)	7.0	6.4	5.9	5.2	5.0	4.8	5.2	4.8	4.7
in percent of ARA	161	152	137	120	116	112	117	109	109
Total external debt (percent of GDP)	45.6	40.7	37.2	35.9	35.8	34.8	36.6	34.0	33.0
Nominal GDP (millions of U.S. dollars)	23,845	28,451	31,698	33,992	35,882	37,796	39,982	42,336	44,815

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

Table 9. Honduras: External Financing Needs and Sources, 2023-2028
(In millions of U.S. dollars)

	Projections					
	2023	2024	2025	2026	2027	2028
Gross external financing requirement (a)	**3,926**	**4,124**	**4,274**	**3,906**	**4,552**	**3,796**
Current account deficit	1,770	1,775	1,762	1,712	1,738	1,736
Debt amortizations (public and private)	2,156	2,349	2,512	2,194	2,813	2,060
Public debt amortization	577	719	786	451	1,124	387
Private debt amortization	1,579	1,629	1,726	1,743	1,690	1,673
External financing sources (b)	**3,173**	**2,909**	**3,286**	**2,146**	**3,825**	**3,192**
Capital account flows (net)	315	339	357	378	400	424
Foreign direct investment (net)	700	777	858	940	1,066	1,152
Other capital flows	1,362	1,866	2,153	1,842	1,949	2,016
Change in reserves (+ decrease)	796	-73	-82	-1,014	410	-400
Financing gap (c) = (a) -(b)	**753**	**1,215**	**988**	**1,761**	**726**	**604**
Official financing	633	975	747	818	726	604
o/w World Bank	225	247	132	114	96	116
o/w CABEI	110	134	291	316	303	303
o/w IADB	135	256	138	141	141	138
o/w Other official	164	337	186	248	186	47
Eurobonds	0	0	0	700	0	0
IMF financing	120	240	242	243	0	0
Prospective ECF	40	80	81	81	0	0
Prospective EFF	80	160	161	162	0	0
Residual Gap	**0**	**0**	**0**	**0**	**0**	**0**

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

Table 10. Honduras: External Financing Gap, 2023-2026 1/

(In millions of U.S. dollars)

	2023	2024	2025	2026	Total USD Million	Total SDR Million	Total Percent of Quota	Total Percent of Gap
Financing gap	**753**	**1,215**	**988**	**1,761**	**4,717**	**3,485**	**1,395**	**100**
Official financing	**633**	**975**	**747**	**818**	**3,172**	**2,346**	**939**	**67**
o/w World Bank	225	247	132	114	718	532	213	15
o/w CABEI	110	134	291	316	850	628	251	18
o/w IADB	135	256	138	141	670	496	199	14
o/w Other official	164	337	186	248	934	691	277	20
Eurobonds	**0**	**0**	**0**	**700**	**700**	**515**	**206**	**15**
IMF Financing	**120**	**240**	**242**	**243**	**845**	**625**	**250**	**18**
Prospective ECF	40	80	81	81	282	208	83	6
Prospective EFF	80	160	161	162	563	416	167	12
Residual Gap	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**

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

1/ Honduras' quota is SDR 249.8 million.

Table 11. Honduras: External Vulnerability Indicators, 2020-2028

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Exports of goods and services, percent change	-15.9	31.9	19.8	-0.2	2.3	5.0	5.6	4.8	5.0
Imports of goods and services, percent change	-17.1	46.4	17.8	4.8	3.4	4.5	4.4	4.0	4.5
Terms of trade (deterioration -)	10.7	-8.9	2.2	0.0	-0.6	1.4	0.9	0.5	0.2
Real effective exchage rate (eop, depreciation -)	3.7	1.2	4.0	…	…	…	…	…	…
Current account balance (percent of GDP)	2.8	-4.6	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1	-3.9
Capital and financial account (percent of GDP)	4.3	5.6	5.0	2.6	5.0	4.6	6.4	3.2	4.9
External public debt (percent of GDP)	37.0	32.5	30.0	28.7	28.6	27.7	29.5	26.9	25.9
Gross official reserves									
in millions of U.S. dollars	8,454	8,973	8,703	7,907	7,980	8,062	9,076	8,666	9,066
in percent of short-term external debt	1,355	890	885	750	717	688	732	660	652
Net international reserves 1/									
in millions of U.S. dollars	8,081	8,653	8,375	7,601	7,698	7,756	8,770	8,360	8,760
in percent of short-term external debt	1,296	859	852	721	692	662	707	637	630

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

1/ NIR (BCH) corresponds to reserves assets minus obligations with the IMF.

Table 12. Honduras: Decomposition of Public Debt and Debt Service by Creditor, 2022-2024

	Debt Stock (end of period)			Debt Service					
	2022			2022	2023	2024	2022	2023	2024
	(In US$)	*(Percent total debt)*	*(Percent GDP)*	*(In US$)*			*(Percent GDP)*		
Total[1]	**16,524.9**	**100.0%**	**52.1%**	**2,100.1**	**1,904.5**	**2,308.5**	**6.6%**	**5.6%**	**6.4%**
External	**9,477.9**	**57.4%**	**29.9%**	**708.4**	**875.5**	**1,036.5**	**2.2%**	**2.6%**	**2.9%**
Multilateral creditors[2]	**6,639.5**	**40.2%**	**20.9%**	**361.5**	**495.2**	**672.3**	**1.1%**	**1.5%**	**1.9%**
IMF	564.3	3.4%	1.8%						
World Bank	935.7	5.7%	3.0%						
ADB/AfDB/IADB	3,101.1	18.8%	9.8%						
Other Multilaterals	2,038.3	12.3%	6.4%						
o/w: CABEI	1,826.2	11.1%	5.8%						
BEI	76.3	0.5%	0.2%						
Bilateral Creditors[2]	**916.3**	5.5%	2.9%	**39.8**	**55.6**	**57.7**	**0.1%**	**0.2%**	**0.2%**
Paris Club	340.5	2.1%	1.1%	0.0	19.5	21.9	0.0%	0.1%	0.1%
o/w: Japan	89.5	0.5%	0.3%						
Italy	65.7	0.4%	0.2%						
Non-Paris Club	575.8	3.5%	1.8%	39.8	36.1	35.8	0.1%	0.1%	0.1%
o/w: China	442.5	2.7%	1.4%						
Venezuela	81.0	0.5%	0.3%						
Bonds	**1,633.3**	9.9%	5.2%	**275.4**	**262.9**	**250.4**	**0.9%**	**0.8%**	**0.7%**
Commercial creditors	**288.8**	1.7%	0.9%	**31.6**	**61.7**	**56.2**	**0.1%**	**0.2%**	**0.2%**
Other international creditors	0.0	0.0%	0.0%	0.0	0.0	0.0	0.0%	0.0%	0.0%
Domestic	**7,047.0**	42.6%	22.2%	**1,391.7**	**1,029.0**	**1,272.0**	**4.4%**	**3.0%**	**3.5%**
Held by residents, total	7,047.0	42.6%	22.2%	1,391.7	1,029.0	1,272.0	4.4%	3.0%	3.5%
Held by non-residents, total	0.0	0.0%	0.0%	0.0	0.0	0.0	0.0%	0.0%	0.0%
T-Bills	0.0	0.0%	0.0%	0.0	0.0	0.0	0.0%	0.0%	0.0%
Bonds	5,171.2	31.3%	16.3%	820.7	606.8	750.1	2.6%	1.8%	2.1%
Loans	1,875.9	11.4%	5.9%	571.0	422.2	521.9	1.8%	1.2%	1.5%
Memo items:									
Collateralized debt[3]	752.5	4.6%	2.4%						
o/w: Related	n/a	n/a	n/a						
o/w: Unrelated	n/a	n/a	n/a						
Contingent liabilities	1,127.8	6.8%	3.6%						
o/w: Public guarantees	520.3	3.1%	1.6%						
o/w: Other explicit contingent liabilities[4]	607.5	3.7%	1.9%						
Nominal GDP	31,698						31,698	33,990	35,879

1/As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.

2/Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)

3/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral. Related/unrelated breakdown not available.

4/Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Table 13. Honduras: Medium-Term Macroeconomic Framework, 2020-2028
(In percent of GDP unless otherwise specified)

	Actual		Est.	Projections					
	2020	2021	2022	2023	2024	2025	2026	2027	2028
Growth and prices (in percent)									
Real GDP growth	-9.0	12.5	4.0	2.9	3.2	3.5	3.7	3.8	3.8
GDP deflator	4.6	3.8	9.1	6.4	4.7	4.1	4.0	4.0	4.0
CPI inflation (eop)	4.0	5.3	9.8	5.3	4.2	4.0	4.0	4.0	4.0
Investment and saving									
Gross domestic investment	**18.7**	**25.5**	**25.2**	**24.3**	**23.9**	**23.4**	**22.7**	**22.4**	**22.0**
Private sector	16.1	21.1	21.0	20.9	19.8	19.2	18.4	18.0	17.6
Public sector	2.6	4.4	4.2	3.4	4.1	4.3	4.3	4.3	4.4
Gross national savings	**21.5**	**20.8**	**22.0**	**19.1**	**18.9**	**18.8**	**18.4**	**18.3**	**18.1**
Private sector	18.7	18.0	19.5	16.3	15.5	15.1	14.7	14.5	14.3
Public sector	2.7	2.9	2.6	2.7	3.5	3.6	3.7	3.8	3.9
Balance of payments									
External current account	2.8	-4.6	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1	-3.9
Non oil current account	6.8	1.4	4.8	1.8	1.7	1.9	2.2	2.2	2.4
Exports goods and services, (percentage change)	-15.9	31.9	19.8	-0.2	2.3	5.0	5.6	4.8	5.0
Imports goods and services, (percentage change)	-17.1	46.4	17.8	4.8	3.4	4.5	4.4	4.0	4.5
Gross international reserves (millions of dollars)	8,454	8,973	8,703	7,907	7,980	8,062	9,076	8,666	9,066
Real effective rate (eop, depreciation -)	3.7	1.2	4.0	...	...	...	...	...	...
Terms of Trade (percent change)	10.7	-8.9	2.2	0.0	-0.6	1.4	0.9	0.5	0.2
External debt	**45.6**	**40.7**	**37.2**	**35.9**	**35.8**	**34.8**	**36.6**	**34.0**	**33.0**
Nonfinancial public sector									
Revenue	28.2	30.0	29.6	28.3	29.0	29.2	29.2	29.2	29.2
Interest revenue	1.5	1.3	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Of which: Non-interest expenditure	26.8	28.7	28.5	27.2	27.9	28.2	28.1	28.1	28.1
Expenditure	33.8	33.7	29.8	30.3	30.6	30.6	30.2	30.1	30.0
Interest expenditure	2.8	2.6	2.5	2.4	2.5	2.5	2.5	2.3	2.4
Of which: Non-interest expenditure	31.0	31.1	27.3	27.9	28.1	28.1	27.8	27.7	27.6
Capital expenditure	4.9	5.6	3.3	6.6	5.8	6.2	5.8	5.8	5.8
Net interest payments	0.9	1.0	1.0	1.2	1.3	1.3	1.3	1.2	1.2
Primary balance	**-4.2**	**-2.3**	**1.2**	**-0.7**	**-0.2**	**0.0**	**0.4**	**0.4**	**0.5**
Overall balance	**-5.5**	**-3.7**	**-0.2**	**-2.0**	**-1.7**	**-1.4**	**-1.0**	**-0.9**	**-0.9**
Central government									
Revenue	16.8	19.1	19.5	19.0	19.3	19.6	19.7	19.7	19.7
Interest revenue	0.2	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Of which: Noninterest revenue and grants	16.6	18.9	19.3	19.0	19.3	19.6	19.7	19.7	19.7
Expenditure	23.6	24.1	20.9	22.0	22.2	22.5	21.9	21.4	21.1
Interest payment	3.2	3.0	2.8	3.0	2.9	2.9	3.0	2.7	2.6
Of which: Non-interest expenditure	20.3	21.1	18.1	19.1	19.3	19.7	18.9	18.7	18.5
Primary balance	**-3.7**	**-2.2**	**1.2**	**0.0**	**0.0**	**0.0**	**0.8**	**1.0**	**1.1**
Overall balance	**-6.7**	**-5.0**	**-1.4**	**-3.0**	**-2.9**	**-2.9**	**-2.2**	**-1.7**	**-1.4**
Nonfinancial public sector debt 1/									
Total	**54.1**	**51.6**	**52.3**	**51.9**	**51.3**	**50.4**	**49.1**	**47.8**	**46.6**
Of which : Domestic debt	17.1	19.2	22.3	23.2	22.6	22.7	19.7	21.0	20.7
Of which: External debt	37.0	32.5	30.0	28.7	28.6	27.7	29.5	26.9	25.9
Monetary and financial									
Broad money (percentage change)	18.6	11.6	12.9	11.4	7.1	7.0	6.5	6.4	6.4
Private sector credit (percentage change)	3.2	12.0	18.9	15.4	8.3	7.5	6.9	6.5	6.4
Bank assets	122.2	117.1	122.7	129.3	129.6	129.4	128.2	126.4	124.6
Private credit	67.1	64.4	67.4	71.1	71.2	71.1	70.5	69.5	68.5
Non-performing loans to total loans (percent)	3.0	2.7	2.3	...	...	...	...	...	...
Capital adequacy (percent)	14.2	14.1	13.5	...	...	...	...	...	...
Lending rate (eop, in percent)	12.9	12.6	11.3	...	...	...	...	...	...
Deposit rate (eop, in percent)	6.1	4.2	5.5	...	...	...	...	...	...
Memorandum items:									
Nominal GDP (in billions of lempiras)	586	684	777	850	919	990	1,068	1,153	1,245

Sources: Central Bank of Honduras, Ministry of Finance, and Fund staff estimates and projections.
1/ Debt projections use the definition from the DSA.

Table 14. Honduras: Structure and Performance of the Banking Sector, 2015-2023 1/

(In percent, unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021	2022	July 2023
Total assets (in millions of Lempiras) 2/	432,178	473,722	521,869	579,373	632,607	715,567	802,598	871,520	927,070
(In percent of GDP)	94	96	96	101	103	122	117	112	109
Number of banks	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0
Domestic	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Foreign	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0
Bank concentration									
Number of banks accounting for at least 25 percent of total assets	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Capital adequacy									
Regulatory capital to risk weighted assets (RWA)	14.0	13.8	13.7	13.4	13.7	14.2	14.1	13.5	13.8
Capital (net worth) to assets	8.7	8.7	8.7	8.7	8.9	8.4	8.3	8.5	8.4
Asset quality and composition									
Nonperforming loans(NPLs) to total loans	3.0	2.9	2.3	2.1	2.2	3.0	2.7	2.3	2.3
NPLs net of provisions to capital	-5.1	-3.4	-5.8	-5.8	-5.3	-5.0	-5.9	-6.7	-5.9
Restructured loans to regulatory capital	27.9	23.7	25.0	25.0	26.2	48.1	50.3	44.0	40.8
Non earning assets net of provisions to regulatory capital	54.6	48.4	41.6	42.4	40.1	42.6	36.5	35.2	34.9
Provisions to total loans	3.8	3.4	3.2	3.0	3.0	3.8	3.6	3.3	3.1
Provisions to NPLs 2/	126.1	117.4	138.0	140.2	135.2	125.7	133.7	143.8	137.0
Sectoral distribution of loans to total loans:									
Commerce	13.6	13.0	14.9	15.2	14.4	14.4	14.1	15.0	14.7
Construction and real estate	24.6	23.6	23.3	23.0	22.8	23.1	22.6	23.3	23.7
Agriculture and related sectors	5.9	7.2	7.4	7.5	7.3	6.9	6.3	5.7	5.5
Industry	11.1	10.4	10.3	10.8	10.1	11.0	11.3	11.5	11.3
Consumption	21.3	23.1	20.9	21.1	21.5	21.2	20.8	21.7	21.9
Other	23.5	22.5	23.0	21.9	23.1	22.7	24.4	22.3	22.4
Profitability									
Return on assets (ROA)	1.4	1.3	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Return on equity (ROE)	14.6	14.6	12.0	12.0	12.8	7.6	11.1	14.7	14.5
Interest margin to total income	52.8	52.9	51.1	49.6	46.7	40.8	40.2	50.8	52.5
Personnel expenses to administrative expenses	42.0	41.8	45.5	45.1	44.2	42.3	40.7	40.7	41.2
Liquidity									
Liquid assets to total assets	24.6	24.3	26.3	22.2	22.9	29.6	28.8	24.8	22.2
Liquid assets to total short-term liabilities	69.5	66.3	71.5	61.7	62.8	71.8	66.2	55.6	51.0
Dollarization									
Deposits in foreign currency in percent of total	29.8	30.2	29.9	28.9	26.7	25.1	23.7	23.0	22.2
Credit in foreign currency in percent of total	33.2	32.1	31.2	31.8	31.1	30.4	29.5	25.4	23.9

Source: National Commission of Banking and Insurance.

1/ The information covers only private banks.

2/ Includes contingent assets.

Table 15. Honduras: Proposed Disbursements, Purchases, and Timing of Reviews Under the ECF/EFF Arrangements, 2023-26 [1/]

		Amount (millions of SDRs)			Percent of quota [2/]		
Date of Availability	Conditions	Total	ECF	EFF	Total	ECF	EFF
Sep. 21, 2023	Approval of the Arrangements	89.21	29.74	59.47	35.71	11.91	23.81
Mar. 1, 2024	Observance of end-December 2023 and continuous performance criteria and completion of first reviews	89.21	29.74	59.47	35.71	11.91	23.81
Sep. 1, 2024	Observance of end-June 2024 and continuous performance criteria and completion of the second reviews	89.21	29.74	59.47	35.71	11.91	23.81
Mar. 1, 2025	Observance of end-December 2024 and continuous performance criteria and completion of the third reviews	89.21	29.74	59.47	35.71	11.91	23.81
Sep. 1, 2025	Observance of end-June 2025 and continuous performance criteria and completion of the fourth reviews	89.21	29.74	59.47	35.71	11.91	23.81
Mar. 1, 2026	Observance of end-December 2025 and continuous performance criteria and completion of the fifth reviews	89.21	29.74	59.47	35.71	11.91	23.81
Aug. 31, 2026	Observance of end-June 2026 and continuous performance criteria and completion of the sixth reviews	89.24	29.76	59.48	35.72	11.91	23.81
	Total Disbursements	624.50	208.20	416.30	250.00	83.35	166.65

1/ Honduras' quota is SDR 249.8 million.
2/ Percentages may not add up due to rounding

Table 16. Honduras: Indicators of Fund Credit, 2023-2031
(As of August 17, 2023; in units indicated)

	2023	2024	2025	2026	2027	2028	2029	2030	2031
Existing Fund credit									
Stock, in millions of SDRs [1/]	369.5	227.5	113.4	59.7	27.9	6.5	0.0	0.0	0.0
Obligations, in millions of SDRs	51.9	165.6	131.8	68.1	45.5	35.1	20.2	13.7	13.7
Proposed ECF									
Stock, in millions of SDRs [1/]	29.7	89.2	148.7	208.2	208.2	208.2	199.3	178.5	145.8
Disbursements, in millions of SDRs	29.7	59.5	59.5	59.5	0.0	0.0	0.0	0.0	0.0
Obligations, in millions of SDRs [2/]	0.0	0.0	0.0	0.0	0.0	0.0	8.9	20.8	32.7
Principal, in millions of SDRs	0.0	0.0	0.0	0.0	0.0	0.0	8.9	20.8	32.7
Interest and charges, in millions of SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Proposed EFF									
Stock, in millions of SDRs [1/]	59.5	178.4	297.4	416.3	416.3	401.4	366.7	312.2	242.8
Disbursements, in millions of SDRs	59.5	118.9	118.9	119.0	0.0	0.0	0.0	0.0	0.0
Obligations, in millions of SDRs [3/]	0.6	6.1	12.1	18.1	21.0	35.6	54.3	71.9	83.7
Principal, in millions of SDRs	0.0	0.0	0.0	0.0	0.0	14.9	34.7	54.5	69.4
Interest and charges, in millions of SDRs	0.6	6.1	12.1	18.1	21.0	20.8	19.6	17.4	14.3
Stock of existing and prospective Fund credit [1/]									
In millions of SDRs	458.7	495.1	559.4	684.2	652.4	616.1	566.0	490.7	388.6
In percent of quota	183.6	198.2	223.9	273.9	261.1	246.6	226.6	196.4	155.6
In percent of exports of goods and services	4.6	4.9	5.3	6.2	5.6	5.1	4.4	3.6	2.7
In percent of external debt	4.9	5.1	5.7	6.3	6.1	5.7	5.0	4.3	3.3
In percent of gross reserves	7.8	8.3	9.4	10.2	10.2	9.3	8.1	6.6	5.0
In percent of GDP	1.8	1.9	2.0	2.3	2.1	1.9	1.6	1.3	1.0
Obligations to the Fund from existing arrangements and prospective Fund arrangements									
In millions of SDRs	52.6	171.7	143.8	86.2	66.5	70.7	83.4	106.4	130.1
In percent of quota	21.0	68.7	57.6	34.5	26.6	28.3	33.4	42.6	52.1
In percent of exports of goods and services	0.5	1.7	1.4	0.8	0.6	0.6	0.6	0.8	0.9
In percent of external debt	0.6	1.8	1.5	0.8	0.6	0.7	0.7	0.9	1.1
In percent of gross reserves	0.9	2.9	2.4	1.3	1.0	1.1	1.2	1.4	1.7
In percent of GDP	0.2	0.6	0.5	0.3	0.2	0.2	0.2	0.3	0.3
Net use of Fund credit (SDR million)	44.0	36.4	64.3	124.8	-31.8	-36.2	-50.1	-75.3	-102.1
Disbursements and purchases	89.2	178.4	178.4	178.5	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	45.2	142.0	114.1	53.7	31.8	36.2	50.1	75.3	102.1

1/ End of period.
2/ The current zero percent interest rate applicable to PRGT facilities will be maintained until the next review of PRGT interest rates scheduled for July 2025.
3/ Total interest/charges based on existing and prospective drawings using GRA rate of charge = 5.037 (as of August 17, 2023).

Table 17. Honduras: Sustainable Development Goals, 2016-2022

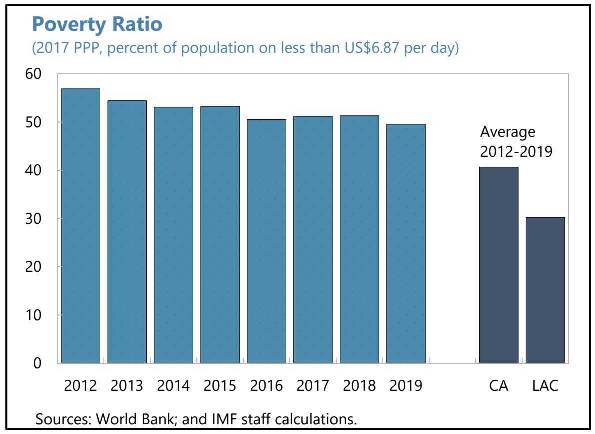
	2016	2017	2018	2019	2020	2021	2022
Goal 1. End poverty in all its forms everywhere							
Proportion of population below international poverty line (%)	16.1	15.4	15.8	14.8	..	..	..
Proportion of population living below the national poverty line (%)	49.7	49.8	50.4	48.0	..	..	..
Goal 2. End hunger, achieve food security and improved nutrition and promote sustainable agriculture							
Prevalence of undernourishment (% of population)	13.8	13.2	13.1	13.5	..	..	..
Goal 3. Ensure healthy lives and promote well-being for all at all ages						..	..
Mortality rate, neonatal (per 1,000 live births)	10.1	9.8	9.4	9.1	8.8	..	..
Mortality rate, under 5 (per 1,000 live births)	18.6	18.0	17.4	16.8	16.2	..	..
Maternal mortality ratio (per 100,000 live births)	65.0	65.0	..	..	..	..	..
Prevalence of HIV, total (% of population ages 15-49)	0.3	0.3	0.3	0.2	0.2	..	..
Goal 4. Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all							
Minimum proficiency in mathematics, secondary (%)	92.0	..	..	..	..	..	..
Minimum proficiency in reading, secondary (%)	93.0	..	..	..	..	..	..
Gender parity index for achievement in mathematics, secondary	..	..	..	..	..	..	..
Gender parity index for achievement in reading, secondary	..	..	..	..	..	..	..
Rural to urban parity index for achievement in mathematics, secondary	..	..	..	..	..	..	..
Rural to urban parity index for achievement in reading, secondary	..	..	..	..	..	..	..
Goal 5. Achieve gender equality and empower all women and girls							
Proportion of seats held by women in national parliaments (%)	25.8	..	21.1	21.1	21.1	..	..
Proportion of women in managerial positions (%)	41.1	41.0	47.1	47.5	39.7	..	..
Goal 6. Ensure availability and sustainable management of water and sanitation for all							
Proportion of population with basic handwashing facilities on premises, rural (%)	82.0	83.0	83.0	83.0	84.0	84.0	84.0
Proportion of population with basic handwashing facilities on premises, urban (%)	86.0	86.0	86.0	86.0	86.0	85.0	85.0
Goal 7. Ensure access to affordable, reliable, sustainable and modern energy for all							
Proportion of population with primary reliance on clean fuels and technology (%)	46.0	47.0	48.0	49.0	49.0	50.0	..
Renewable energy share in total energy consumption (%)	52.7	45.6	48.8	46.2	50.1	..	..
Goal 8. Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all							
Annual growth rate of real GDP per capita (%)	2.1	3.0	2.1	0.9	-10.4	10.8	..
Proportion of informal employment in non-agriculture employment (%)	73.8	..	..	..	..	..	..
Proportion of youth not in education, employment or training (%)	27.8	27.7	26.6	26.8	..	..	..
Goal 9. Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation							
Manufacturing value added as a proportion of GDP (%)	17.4	17.2	17.3	17.1	16.2	17.2	17.2
Researchers (in full-time equivalent) per million inhabitants (per 1,000,000 population)	..	34.7	203.8	189.9	..	..	..
Proportion of medium and high-tech industry value added in total value added (%)	7.2	..	..	..	..	..	..
Goal 10. Reduce inequality within and among countries							
Growth rate of household expenditure or income per capita (%)	..	..	..	..	..	..	..
Remittance costs as a proportion of the amount remitted (%)	5.8	4.2	4.1	3.6	4.6	..	..
Goal 11. Make cities and human settlements inclusive, safe, resilient and sustainable							
Annual mean levels of fine particulate matter in cities, total population (micrograms per cubic meter)	22.6	21.1	20.0	18.9	..	..	..
Goal 14. Conserve and sustainably use the oceans, seas and marine resources for sustainable development							
Average proportion of Marine Key Biodiversity Areas (KBAs) covered by protected areas (%)	41.0	41.0	41.0	41.0	41.0	41.0	41.0
Goal 16. Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels							
Number of victims of intentional homicide per 100,000 population	54.4	40.1	38.1	41.1	35.8	38.3	..
Bribery incidence (% of firms experiencing at least one bribe payment request)	33.0	..	..	28.0	..	..	..

Source: UN SDG Indicators Global Database.

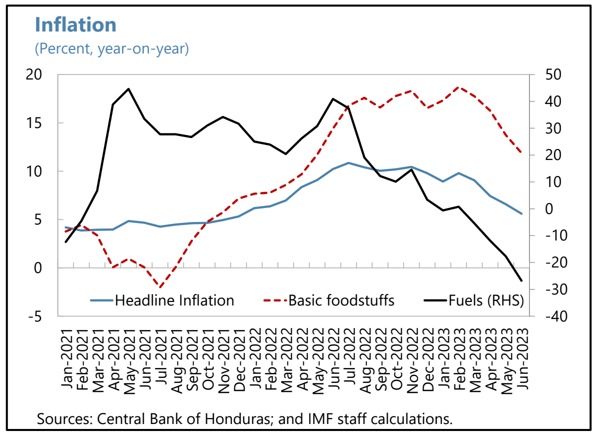
Note: Goals 12, 13 and 17 are not listed due to data limitations.

Box 1. Honduras: Poverty and Food Insecurity

Honduras remains one of the poorest and most unequal countries in the Western Hemisphere, with poverty estimates for 2021 at over 70 percent (around 50 percent for extreme poverty).[1] Honduras faces several challenges in its efforts to reduce poverty, including slow and volatile growth, weak governance and institutions, high unemployment and informality. Widespread corruption, crime, and political instability also contribute to the country's high poverty rates. In addition, Honduras has one of the highest levels of income inequality in the region, with the top 20 percent holding about 52 percent of the country's income share (as of 2019).[2]



Challenges related to food security stem from constrained availability of affordable and nutritious food. A surge in food and fuel prices since 2021, coupled with lackluster production of essential crops—corn and beans production grew by 1 percent and 1.5 percent, respectively, due to poor climate conditions and inadequate access to agricultural inputs—have led to an increase in food insecurity. Close to a quarter of the population is in food crisis or emergency (World Food Program phases 3 and 4). Particularly exposed are women living in rural areas with high poverty rates and areas where families rely on subsistence farming.



Climate change has had a significant impact on poverty and food insecurity in Honduras. Honduras is considered one of the most vulnerable countries to the impacts of climate change (Annex II), with extreme weather events disrupting economic activity and forcing people to relocate, intensifying poverty and food insecurity. Additionally, climate change has led to a decline in crop yields, loss of biodiversity, and decreased water availability. In 2020, Tropical Storms Eta and Iota resulted in the loss of approximately 2 and 7 percent of the cultivated acreage of corn and beans, respectively.

The Honduran government, in partnership with international organizations, has implemented several programs and policies aimed at improving food security and reducing poverty. These include expanding and prioritizing social protection policies, such as cash transfers (a focus of *Red Solidaria*), targeted subsidies, and resuming school meal programs, which aim to support vulnerable populations and reduce malnutrition. The government has also implemented agricultural programs to promote sustainable farming practices (*Bonos Tecnológicos*) and increase crop yields, including by providing fertilizer and seedlings to farmers, and provide better access to markets for small farmers. Additionally, recently approved legislation, such as the *Ley de Seguridad Alimentaria y Nutricional*, aims to establish a regulatory framework for structuring, harmonizing, and coordinating actions for food and nutritional security.

[1] Preliminary data from the *Instituto Nacional de Estadísticas* (INE).
[2] World Bank WDI Database, 2023.

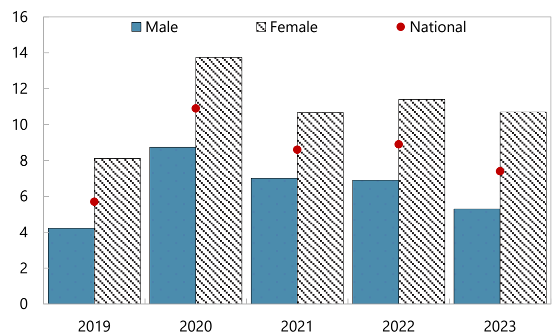
Box 2. Honduras: Labor Markets and Education[1]

The pandemic, coupled with the impact of two back-to back tropical storms, led to disruptions in the Honduran labor market. Like other countries, Honduras experienced the consequences of diminished business operations, temporary shutdowns, and lockdowns during the pandemic. These measures had a notable impact on economic activities including agriculture, manufacturing, and tourism, with job opportunities becoming scarcer, further fostering informal labor practices.

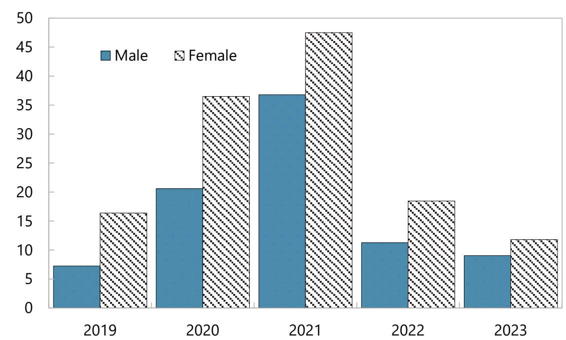
Women were particularly affected by job losses and reduced working hours. The national unemployment rate increased to 10.9 percent in 2020 from 5.7 percent in 2019. After the economy reopened and health measures were lifted, the unemployment rate decreased to 7.4 percent during 2023:H1 Nevertheless, it still exceeds pre-pandemic levels. Women's employment bore a severe impact from the adverse shocks; female unemployment peaked at 13.9 percent in 2020 (Figure 1, Panel A) and remains high. The visible underemployment rate for women has been declining since 2021, albeit at a more gradual pace compared to that of males, and it continues to hover around 12 percent (Figure 1, Panel B). Furthermore, in 2023 the labor force participation rate for women (38 percent) remains much lower than for men (74 percent).

Box 2. Figure 1. Honduras Unemployment and Underemployment Rate by Gender

Panel A. Unemployment Rate
(Percent)



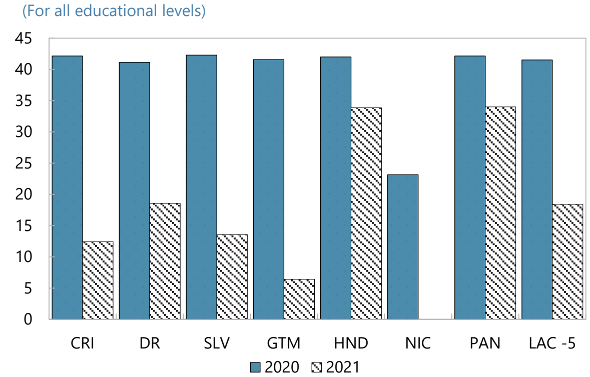
Panel B. Visible Underemployment
(Percent)



Source: Honduras National Statistics Office (INE) and IMF staff calculations.

The education system continues to recover in the aftermath of the pandemic. The health measures adopted to address the pandemic including a shift from an in-person to a remote-learning model, though in the context of high technological inequality and limited internet connectivity. Additionally, Honduras kept schools closed for a longer period in 2021-22 than other countries in the region, exacerbating an educational lag that could lead to lower human capital, affecting Honduras' potential output in the long run. The country also suffers from scarce educational infrastructure and the need to repair and reconstruct around 12,000 schools.

Weeks of School Closures
(For all educational levels)



Source: Oxford University; and IMF staff calculations.

[1] 2023 numbers are preliminary subject to revision.

Box 2. Honduras: Labor Markets and Education (Concluded)

The authorities have taken measures to address challenges in the labor market and education system. To promote labor formality and reduce the visible underemployment rate, the Hourly Employment Law (*Ley de Empleo por Hora*), which allowed the signing of contracts, whether for hours or half-day shifts, during daytime, mixed or nighttime, for a limited period of time and for specific tasks or services, was repealed in 2022. Furthermore, steps have been taken to enhance on-site inspections of manufacturing and maquiladora companies to improve adherence to minimum quality of employment conditions. An ambitious plan to boost national employment has been initiated, involving the establishment of 17 regional employment offices to facilitate labor market entry. Recognizing the vulnerability of women in the labor market, the authorities are in the final stages of reviewing the 3rd National Equality Plan (*Plan Nacional de Igualdad*). This plan is centered around three core pillars: i) strengthening inclusion and bridging gender gaps, ii) promoting gender parity, and iii) providing improved educational opportunities for women. The reconstruction of schools, the revival of the school lunch program, and student scholarships serve as the cornerstones for bridging educational gaps. Simultaneously, with a forward-looking perspective, the Ministries of Education and Labor are collaborating to identify labor market demands and tailor educational offerings to meet those needs.

Box 3. Honduras: Comprehensive Tax Reform to Support Development Needs

The Honduran tax authorities have made notable collection efforts in recent years without having to change statutory tax rates. Tax revenues for 2022 were close to the Latin America/Caribbean average of 18 percent of GDP (Box Figure 1). Total revenues and grants averaged around 30 percent of GDP between 2015 and 2019, significantly higher than regional peers, with non-tax revenues largely driven by electricity sales of the public utility company ENEE.

The tax administration diagnostics assessment tool (TADAT) evaluation in 2020 reflected significant progress on tax administration in recent years. The Revenue Administration (SAR) performs well in terms of its core competencies relative to regional peers. Using the operational strength index of tax administration based on the International Survey on Revenue Administration (ISORA), Honduras is estimated to have a higher composite score for operational strength in revenue administration than the LAC average but a lower composite score than aspirational peers such as the Dominican Republic (Box Figure 1, Panel 5).[1] Importantly, SAR scores high in key competencies of its operation, including compliance risk management, degree of autonomy, the establishment of a large taxpayer office (LTO) or large taxpayer program, public accountability, and service orientation, but low in the use of third-party data (Box Figure 1, Panel 6).

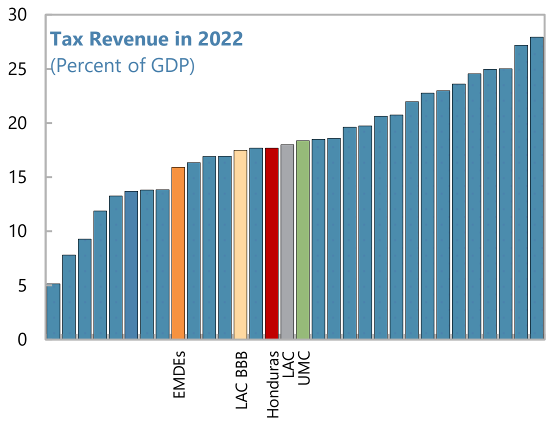
Despite high tax revenue as a share of GDP and sound revenue administration capabilities, there is scope for further improvement. As identified by previous staff reports (Country Report No. 19/237), the main shortcomings of the Honduran tax regime include: (i) its regressive nature (exemptions and exonerations concentrated in the highest income percentiles); (ii) the high level of tax expenditures (38 percent of collection, with income taxes comprising around 2/5 thereof—the planned tax reform (LJT) addresses CIT exemptions only) and their lack of evaluation; (iii) its complexity (exacerbated by the number of waivers and exonerations); and (iv) its high level of informality, caused in part by the high burden on the formal sector (high nominal rates to compensate for the high level of tax expenditures). In tax administration, there is scope to strengthen administration and enforcement mechanisms to minimize tax evasion. Further advances could be made in compliance risk management (CRM) and the digitalization of services. Specifically, automated risk profiling as part of processing payments and returns and use of electronic audit methods and third-party data could further improve compliance risk management, while mandatory e-filing, e-payment, and electronic invoicing could facilitate digitalization of the taxation systems.

Importantly, the authorities aspire to an ambitious tax reform envisaged to reduce tax expenditures and to broaden the tax base (Staff Report ¶20). The authorities have submitted to the National Congress the "Bill on Tax Justice" (Ley de Justicia de Tributaria, LJT), a comprehensive reform, designed with extensive Fund assistance, that would significantly reform the current tax system, in particular exemptions to corporate income taxes. This tax reform would create policy space, lower public debt, and support development needs, while striking a fine balance to also safeguard Honduras' competitiveness. Finally, it would also help improve the efficiency and equity of the overall tax system. Once approved, it will be critical that implementing regulations be transparent and clear to promote compliance, improve revenue-raising efficiencies, and support the business environment.

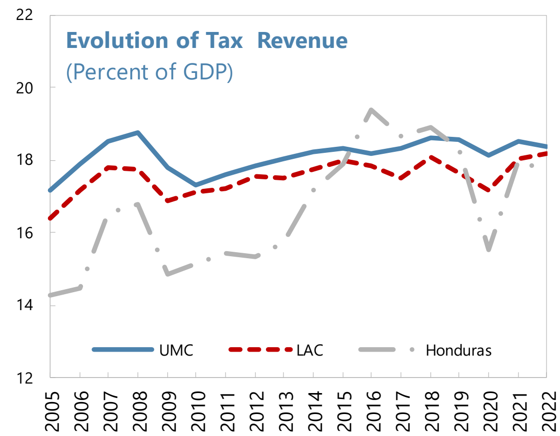
[1] Structural and aspirational peers are identified based on Honduras Public Expenditure Review (World Bank Group, 2023)

Box 3. Figure 1. Tax Revenue and Administration Metrics

Tax revenues are close to the LAC average....

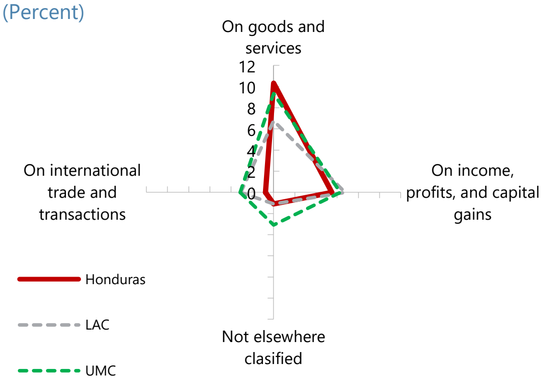


...and have increased over time, though with significant volatility.



Most tax revenue comes from taxes on income and goods and services...

Composition of Tax Revenue
(Percent)



...while tax rates are broadly in line with regional averages.

Tax Rates in 2019
(Percent)

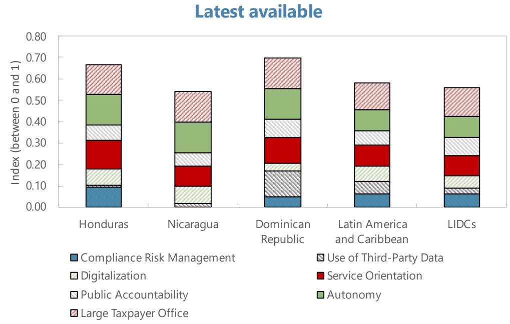
	Honduras	Central America without Honduras	LAC without Honduras	OECD
VAT (ITBIS) Standard Rate	15.0	12.0	14.3	19.5
PIT Rate	25.0	23.4	28.4	34.4
CIT and Dividend Rate	25.0	28.0	27.7	22.5

Source: WEO, IBFD, and Tax Laws.

Notes: Central America only includes Costa Rica, El Salvador, Guatemala, Honduras, and Panama. Using latest available data, 2019 for most countries and indicators

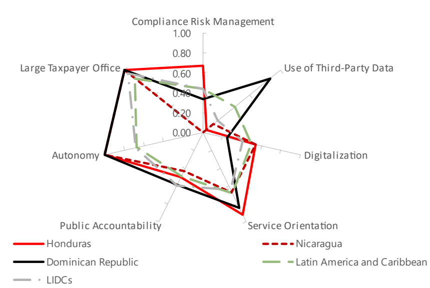
The assessed operational strength of revenue administration exceeds the LAC average...

Contribution to Operational Strength Index, Latest available



...scoring highly in key competencies, but poorly in the use of third-party data.

Operational Strength Index subcomponents, Latest available



Sources: World Economic Outlook, IBFD, TAX Law, and ISORA dataset.
Notes: LAC: Latin America and the Caribbean; LAC BBB: Panama, Peru, Trinidad and Tobago, and Uruguay; LAC BB: Brazil, Colombia, Guatemala, and Honduras; EMDEs: Emerging and Developing Economies; UMC: upper-middle income countries. Blue bars without country names are for other LAC countries.

Box 4. Honduras: Neutral Interest Rate Estimates

The monetary policy rate remains below staff's estimates of the neutral nominal policy interest rate. To estimate the neutral interest rate, staff employed several methods, including uncovered interest rate parity (UIP), a small-scale monetary policy model, an expected-inflation augmented Taylor rule, and a small-scale projection model. The current monetary policy interest rate of 3.0 percent falls below the neutral rate estimate of 4.1 to 5.3 percent. Among the factors that drive the evolution of these estimates include: (i) the evolution of inflation expectations; (ii) expected inflation of trading partners; (iii) international interest rates and risk premia; and (iv) the output gap. Sustained deviations between local and foreign interest rates could pose risks to the stability of the monetary and exchange rate framework, the return of inflation to the central bank's reference range, and the anchoring of inflation expectations.

Honduras: Neutral Nominal Interest Rate Estimates

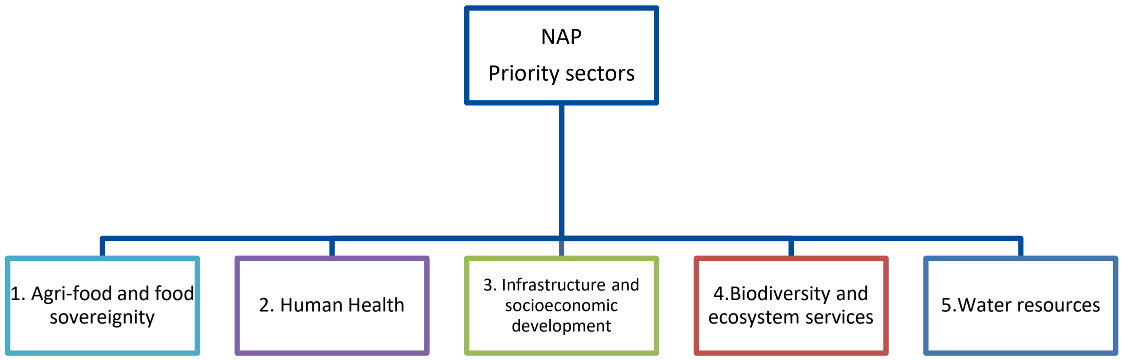
	With BCH expectations survey			With Consensus Forecast expectations		
Method	Neutral Nominal Interest Rate	MPR	Nominal Monetary Policy Gap (bps)	Neutral Nominal Interest Rate	MPR	Nominal Monetary Policy Gap (bps)
UIP						
Method A [1/]	5.0	3.0	196	5.0	3.0	196
Inflation augmented Taylor rule	4.9	3.0	186	5.3	3.0	226
General Equilibrium Model [2/]	4.8	3.0	180	4.8	3.0	180
Small Scale Projection Model [3/]	4.1	3.0	110	4.1	3.0	110
Average	4.7	3.0	168	4.8	3.0	178

1/ Using the long run values for local and external inflation, international interest rate and risk premium.
2/ A rational expectations model based on four behavior equations: aggregate demand, a short-term aggregate supply, a monetary policy rule and the uncovered interest rate parity condition.
3/ A semi-structural neo-Keynesian model based on five equations: a Phillips curve, an inflation expectations equation that depends on the inflation target announced by the central bank, an IS curve, and a prospective monetary policy rule.

Source: IMF staff calculations.

Box 5. Honduras: Climate Change Adaptation Strategies

In response to the increasing challenges posed by climate change, the Honduran authorities have been actively designing and implementing a range of adaptation strategies at the national level for five priority sectors identified in the National Adaptation Plan (NAP).



Source : Honduras National Adaptation Plan.

Strategies within these critical sectors include: enhancing the adaptive capacity of the agri-food industry; strengthening water storage capabilities for increased resilience; safeguarding and conserving protected areas; and revitalizing ecosystems that have experienced degradation through risk reduction management with a gender-focused approach, as well as cross-cutting areas such as human rights and adaptative governance, knowledge management, and territorial planning.

In the short term and as a complement to the actions to strengthen adaptation strategies, the authorities are in the process of developing the National Water Policy and the Infrastructure Sector Adaptation Strategy. In the medium term, complementary actions include updating the management plans of protected areas, establishing and strengthening agri-food consultation groups (*Mesas Agroalimentarias Participativas*) across the country, and updating Municipal Territorial Plans with a focus on adaptation and a gender perspective.

In addition to the NAP, Honduras has a Technological Action Plan (TAP), which outlines a series of technological actions for national-level adaptation and prioritizes technologies for the Agri-food Sector and the Water Resources Sector.

Annex I. External Sector Assessment

Overall Assessment: *The external position of Honduras in 2022 was broadly in line with the level implied by fundamentals and desirable policies. Risks to external sustainability are mitigated by the path and composition of the net international investment position, with gross external liabilities tilted towards foreign direct investment and a declining trend for external debt. The gross international reserves coverage ratio is adequate and expected to be comfortably within the recommended range of the ARA metric over the medium term.*

Potential Policy Responses*: Steps to maintain prudent fiscal and debt policies, strengthen the consistency between monetary and exchange rate policies, and advance the structural reform agenda remain essential to maintaining external sustainability. Strengthening the crawling band regime and ensuring that the exchange rate reflects economic fundamentals, which could be supported by IMF technical assistance, should also help maintain external competitiveness.*

Foreign Assets and Liabilities: Position and Trajectory

Background. The net international investment position (NIIP) improved to -53 percent of GDP in 2022, from -56 percent in 2021, driven by the decline in gross FDI liabilities. Gross assets stood at 47 percent of GDP, with reserves accounting for the largest share (57 percent of gross assets). At 99 percent of GDP in 2022, gross liabilities were primarily composed of FDI liabilities (59 percent of GDP and 59 percent of gross liabilities). External debt stood at US$11,796 million at end-2022 (37.4 percent of GDP) and was mostly public (81 percent of the total stock), with private external debt driven by the financial sector. As of May 2023, public external debt stood at US$9,380.2 million (27.6 percent of GDP), against US$9,533.3million (30.1 percent of GDP) at end-2022. Public external debt was mainly US$-denominated and primarily consisted of loan liabilities to multilateral creditors (71.5 percent of total public external debt as of May 2023).

Assessment. Honduras' negative NIIP does not flag risks to external sustainability. The composition of gross liabilities, tilted towards FDI, also limits vulnerabilities. Additionally, the external sustainability (ES) approach of the EBA-lite methodology does not raise concerns about external sustainability as stabilizing Honduras' NIIP at its 2022 level in the medium-term would not require a REER adjustment given the near-zero CA gap from the model.

Current Account and Real Exchange Rate

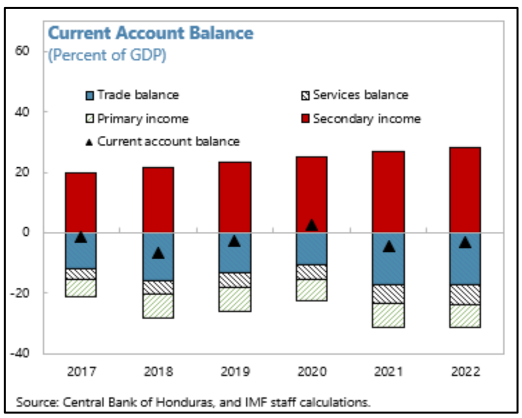
Background. The CA balance sharply improved to -3.2 percent of GDP in 2022, from -4.6 percent of GDP in 2021, driven by strong remittances, favorable prices for key export products (coffee, banana, and palm oil), and a dynamic maquila sector. From the savings-investment balance perspective, the CA deficit in 2022 reflected improvements in private investment linked to the recovery of the economy from the pandemic, partly offset by an improvement in the fiscal balance. As of 2023Q1, goods exports and imports declined by 6.6 and 4.7 percent y/y, respectively. Remittances recorded a 9.2 percent y/y increase as of 2023Q1. The CA deficit is expected to average about 4 percent of GDP going forward. The REER modestly appreciated by 2 percent in 2022.

Assessment. The CA approach finds that the cyclically adjusted CA was -3.9 percent of GDP after accounting for the model's cyclical contributions, COVID-19 adjustor, and natural disasters. The cyclically adjusted CA norm, which reflects the CA level that is in line with fundamentals and desirable policy levels, stood at -5.1 percent of GDP. This yields a positive CA gap of 1.2 percent of GDP consistent with a REER undervaluation of 3.7 percent (simply assuming the CA elasticity of -0.31 with respect to REER). The contribution of policy gaps is estimated at 3.9 percent of GDP, primarily driven by the fiscal spending gap. In contrast, the REER index model finds a CA gap of -1 percent of GDP, suggesting a REER overvaluation of 2.9 percent. The CA and the REER models complement each other but accentuate different economic channels.[1] In the case of Honduras, the overall assessment of the external position is based on the REER model, which has the advantage of explicitly accounting for the level of real interest rates in home and foreign economies. This is particularly relevant at the current juncture when domestic real interest rates are lower than in the U.S. and the neighboring countries and the authorities have reinstated the centralized allocation of FX. That said, the contribution of the policy gap in the REER is limited, with the contribution of the real interest rate negligible.

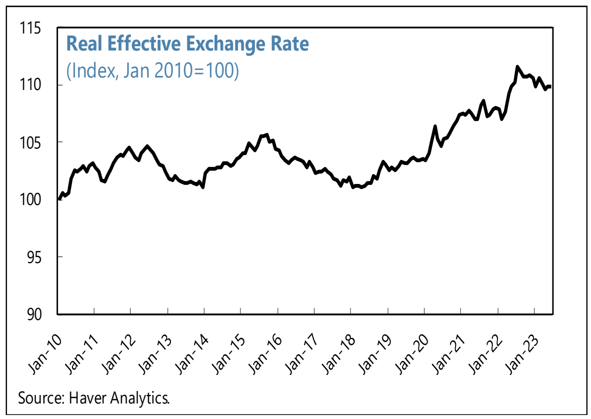
Honduras: EBA-lite Model Results, 2022

	CA model 1/	REER model 1/ (in percent of GDP)	ES model
CA-Actual	**-3.2**		
Cyclical contributions (from model) (-)	0.9		
COVID-19 adjustors (-) 2/	-0.2		
Natural disasters and conflicts (-)	-0.1		
Adjusted CA	**-3.9**		
CA Norm (from model) 3/	**-5.1**		
Adjustments to the norm (-)	0.0		
Adjusted CA Norm	**-5.1**		
CA Gap	**1.2**	**-1.0**	**0.1**
o/w Relative policy gap	3.9		
Elasticity	-0.3		
REER Gap (in percent)	**-3.7**	**2.9**	**-0.3**

1/ Based on the EBA-lite 3.0 methodology
2/ Additional cyclical adjustment to account for the temporary impact of the pandemic on tourism (0.04 percent of GDP) and remittances (0.13 percent of GDP).
3/ Cyclically adjusted, including multilateral consistency adjustments.



Source: Central Bank of Honduras, and IMF staff calculations.



Source: Haver Analytics.

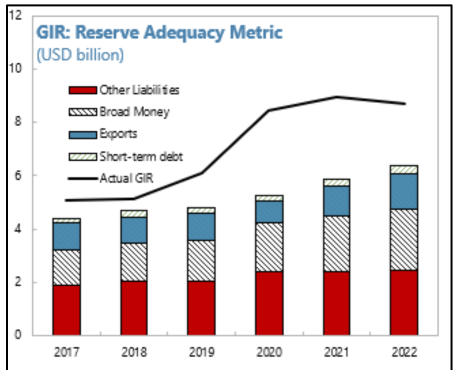
Capital and Financial Accounts: Flows and Policy Measures

Background. The financial account surplus stood at 4.1 percent of GDP in 2022, mainly driven by net inflows of FDI (2.0 percent of GDP) and government borrowing (1.4 percent of GDP). Between 2017 and June 2021, the surrender requirement for foreign exchange agents on proceeds from current and capital transactions to the central bank was phased out as part of the reforms supporting the transition toward a more flexible exchange rate regime and fewer foreign exchange interventions by the central bank. The central bank also ended its daily FX auctions. However, in April 2023, the authorities reinstated a 100 percent surrender requirement for exchange agents together with the daily FX auctions and shut down the interbank FX market. Exporters also remain required to sell all their export receipts in FX to foreign exchange agents, except for those exporters authorized by the Central Bank's Board of Directors to retain up to 30 percent for priority purchases or debt service abroad.

Assessment. Going forward, the financial account is projected to continue recording a surplus, primarily on the back of net FDI inflows.

FX Intervention and Reserves Level

Background. Gross international reserves (GIR) reached US$8,703 million or 5.9 months of non-maquila imports of goods and services at end-2022. This represents 885 percent of short-term debt in 2022. GIR stood at US$7,970.3 million (5.2 months of prospective imports) as of August 21, 2023. Honduras's de jure exchange rate arrangement is a crawling band, while de facto the exchange rate is stabilized. In 2022, the central bank intervened in the FX market selling on net a total of US$336 million, most of which late in the year, when supply shortfalls of FX became more prevalent, including as a result of higher import prices during the year. BCH has also been selling FX to oil importers during December 2022-February 2023 and again since June—around US$500 million in total through August 7, 2023.



Source: Central Bank of Honduras, and IMF staff calculations.

Assessment. GIR stood at 137 percent of the ARA metric in 2022 and are projected to be comfortably within the recommended range of 100-150 percent of the ARA metric during the projection horizon.

[1] See the details of the models in IMF: Methodological Note on EBA-Lite, February 2016.

Annex II. Economic Impact of Climate Change and Natural Disasters

1. **While not being a significant global emitter, Honduras is highly vulnerable to climate change risk.** While mainly exposed to tropical storms and associated floods and landslides, the country is also exposed to higher risks of droughts and sea level rise associated with climate change. The Global Climate Risk Index (CRI) ranks Honduras 41 out of 180 countries based on the average losses as a percentage of its GDP between 2000 and 2019. Honduras' vulnerability to severe natural hazards severely compromises its economic stability and puts at risk the safety and well-being of its population.

2. **Honduras has been buffeted by recurrent extreme weather events with sizeable economic impact.** Honduras recorded over 85 climate-related hazards between 1960-2022, including Hurricane Fifi in 1974 (with economic damage of 35 percent of GDP), Hurricane Mitch in 1998 (60 percent of GDP), and tropical storms Eta and Iota in 2020 (7½ percent of GDP). The recorded losses of floods and storms average 6.3 percent of GDP per year. Climate events tend to disproportionately affect the most vulnerable population, causing greater food insecurity.

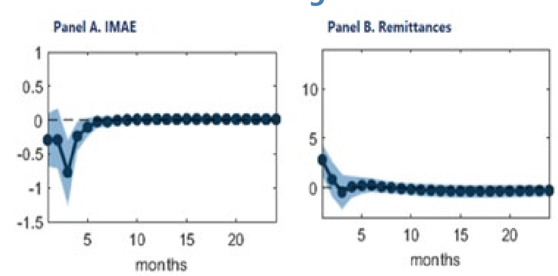
Table 1. CAPDR: Damages from Floods and Storms, 1960-2022

	Damages (% of GDP)		Rank (172 countries)	
	Average	Median	Average	Median
Costa Rica	0.81	0.31	65	74
Dominican Republic	1.24	0.21	52	90
El Salvador	2.56	1.66	33	37
Guatemala	0.99	0.31	59	73
Honduras	**6.30**	**0.47**	**18**	**65**
Nicaragua	5.35	0.22	21	88
Panama	0.17	0.04	114	149

Source: EM-DAT and IMF staff calculations.

3. **Staff analysis confirms the significant macroeconomic impact of extreme climate events.**[1] Using high-frequency indicators and various econometric techniques, staff[2] estimate that, around three to five months after an extreme weather shock, economic activity growth (y/y) experiences a contraction of around 0.75 percentage points[3] on average (Figure 1, Panel A). In contrast, remittances show an immediate increase of more than 3

Figure 1. Honduras: Response of IMAE and Remittance Growth Using Climate Dummies



Source: Kim, Chaverri, Fernandez-Corugedo and Juarros, IMF 2022.

[1] See Kim, Chaverri, Fernandez-Corugedo & Juarros, (2022). *On the Macro Impact of Extreme Climate Events in Central America: a higher frequency investigation*. IMF Working Paper 22/237.

[2] This annex presents the results of country-specific VARs estimates with a 'dummy-based' climate variable that incorporates storm and flood events to identify climate shocks. The response of the dummy variable is normalized to 1 on impact, allowing for the interpretation of the remaining responses as an impact to a climate event.

[3] The implied annual growth impact is estimated at -0.6 percentage points of GDP.

percentage points. The decrease in economic activity is mainly attributable to the shrinkage in the agricultural sector. Conversely, the increase in remittances aligns with their role in mitigating the effects of climate disasters as they function as a private insurance mechanism that supports households' consumption smoothing.

4. **Climate change is expected to further deteriorate these outcomes.** The World Bank (CCDR, 2022) estimates that under a high-emissions scenario (RCP[4] 8.5) projections, Honduras' annual mean temperature is projected to rise by 1.8 °C by 2050 and by 3 to 5.6 °C by 2100.[5] At the same time, climate change is expected to lead to declines in precipitation (resulting in more prolonged and intense droughts), while increasing events of rapid heavy rainfall volume and flooding and producing more severe hurricanes. The World Bank CCDR report emphasizes that climate change is expected to have significant impacts on key sectors in Honduras. Sectors like agriculture, manufacturing, and energy would be particularly affected, posing challenges to social outcomes as historically marginalized groups tend to bear the brunt of climate events.

5. **Accelerating adaptation measures remains essential.** Rising risks from climate change pose a significant threat to Honduras's social and economic stability, compromising external and fiscal sustainability as well as labor and supply chains. To begin addressing these risks, the government has defined a strategy to increase structural resilience and adaptation to climate change under the *Estrategia Nacional de Cambio Climático*. Nonetheless, it would be useful to broaden the scope of this strategy to specify specific actions and investments to foster structural, financial, and post-disaster resilience and integrate these into the multi-year macro-fiscal framework. This could also deepen access to financing from multilateral creditors for resilience and adaptation initiatives to undertake urgent investments supporting climate resilient infrastructure. Building physical flood defenses (mainly dams) remains essential, including for the main Sula Valley manufacturing region.

[4] Representative Concentration Pathway.

[5] Additional warming relative to pre-industrial levels. The base temperature used was 23.99ºC (World Bank, Honduras CCDR, 2022).

Annex III. Risk Assessment Matrix[1]

Sources	Likelihood	Impact	Policy
		Global risks	
Intensification of regional conflict(s). Escalation of Russia's war in Ukraine or other regional conflicts and resulting economic sanctions disrupt trade, remittances, refugee flows, FDI and financial flows, and payment systems.	H	**High**. Trade disruption, elevated commodity prices due to lower supply, cost of food and basic materials, hurting growth.	Diversify supply chains, create or increase buffers for short-term unavailability of key commodities.
Abrupt global slowdown or recession. Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and market fragmentation causing sudden stops in EMDEs.	M	**High**. Lower economic activity due to weaker demand for exports, lower remittances, tight financial conditions, spiking risk premia, fiscal pressures.	Diversify trade patterns, allow real exchange rate to cushion a portion of external shock, continue executing key infrastructure spending. Support domestic market development and labor markets.
Commodity price volatility. A succession of supply disruptions (e.g., due to conflicts, uncertainty, and export restrictions) and demand fluctuations causes recurrent commodity price volatility, external and fiscal pressures in EMDEs, contagion effects, and social and economic instability.	H	**High**. Larger import bill and current account deficit, leading to lower FX reserves; higher domestic inflation due to large share of food in CPI basket.	Provide targeted fiscal support to the vulnerable. Monetary policy to remain proactive to forestall second-round effects. In the long-term, expand productive capacity, diversify trade and increase value added content of exports.
Monetary policy miscalibration. Amid high uncertainty and financial sector fragility, major central banks pause monetary policy tightening or pivot to loosen policy stance prematurely, de-anchoring inflation expectations, triggering a wage-price spiral and spillovers to financial markets.	M	**High**. Global financial conditions tighten and emerging market bond yields increase amid outflows from emerging markets.	Allow real exchange rate to cushion a portion of the external shock while adjusting policy interest rates to support external stability. Remain committed to fiscal adjustment program to bolster market access and safeguard debt sustainability.
Systemic financial instability. Sharp swings in real interest rates and risk premia, and asset repricing amid economic slowdowns and policy shifts trigger insolvencies in countries with weak banks or non-bank financial institutions, causing market dislocations and adverse cross-border spillovers.	M	**High**. Global financial conditions tighten and emerging market bond yields increase amid outflows from emerging markets. External demand falters, with spillovers to exports.	Allow real exchange rate to cushion a portion of the external shock while adjusting policy interest rates to support external stability. Remain committed to fiscal adjustment program to bolster market access and safeguard debt sustainability. Continue executing key infrastructure spending. Support domestic market development and labor markets.

Sources	Likelihood	Impact	Policy
Sovereign debt distress. Domino effects of higher global interest rates, a growth slowdown in AEs, and/or disorderly debt events in some EMDEs spillover to other highly indebted countries, resulting in capital outflows, an increase in risk premia, and loss of market access.	M	High. Capital outflows and pressure on exchange rate prompt higher domestic interest rates. External market access is jeopardized.	Remain committed to fiscal adjustment program to safeguard debt sustainability; allow real exchange rate to cushion a portion of external shock.
Extreme climate events. Extreme climate events driven by rising temperatures cause loss of human lives, severe damage to infrastructure, supply disruptions, lower growth, and financial instability.	M	High. Disruptions in economic activity; lower GDP growth; damage to properties and infrastructure, resulting in lower growth potential.	Prioritize expenditure to support affected households. Guard against second-round effects of inflation. Accelerate reconstruction and building of climate-resilient infrastructure. Design and implement an adaptation plan.
Social discontent. High inflation, real income loss, and spillovers from crises in other countries (including migration) worsen inequality, trigger social unrest, and give rise to financing pressures and detrimental populist policies. This exacerbates imbalances, slows growth, and triggers market repricing.	M	Medium. Disruptions to economic activity, political polarization, and instability. Harms confidence, raising risk premia.	Strengthen governance and accountability to attract investment and support growth. Foster diversification and job creation. Strengthen social safety net.
Domestic risks			
Implementation risks to reform agenda. Low implementation capacity and divided Congress. Implementation slippages can jeopardize reforms and program objectives.	M	Medium. Needed reforms stall.	Retain strong commitment to build institutions and ensure policy continuity. Build broader political coalition.
Inconsistent macroeconomic policies. Inconsistency may hamper the response in the event of global shocks, with knock-on effects on domestic and external stability.	M	Medium. Inconsistent policies can undermine external and internal stability.	Monetary policy needs to support the exchange rate crawling band, the center of the crawling band should adjust more for the targeted inflation differential.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff. The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Annex IV. Implementation of 2019 Article IV Recommendations

2019 Article IV Recommendations	Policy Actions
Fiscal Policies	
• Strictly adhere to the Fiscal Responsibility Law (FRL) and maintaining the deficit of the NFPS slightly below the ceiling established in the law to maintain a sustainable path for public debt.	• The escape clauses allowed under the FRL were activated three times due to the pandemic and the adverse effects of the 2020 tropical storms. The FRL was reformed to permit a period of two years in which the fiscal path could allocate the necessary resources to address the health, social, and infrastructure emergency.
• Improve mobilization efforts by broadening the tax base.	• Various measures aimed at improving tax collection and increasing revenue streams have been implemented. These initiatives include strengthening tax administration capabilities, implementing technology-driven solutions for better tax monitoring, and enhancing tax compliance and enforcement mechanisms.
• Implement reforms in the electricity sector to reduce ENEE's technical and non-technical losses; improve ENEE's governance; reduce energy purchase costs; and introduce a new tariff scheme.	• Despite the efforts of the authorities, technical and non-technical losses have not been reduced as planned. The authorities are now implementing a national plan to reduce losses, which includes actions aimed at controlling energy theft, modernizing measurement systems, and improving the infrastructure of the electrical system.
Monetary and Exchange Rate Policies	
• Remain vigilant to assess whether the evolution of global financial conditions, as well as inflation and inflation expectations, warrant further adjustments in the policy rate. Continued developing monetary and exchange rate markets to transition towards inflation targeting.	• The central bank raised the monetary policy rate in 2019 to contain inflationary pressures prior to reducing the rate during the pandemic. The authorities have opted not to progress further towards an inflation targeting regime at the current moment.
• Introduce reforms to the central bank law to strengthen governance at the BCH.	• A reform to the organic law of the central bank was submitted to Congress, but not approved, during the previous administration. Current authorities do not consider it necessary to reform the objectives and attributions conferred by the current law.
• Phase out FX surrender requirements and the gradual development of interbank FX transactions and rules for intervention.	• The surrender requirements for exchange agents were gradually eliminated until they were completely removed in June 2021. The interbank foreign exchange market thereafter became the

2019 Article IV Recommendations	Policy Actions
	only means for banks/FX agents to transact FX among each other, as the BCH auctions were eliminated. However, the authorities reintroduced the 100 percent surrender requirements in April 2023 for banks and other exchange agents and reinstated the BCH's FX auction system.
Financial Sector Policy	
• Macroprudential polices should be the first line of defense to address rapid credit growth if the expected deceleration fails to materialize.	• The CNBS (National Banking and Insurance Commission) used macroprudential measures to safeguard the stability of the financial system in response to the adverse effects of the pandemic, introducing grace periods for debtors and measures to strengthen the capital of financial institutions.
• Continue with the adoption of a risk-based supervision system.	• The CNBS continued to make progress toward implementing risk-based supervision, introducing a framework to assess market conduct risks, enhancing stress testing capacities, and strengthening the regulatory framework in line with Basel III standards—specifically by starting a gradual introduction of the capital conservation buffer and liquidity coverage ratio.
Governance	
• Improve the registry of legal persons through a systematization of databases to achieve an adequate identification of beneficial ownership.	• This has been completed.
Structural Reforms	
• Simplify administrative procedures in the public sector to reduce discretion and the time needed for approval.	• Authorities submitted draft legislation to the National Congress requiring regulatory agencies to streamline and publicize requirements for obtaining permits and other administrative procedures (*Executive Decree PCM-045-2019)*, but it was not approved. The new authorities are again working on such a reform (MEFP ¶46).
• Use of information technology to reduce transaction costs.	• The authorities developed a plan for the adoption of electronic signatures and approved *The Regulation for the Use and Operation of the Electronic Signature at the Secretary of Finance (Agreement Number 283-2021).*
Source: IMF staff.	

Annex V. Implementation of 2016 FSSR 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/Concluded
Complete the regulatory framework on market and liquidity risk	Near term/Partially completed
Enhance the supervisory capacity building program	Medium term/Completed
Intensify efforts to improve AML/CFT, taking into account 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/Completed
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/Completed
Insurance Regulation and Supervision	
Restore resources to the Insurance Superintendency to allow it to complete its RBS program	Near term/Completed
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/In progress
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/Completed
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/Completed
Coordinate BCH and CNBS work to ensure the smooth integration of macroeconomic and financial models	Near term/Completed

Appendix I. Letter of Intent

September 1, 2023

Ms. Kristalina Georgieva
Managing Director

International Monetary Fund
Washington, DC 20431

Dear Ms. Georgieva,

1. **Honduras is facing among its most severe social and economic crisis.** This has been marked by high levels of public-private corruption over the last decade, including the scourge of drug trafficking, that have led to an increase in the fragility of the main governmental institutions. More recently, the pandemic and its aftermath, tropical storms and global warming have deteriorated social conditions and increased poverty. The external economic shocks as a result of the war in Ukraine and the deterioration of financial conditions due to the increase in international interest rates have led to higher inflation in fuels, food, fertilizers and other imported inputs, affecting thousands of families and generating more migration.

2. **The Government of President Xiomara Castro believes that it is necessary to approve structural reforms to put the country on a path of development.** These reforms will also support greater, inclusive and sustainable economic growth. A program with the IMF will improve the management and sustainability of public finances, as well as macroeconomic stability, and would support our policies to reduce poverty, protect the most vulnerable population, and combat public-private corruption.

3. **To restore confidence and credibility in our democratic institutions, our government approved several legal reforms during 2022-2023.** We returned to the constitutional principle of a Treasury Single Account, eliminating trust funds that weakened the transparency of public spending and, therefore, created corruption. As part of our fight against corruption, we also began the process for the installation of the International Commission Against Corruption and Impunity in Honduras (CICIH), as an independent and autonomous mechanism. We repealed the Secrecy Law, which hindered access to much public information, and the laws that limited the investigative activity of the attorney general. We strengthened our anti-money laundering framework in accordance with international standards, repealing decree 57-2020 and modifying decree 93-2021, and we have submitted a law to Congress to create a beneficial ownership registry. Likewise, the Law on Tax Justice which reduces tax expenditures, by limiting tax exoneration and exemption regimes, and the repeal of banking secrecy for tax reasons in accordance with

international standards, have been submitted to Congress.

4. **To minimize the impact of the international crisis that increased prices, affecting the most vulnerable population, we adopted measures which are supporting our economic and social conditions.** The Government subsidized fuel prices and provided free energy to poor households; granted "*bonos tecnológicos*" (productivity-enhancing assistance in the form of seedlings and fertilizers) to our small farmers, ranchers and coffee growers; lowered interest rates for social and middle-class housing; and facilitated loans to the agricultural sector at low interest. To assist households in extreme poverty and vulnerable groups in a focused manner, we have been implementing the flagship programs of the President, *Red Solidaria* and *Proasol*, since late last year. In order to create more fiscal space for these initiatives and to create a solid and secure environment for private investment in the energy sector, we continue to implement the necessary energy sector reforms, including the National Loss Reduction Plan of our national power company (Empresa Nacional de Energía Eléctrica, ENEE).

5. **We consider the policies contained in attached Memorandum on Economic and Financial Policies (Annex I) well suited to achieve the objectives of our economic program, and to underpin our democratic institutions, poverty reduction and equitable and sustainable economic growth.** The attached memorandum describes the progress and key elements of our policies that will allow us to (i) maintain sound macroeconomic management and fiscal discipline to preserve the sustainability of public finances; (ii) guarantee the protection of and social investment in favor of the most vulnerable, including the guarantee of food security; (iii) implement and accelerate sustainable public investment to improve growth with a climate adaptation focus; (iv) reinforce the internal and external stability of our currency; and (v) continue strengthening governance and the fight against public-private corruption. The Government of Honduras believes that these policies are adequate to achieve the objectives of its program. We stand ready to take any additional measures that may become appropriate. We will engage with the Fund on the adoption of these measures, and in advance of any revisions to the policies contained in this memorandum, in accordance with the Fund's policies on consultations. Such consultations will also take place in line with Honduras's legal framework. The success of this program, however, requires the commitment of civil society, private business, and economic actors to promote certainty and favorable conditions for greater investment and the country's economic and social stability.

6. **In support of our program, we are requesting a 36-month arrangement under the Extended Credit Facility and under the Extended Fund Facility for a total of SDR 624.5 million.** The arrangements we are requesting will be used as budgetary support and will signal our commitment to implementing sound economic policies which will allow us to attract and steer external financial assistance, boost investor confidence, and reaffirm the social consensus among the Honduran people in favor of the reform program.

7. **About the Climate Finance Program.** Honduras intends to apply, as part of a future review of the program, for support under the Resilience and Sustainability Facility (RSF) to reduce the risks in the stability of the balance of payments related to climate change and the eventuality of pandemics.

8. **The program will have semi-annual reviews.** The quantitative and indicative program targets are set out in Table AI.2 of the attached Memorandum of Economic and Financial Policies (MEFP). We also provide a list of prior actions and structural benchmarks in Table AI.1. We will share all the information necessary to monitor the performance of the program agreed with the Fund and complete its reviews as indicated in the Technical Memorandum of Understanding agreed with the Fund (Attachment II).

9. **In keeping with our commitment to transparency, we will keep the public and the international community informed and we authorize the IMF to publish this Letter of Intent, its annexes, and the Fund staff report, as well as all future program documents.**

Sincerely,

/S/

Rebeca Santos

President, Central Bank of Honduras

/S/

Rixi Moncada

Secretary of Finance

Attachments (2)

Memorandum of Economic and Financial Policies

Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

A. Background and Outlook

1. Honduras is faced with an adverse international environment, the strong impact of domestic public debt and public-private corruption, the aftermath of the pandemic, vulnerability to climate change, violence, migration, poverty, and other structural challenges. Although most economic activity has surpassed pre-pandemic levels – with the exception of agriculture as a result of tropical storms in 2020 and heavy rains in 2022 – the recovery of the labor markets remains incomplete, informality worsened, and during the 2010-2021 decade, public debt, public-private corruption, and poverty (74 percent) increased markedly. In addition, about one third of our population is at risk of food insecurity, with children being the most affected. Honduras is also one of the most vulnerable countries in the world to climate disasters. The double blow of tropical storms Eta and Iota in 2020, the pandemic, and high levels of violence remain critical issues and continue to fuel migration.

2. High commodity prices had a profound effect on our country, but the government acted quickly to minimize the impact on the population. Driven by increases in prices for fuel, fertilizers, and other inputs, inflation has been especially high for food. Our administration acted quickly to help mitigate these shocks. We implemented a fuel subsidy, provided free electricity to poor households, granted "*bonos tecnológicos*" (productivity-enhancing assistance in the form of seedlings and fertilizers) to our small farmers and coffee growers, and provided credit to the agricultural and housing sectors at low interest rates, while the Central Bank of Honduras (BCH) accelerated the absorption of liquidity through open market operations. These measures were essential to contain inflation. The most vulnerable population, however, will need greater support, which we are providing through the President's flagship program, "*Red Solidaria*," and other complementary interventions in the social sectors, in addition to promoting a robust public investment program with an emphasis on climate change.

3. Our economic program is focused on reducing poverty and improving climate resilience in order to support inclusive and sustainable growth while preserving economic stability. Strengthening institutions, transparency, combating public-private corruption, and governance, together with improving the management of public finances, are essential to ensure the proper use of our resources. We have already passed and are implementing laws to eliminate trust funds, which have made public spending opaque and difficult to monitor. We have submitted to the National Congress the Law on Tax Justice, which is aimed at reining in tax exemptions and strengthening our controls to make the tax system fairer and more equitable. Likewise, the implementation of urgent reforms in the energy sector is critical in order to reduce costs and losses in the sector and ensure a sufficient supply of electricity. In order to promote growth, it is necessary to preserve macroeconomic stability within an environment of economic equity and social equality.

4. Short-term economic risks have deepened, which could exacerbate the difficult economic situation we are facing. In addition to the external risks of slower growth in the United States and a worsening of our terms of trade, the current drought conditions that Honduras and the region are experiencing may have a very disruptive effect on our economy. The impact on agriculture is already beginning to be felt, which could lead to significant losses for the sector, higher food prices, and greater poverty. Domestic and regional energy production presents problems, especially due to the lack of investment in the areas of transmission and distribution; the power generation contracts, 80 percent of which are privatized; and the high electricity losses, coupled with the low water levels in reservoirs. This situation as a whole makes it necessary to purchase energy, so the impact on international reserves must be considered.

5. Support from the IMF is important in order to finance the gap in our balance of payments and meet our fiscal needs. The already high prices for food, fuel, and fertilizers have risen significantly since the war began in Ukraine, aggravating the plight of our population, especially in terms of food security. While our financing needs are affected by global shocks, they are also a consequence of past neglect; for example, reconstruction after tropical storms Eta and Iota in 2020 remains incomplete and the country requires major public investment. The program will bolster economic stability, while also supporting social spending and reducing critical infrastructure gaps. The financing from the IMF will help maintain international reserves at adequate levels.

B. Fiscal Policies

6. Our administration is committed to maintaining budgetary discipline and creating fiscal space for spending on investment and social assistance. Our aim is to improve the composition of spending, orienting it more towards investment and social spending. Public investment will be focused on infrastructure, the road network, the energy sector, the hospital network, school repairs, food security, social protection, and adaptation to climate change. In terms of tax collection, our main objectives are to make it more equitable, to reform and improve the oversight over exonerations and exemptions, and to strengthen tax and customs administrations (see below). We are also addressing the situation at the national power company (Empresa Nacional de Energía Eléctrica, ENEE) to ensure its financial stability and an adequate supply of electricity (see ¶29). We will also continue to ensure debt sustainability and the timely payment of debts falling due. The program includes a ***quantitative performance criterion*** of no accumulation of external arrears.

7. Spending restraint and tax administration efforts allowed us to achieve a balanced budget in 2022. The low fiscal deficit reflects high tax revenues driven by the growth of our economy; solid performance in the collection of income and sales taxes and customs duties; as well as measures implemented to combat tax evasion, coupled with limited budget execution. In 2022, revenue collection was 0.9 percent of GDP higher than budgeted, while spending execution was slower. Current and capital expenditures were 0.3 and 3.3 percent of GDP lower than budgeted, respectively. This low execution has resulted from the need to restructure the government, the process of eliminating trust funds, and the review and updating of studies for investment project to ensure their transparency.

8. Our priority is to boost infrastructure investments to support economic growth and reduce poverty:

a) A considerable part of the reconstruction after tropical storms Eta and Iota – with damages of 5 billion lempiras in the housing, education, and transportation sectors – is still unfinished, leading to even more poverty. We estimate that investment totaling ½ percent of GDP will be needed over the next three years to complete this reconstruction.

b) In order to address the critical investment needs of ENEE, our public electricity utility, and our country's growing need for energy, we estimate that $3 billion (9 percent of GDP) in investments will be needed over the next six years, with approximately half for generation and the other half split between transmission and distribution.

c) Finally, adaptation to climate change will require investments to decrease the vulnerability of Honduras to climate shocks (¶55-57 below). In particular, five new dams are needed to store water and to protect certain regions of the country against flooding. We estimate that the cost of building these five dams could amount, in total, to 15 percent of GDP over the remainder of this decade.

9. Our fiscal policies seek to anchor fiscal stability and discipline without sacrificing social and capital investment. Under the Fiscal Responsibility Law (2016), which was adopted to control excessive debt, the exception clause was activated three times in less than two years due to the pandemic, tropical storms Eta and Iota, and, during our government's administration, the exception clause was interpreted to ensure social and capital investment; thus, it will be necessary to continue with this interpretation or, as appropriate, for the National Congress to adopt a reform to continue guaranteeing social and capital investment in support of the most vulnerable. Over the next few years, we will gradually reduce the deficit in order to reach 1 percent of GDP by the end of the program, which is critical to maintaining fiscal stability and debt sustainability. The program will remain flexible and the fiscal path over the life of the program will allow for the inclusion of higher capital expenditures for the development of productive and social investment projects that are already provided for under the Government Plan. We will ensure that the financing of these projects is properly identified. The program includes a ***quantitative performance criterion*** on net lending/borrowing of the nonfinancial public sector.

10. Making the tax system more equitable and reducing high and inefficient tax expenditures. Tax expenditures in Honduras (7.6 percent of GDP) are much higher than elsewhere in the region (3.6 percent of GDP) and make the tax system inequitable and difficult to administer. Our Law on Tax Justice bill seeks to reform tax exemptions while at the same time respecting acquired rights. After extensive public discussion, we have already submitted to the National Congress this bill, which has been prepared with technical assistance from the IMF. This bill includes measures to improve the Honduran tax system. In addition to reforming exemptions, it (i) strengthens controls over exempted companies; (ii) repeals the decree that allows companies under export regimes to sell their products in the local market; (iii) reinstates the principle of worldwide income in our tax code; and (iv) suppresses banking secrecy for tax reasons, while safeguarding confidentiality. We expect Congress to pass the Law on Tax Justice by ***December 2023 (structural benchmark).*** With the support of the IMF, we will work on regulations to implement the Law on Tax Justice, and in particular to define the processes properly so that they are objective and transparent. We submitted to Congress, together with the Law on Tax Justice, a decree to ratify the Convention on Mutual Administrative Assistance in Tax Matters (MAAC), which will promote international cooperation by our tax administration. We expect that Congress will also pass this decree by ***December 2023 (structural benchmark).***

11. A more efficient tax administration is also key to making the tax system fairer and curbing tax evasion and fraud. The program includes an ***indicative target*** on the tax revenue of the Central Government. We have an ambitious program in the following areas, which will be strengthened by the passage of the Law on Tax Justice:

a) At the heart of our tax administration reforms are the comprehensive joint action plans for the Revenue Administration Service (SAR), the Customs Administration, and the Ministry of Finance (SEFIN), which were developed with technical assistance from the IMF. The measures will make tax administration more effective, particularly through better control of special regimes, an area that had been neglected in the past. We will continue to improve coordination among SEFIN, SAR, Customs, and other institutions involved in the administration of special tax regimes. To this end, we already signed in February 2023 an inter-institutional cooperation agreement among these three institutions on procedures to better monitor benefits related to exemptions and implement audits of exempted taxpayers. With the assistance of the Inter-American Development Bank (IDB), we are working on two projects related to tax administration: (i) a comprehensive reform of the Honduran Customs Administration that will further strengthen the efficiency of our revenue administration and (ii) the development of new information management systems, including a platform for the exchange of information among government institutions.

b) We are taking steps to make the tax system more accessible and transparent for our taxpayers, while improving its efficiency and fairness. To this end, we are preparing actions to establish a risk-based sales tax refund system to replace the *ex-ante* sales tax exemptions, which are difficult to monitor. The IMF is providing us with technical assistance.

c) The SAR is working to strengthen its tax and forensic audit capabilities, increase fiscal transparency, and align Honduras with international conventions. The approval of the MAAC will help advance these efforts.

C. Social Safety Net

12. In response to higher fuel, food, and fertilizer prices in 2022, we rapidly deployed measures to provide social support. In particular, we reduced the fuel tax by 10 lempiras per gallon and we have promoted teleworking in the public sector. We consider access to electricity to be a human right and therefore we began providing electricity free of charge to poor households consuming less than 150 kWh per month, with 60 percent of the cost borne by the state, while 40 percent is financed by large consumers through a cross-subsidy. We have focused on the poorest areas, reducing the number of eligible households to 900,000. In addition, we temporarily halted an increase in electricity rates in July 2022, as it would have led to rate increases in the 10-12 percent range for many households, which would not have been socially sustainable, but we eliminated this subsidy in January 2023. We also established a subsidy that sets a maximum ceiling for the price of LPG gas cylinders, as well as a subsidy for urban bus fares.

13. We remain strongly committed to protecting and strengthening social spending, which is key to reducing poverty. As part of our commitment to safeguarding and expanding resources provided to the most vulnerable, our program includes an ***indicative target*** for priority social spending, with a commitment to increase these expenditures over the course of the program. To help improve and guide our fight against poverty and as part of the program, we will update our poverty reduction strategy paper ***by July 2024***, thereby complying with this requirement for programs financed by the IMF Poverty Reduction and Growth Trust, prior to the second program review. In order to create sufficient space for social spending, we are committed to optimizing its targeting and continuing to control other current primary expenditure (***indicative target***).

14. The development of our rural agricultural sector is essential to support economic growth and curb migration. The agricultural sector in Honduras can make a significant contribution to curbing food inflation by expanding its production of staple foods. We have delivered 100,000 "*bonos tecnológicos*" consisting of free seeds and fertilizers to small producers living in extreme poverty in the *Dry Corridor* region. In addition, we injected 1 billion lempiras into our National Agricultural Development Bank (Banadesa) during 2022 and 2.4 billion lempiras this year to provide subsidized loans to producers of staple grains. Likewise, loans have been provided for agricultural food production on favorable terms through the Honduran Bank for Production and Housing (Banhprovi).

15. We are strengthening the design of our social safety net through the *Red Solidaria* program. *Red Solidaria* – a comprehensive social assistance system introduced in November 2022 – includes programs that are efficiently administered and have broad coverage focused on extreme poverty in some 2,000 villages selected for their precariousness and social vulnerability. The latter is a necessary compromise given the scarcity of resources and widespread poverty in our country. The beneficiaries were identified using an objective and transparent methodology – supported by the IDB and the World Bank – through a census of extreme rural poverty. The data for the 350,000 households that participated in this census and are served by *Red Solidaria* were entered into the Honduran Beneficiary Information and Registration System (SIRBHO). Conditional cash transfers represent the largest component of *Red Solidaria*. Other components are focused on improving health and education services, strengthening labor market integration, and improving local infrastructure such as rural roads important for agricultural production. We are working toward expanding *Red Solidaria* to 100,000 households in 500 marginalized urban areas. In order to reach these families, we are working with the help of the World Bank on a census of extreme poverty. We will complete this census and enter the data in SIRBHO by ***September 2024 (structural benchmark).***

16. *Red Solidaria* will be complemented by other social programs. The Solidarity Action Program (PROASOL) is a program that complements the *Red Solidaria* and assists vulnerable groups, including children, the elderly and people with disabilities, indigenous groups, and the LGBT community, among others. Finally, we will implement other social programs as needed, such as the National Scholarship Program.

17. Social welfare institutions are working on a proposal to reform the social safety net. The pension institutes are working on and conducting nationwide public discussions of a draft social protection law to be submitted to Congress by June 2024, for which they have received support from the Economic Commission for Latin America and the Caribbean (ECLAC).

18. To facilitate the design, monitoring, and transparency of our social programs, we are creating the Single Social Sector Information System (SUISS). SUISS will bring together and centralize information generated by the existing data systems within the Social Cabinet such as SIRBHO, the Registry of Institutional Programs and Social Organizations (ROPI), the Returned Migrant Assistance Registry Information System (SIAMIR), the Program Monitoring System (SIMOP), the Migration Observatory Data System managed by the National Autonomous University of Honduras (UNAH), the School Lunch Monitoring System (SIMME), the Poverty Measurement Panel and its indicators, the Social Intervention Management System for Children, the Rural Roads Monitoring System, and the Health Sector Intervention Monitoring System. This system is being developed by the Social Development Observatory of the Ministry of Social Development (Sedesol) and will provide updated information on the socio-economic status of households through the systematic recording of social, economic, and environmental variables. The system will help improve the effectiveness and coverage of social assistance programs by targeting the population living in conditions of poverty and vulnerability. We are committed to making SUISS operational by ***June 2024 (structural benchmark).***

D. Quality of Spending and Structural Fiscal Measures

19. Better practices in public investment management. We will choose projects that are well planned and have the highest social return. Our implementation capacity is gradually being strengthened due to the change in government and restructuring of the previous regime's administration. We have also already requested an updated public investment management assessment (PIMA), which is expected by the end of this year, to help us improve our investment management. The reform of procurement procedures is essential to speed up project implementation.

20. We have been eliminating the trust funds that created considerable opacity and corruption in the execution of public spending. In 2022, we approved decrees to eliminate trust funds. Their integration into the budget improves transparency and expenditure control by subjecting all resources to the budget process, and this also improves liquidity management. We have already incorporated the funds of most of the trusts into the accounts of the General Treasury of the Republic. We are currently in the process of liquidating some trust funds, namely *INVEST-H*, *Tasa de Seguridad*, *Vida Mejor*, and *Instituto de la Propiedad (IP-SITEC)*. We are also conducting an audit of the transactions undertaken outside of the contracting laws and are complying with the payment of outstanding obligations that are duly verified. We will complete this process, quantify trust funds' assets and liabilities and integrate them into the government's financial statements, and record as part of public debt those debts of trust funds (including those to suppliers) that are in compliance with the law by ***December 2024 (structural benchmark).*** The 2023 budget already incorporates resources from the liquidation of private trust funds that executed budgetary resources.

21. We are working to strengthen the Treasury Single Account to improve liquidity and debt management as part of the reorganization of public finances. The integration of trust funds is an important part of this process. In addition, with technical assistance from the Regional Technical Assistance Center for Central America, Panama and the Dominican Republic (CAPTAC-DR), SEFIN has improved its liquidity projections and has implemented cash management aimed at anticipating future cash flow. The Treasury Single Account, however, has regulatory limitations with many funds earmarked for specific purposes, which do not allow for their fungibility, and as a result, good liquidity management becomes more difficult. We are finalizing a new Special Law to Strengthen the Single Treasury Account, with support from the IMF. We will submit this law, which has also benefited from IDB technical assistance, to the National Congress by ***March 2024 (structural benchmark).*** Once this law is passed, we will make it operational by ***December 2025 (structural benchmark)*** in order to strengthen the Treasury Single Account.

22. The materialization of risks could trigger additional expenditures. Honduras is highly vulnerable to adverse weather events, while other economic shocks and emergencies may require government assistance to mitigate the adverse effects on the most vulnerable or on revenue collection. We plan to conserve fiscal space by carefully prioritizing expenditures in line with our planning, and to continue close monitoring of the fiscal risks of public companies and public-private partnerships, considering the legal problems caused by contracts that violated the Constitution of the Republic and ordinary laws, as well as the various complaints filed regarding public-private corruption offenses, which result in liability for public officials.

E. Financing

23. The critical conditions under which we took over the public finances in 2022 led us to use monetary financing from the central bank as a last resort. Against the backdrop of the State of Fiscal and Financial Emergency in the Public Sector declared by a Legislative Decree approved by the Congress of the Republic in February 2022, the Ministry of Finance negotiated an exceptional loan of US$1 billion with the Central Bank of Honduras to meet service obligations related to inherited debt and to finance urgent public investment projects, since our government inherited a large part of the public finances pledged through trust funds, and a

Treasury with insufficient funds to meet its obligations, aggravated by the international increase in the price of fuel and fertilizers, among other things. Our government took over the country in a situation of a financial emergency and humanitarian crisis, and in this context we plan to establish a schedule for the issuance of public bonds in 2024. Furthermore, taking into account the strength of our economic program and the transparency and efficiency in the management of public resources, we would not obtain monetary financing from the BCH in normal times (***quantitative performance criterion***). In the event of an emergency, the most appropriate response will be in line with our legal framework and the objectives of our program.

24. Continued development of domestic bond markets is key to financial deepening. We recognize the need to further develop domestic debt markets and to continue diversifying the government's sources of financing. We will continue to work in line with our Medium-Term Debt Strategy and the Public Borrowing Policy (PEP) within the framework of the 2024 Budget. The Public Credit Committee will approve the Public Borrowing Policy and we will publish it on the website of the Ministry of Finance by ***September 2023 (structural benchmark).*** We will also prepare a Medium-Term Debt Strategy and we will publish it on the website of the Ministry of Finance by ***December 2023 (structural benchmark).*** In addition, we will publish a schedule for the issuance of public bonds no later than ***January 2024 (structural benchmark)*** for execution in 2024, which will help with the development of domestic markets. Our objective is to diversify the sources and forms of financing and for the government to start issuing bonds this year.

25. International financial support will be needed to strengthen the program. We are negotiating financing with the Central American Bank for Economic Integration (CABEI), the IDB, and the World Bank, and we hope to complete the process of becoming a member of the development bank of the Andean Development Corporation (CAF), among others. This financing will be important for investment spending, especially in the social, energy, and infrastructure sectors. We hope that our program will build confidence and catalyze funding from multilateral and bilateral donors. As international financial conditions normalize and our policies make our economy more resilient, we also plan to access the international debt markets with a thematic bond issue.

F. Energy Sector

26. We remain committed to improving the condition of our energy system and public power company ENEE to support long-term growth. Due to high contracted energy costs, technical and non-technical losses in transmission and distribution (amounting to about 35 percent), and a lack of investment in the entire network, ENEE has had deficits in excess of 1 percent of GDP for many years. As a consequence of the measures implemented during our administration based on the new Energy Law, we have achieved a reduction in the deficit to 0.8 percent of GDP in 2022 and we have started to implement a National Loss Reduction Plan (¶29). In order to address this critical situation and our country's growing need for energy, however, a comprehensive strategy that encompasses all aspects of the energy sector will be necessary.

27. We have made significant progress in the renegotiation of contracts with private power suppliers to reduce generation costs. As established in the new Energy Law passed by Congress in April 2022, we initiated a renegotiation process with private electricity suppliers for 28 contracts that had irregularities. In the first phase, we negotiated 23 contracts (650 MW), which has led to improved rates for consumers and represents significant savings. We recognize that Honduras needs to expand its generation capacity in order to provide security and stability in the delivery of electricity, and we are working toward this goal.

28. We will continue to implement a fair pricing system to ensure ENEE's recovery in the short and medium term. The Honduran electricity pricing system is designed to cover all generation, transmission, and distribution costs in the rate. Over time, studies have been conducted to provide estimates that better reflect actual costs of these components of electricity rates. In 2022, we concluded the value added in transmission (VAT) study and incorporated the results obtained in the calculation of the rate effective as of January 2023. We will reflect the results of the value added in distribution (VAD) study by January 2024. Nonetheless, ENEE continues to record significant operating losses (close to 6 billion lempiras in 2022), and according to the calculation methodology the rate can reflect only up to 15 percent of lost electricity. Reducing these electricity losses is key to ENEE's financial sustainability (see next paragraph). SEFIN will provide transfers to ENEE to cover the subsidies.

29. A reduction in technical and non-technical losses will be key to ensuring ENEE's financial sustainability. At the end of November 2022, we launched ENEE's National Loss Reduction Program (PNRP) as a cornerstone in the rescue of the public company and the recovery of the government's finances. The program calls for reviewing the circuits that produce the greatest losses, installing conventional and smart meters, and inspecting the installations of medium-size and large consumers in order to combat energy theft and reduce electricity losses. By the end of 2023, we expect to install some 180,000 residential meters and 600 telemeters for medium-size and large consumers. Our goal is to reduce losses to the international average of 15 percent. To help reduce non-technical losses, the Ministry of Finance has ensured, starting this year, that all government institutions will properly fulfill their obligations to ENEE in a timely manner. In 2023, we have continued to face some supply delays, but we will be able to stabilize the electricity losses this year. Our program includes an ***indicative target*** for these technical/non-technical distribution losses, which should decrease over time. Starting in 2024, the plan's goal is to reduce these losses by 4 percentage points per year. To enable public monitoring of our efforts, we will publish monthly statistics of ENEE's technical/non-technical distribution losses within 45 days of the end of each month on the websites of ENEE and the Ministry of Finance.

30. ENEE will continue the process of clearing the inherited debt through various initiatives within the framework of the new Energy Law. ENEE's accounts payable amounted to 16.5 billion lempiras at the end of 2022, of which 9.8 billion lempiras were arrears, i.e., invoices more than 45 days past due. ENEE issued bonds in December 2022 and January 2023 in the amount of 6.6 billion lempiras, which were placed through an auction mechanism, and the funds raised were used to pay part of the arrears. In 2023, placements totaling 8.2 billion lempiras in authorized bonds will be made, which will stabilize ENEE's arrears situation. We are committed to continuing the efforts to reduce ENEE's stock of overdue invoices, prioritizing arrears with those electricity suppliers with whom we have successfully renegotiated contracts ***(quantitative performance criterion)***.

31. We are working to transform the public company ENEE into an integrated, secure, and efficient entity. In order to improve ENEE's efficiency, we have been working on separating the administrative functions of generation, transmission, and distribution. We will improve ENEE's financial transparency over the course of the program: We will adapt its accounting to international financial standards and will work to publish duly audited annual financial statements. In the last few years, ENEE granted an onerous private contract through a trust fund for the reading of meters, billing, and collection for services, and for the reduction of technical and non-technical losses. This contract, after having been under government intervention for several years expired on August 18, 2023. Intervention by our administration succeeded in stemming the upward spiral of losses. ENEE should once again assume the distribution function through an orderly transition that establishes the relevant procedures, considering the magnitude of the responsibility. Our administration is committed to maintaining the state-owned company.

G. Monetary and Exchange Rate Policies

32. Inflation started to moderate in late 2022 and is expected to end this year between 5 and 6 percent. Year-on-year inflation reached 9.8 percent at the end of 2022, reflecting global inflationary pressures from rising commodity prices, disruptions in supply chains due to the pandemic, and the conflict in Eastern Europe, which affected energy and food prices in particular. Imported inflation accounted for nearly 5 percentage points (51 percent). Inflationary pressures are already declining significantly – to a year-on-year change of 5.15 percent in July 2023 – reflecting the easing in fuel prices, as well as the effect of the exchange rate, monetary, and fiscal measures we adopted with the aim of mopping up excess liquidity, moderating exchange rate volatility, and granting energy and fuel subsidies, which taken together reduced year-on-year inflation by 2.85 percentage points at the end of 2022. We expect prices to continue to decline as external supply shocks dissipate. Nonetheless, upside risks remain, mainly due to the recent increase in oil prices in international markets, the ongoing drought and electricity supply difficulties. Inflation is expected to converge to the BCH's 4.0 percent (± 1.0 percentage point) target range in the first half of 2024.

33. The BCH has continued the process of mopping up excess liquidity, causing a rate adjustment that helped to temper the ramp up in inflation. BCH market operations have reduced the excess liquidity in the financial system by more than 25 billion lempiras, or 3.3 percent of GDP, compared to the end of 2021, by increasing the amounts offered in securities auctions, thereby creating greater monetary absorption. This caused the interest rates on BCH bills and the interbank rate to rise. The latter rose from 1 percent to 3.48 percent. The resources associated with the excess liquidity were used to finance loans and thus contribute to the economic recovery. In order to create more space for the interbank market and contribute to the disinflation process, on August 24th the BCH modified the interest rate corridor, adjusting the Permanent Credit Facility (FPC) rate to 4.0 percent (***prior action***). The program includes a ***quantitative performance criterion*** on the BCH's stock of domestic assets.

34. The BCH will continue to implement a set of monetary and exchange rate policies to contain inflationary pressures and that are consistent with our crawling-band exchange rate regime. We remain committed to monitoring inflation closely and we stand ready to take the necessary measures and use the policy tools at our disposal to: (i) ensure that inflation continues on a downward path and that possible domestic/external shocks do not have second round effects on inflation; (ii) keep inflation expectations anchored; and (iii) strengthen the use of monetary policy instruments, such as the monetary policy rate (TPM), open market operations, and legal reserve requirements. We will monitor trends in international interest rates in order to maintain the consistency of our monetary and exchange rate policies and preserve the positive dynamics of our economy, while avoiding exchange rate pressures. We will maintain active communication with market participants.

35. We remain committed to improving the operational framework for monetary policy to enhance its effectiveness, in line with the mandate of the current law, and we will therefore continue to develop analytical tools to improve our understanding of the behavior of the transmission mechanism of the monetary policy rate (TPM), including its channels, effectiveness, and lags, and the reaction of the national financial system to changes in the instrument. We will revise the current operational framework to bring it into line with international best practices in accordance with the socio-economic reality of Honduras. These revisions will be aimed at improving open market operations, the functioning of legal reserve requirements, and coordination between the BCH and SEFIN. Finally, we are carrying out a process of public discussion and consultation with different segments of Honduran society to determine the way forward for modernizing the country's digital payment systems.

36. In terms of our exchange rate policy, we are committed to strengthening our crawling-band regime and maintaining the real value of the lempira. We believe that coordination and consistency of fiscal and monetary policies are essential for macroeconomic stability in Honduras. The BCH is committed to acting, in accordance with its mandate and instruments, to ensure that exchange rate management maintains internal and external economic stability; supporting the country's productive capacity, trade, economic growth, and strengthening of international reserves; and to conducting a study, with the support of technical assistance from the IMF, to evaluate and strengthen the crawling-band regime within the context of our current system, and the appropriate responses to external shocks, taking into account the need to preserve the positive impact of remittances for the families that receive them. Subsequently, the results of the study will be evaluated for possible incorporation into this program.

37. Honduras has a healthy level of international reserves, but we have adjusted our policies to safeguard them. A priority of our program is to maintain solid reserve coverage and a robust external position; accordingly, it includes a ***quantitative performance criterion*** on net international reserves. At end-2022, our gross international reserves were equal to $8.7 billion – about a coverage of almost six months of imports – although high commodity and fuel prices limited our build-up of reserves during the year.

38. The BCH reactivated the foreign currency auction system in order to improve certainty and fairness in the allocation of foreign currency. In this context, we saw a decrease in volumes traded in the interbank foreign exchange market (MID), especially in the second half of 2022. This resulted in an inequitable allocation of foreign exchange, with large clients favored in the allocation of foreign currency at the expense of smaller bidders. We tried to remedy this situation through BCH interventions in the MID and by aligning the fees that banks can charge customers and in the MID to further develop the latter. In the first quarter of 2023, we provided foreign exchange directly to fuel importers and issued a regulation requiring foreign exchange dealers to sell 25 percent of their foreign exchange inflows in the MID. However, these measures did not resolve the preferential and inequitable allocation of foreign currency in the MID. Due to this, the foreign currency auction mechanism was reinstated, a measure that came into operation on April 13 of this year, whereby foreign exchange dealers must transfer to the BCH 100 percent of foreign currency receipts, which are subsequently auctioned – at least 80 percent of the receipts – to economic agents. Foreign exchange is awarded to the bidders offering the best prices within a band of ±1 percent around the center of the exchange rate band. The purpose of this measure is to stabilize the foreign exchange market, reduce speculative pressures on the demand for foreign currency and the exchange rate, and meet the demand for foreign exchange accounting for the seasonality of its flows and the cycles of economic activity, with an equitable distribution among all participants.

39. We will continue to strengthen the mechanisms for the allocation of foreign currency so that it remains equitable and transparent. The evidence indicates that the modifications to the foreign exchange policy framework have been appropriate and handled prudently, both by the authorities and by economic agents. In this regard, we will carry out a diagnostic assessment, with the support of the IMF, of the conditions and measures necessary to improve efficiency in the allocation of foreign currency. Based on the results, the BCH will take the actions it deems necessary to safeguard the national interest and economic stability, and to transition gradually during the life of the program to a balanced, competitive, and efficient foreign exchange allocation system that allows for price discovery and reflects foreign exchange supply and demand. During this process, we will ensure that all the prerequisites for its proper functioning have been identified and addressed in a way that protects and guarantees the country's exchange rate stability and the rights of economic agents to purchase and sell of foreign currency at equal conditions. Taking into consideration the nature of our banking system, we will implement the necessary economic and regulatory policies to prevent abuse and arbitrage opportunities and ensure a fair and transparent allocation of foreign exchange.

H. Financial Sector

40. Our financial system remains sound, well capitalized, and liquid. The Honduran financial system has weathered the impact of recent economic shocks well thanks to support measures that were implemented, such as: (i) deferment and restructuring of loans; (ii) a reduction in contributions to the liquidity fund; (iii) extension of the period for classifying non-performing loans; and (iv) a reduction in provisioning requirements, which contributed to cushioning the impact of the crisis. Banks are well capitalized, liquid, and highly profitable, non-performing loans remain low (around 2-3 percent), and the latest stress tests conducted by the National Banking and Insurance Commission (CNBS) show that the banking system is resilient to significant shocks and impacts; there is, however, still a long way to go to achieve access to and democratization of credit, especially for micro, small, and medium-sized enterprises, the agricultural sector, and vulnerable groups. We will continue to monitor trends in the financial system, including bank liquidity and solvency scenarios and stress tests. We are ready to take any necessary measures, including the use of any of our macroprudential tools, to address any problem that may arise and ensure that the government and financial institutions maintain sufficient reserves.

41. We will continue to strengthen the regulatory framework and banking supervision practices. We are keeping up our efforts to enhance the capacity of the CNBS in risk-based supervision, applying the supervision methodology developed by the Toronto Centre, and we are continuing to strengthen our technical and institutional capacities to run stress tests. The CNBS has also developed a methodology for identifying systemically important financial institutions (SIFIs) and as a next step, we plan to formalize the criteria for SIFIs in a regulation. This will allow us to introduce a systemic buffer in line with the Basel III standards, which we will consider after the introduction of the capital conservation buffer that currently stands at 1.75 percent and will reach 2.5 percent as of January 2025. In the future, we also plan to: (i) continue with the gradual introduction of the liquidity coverage ratio and the capital conservation buffer requirements and develop a net stable funding ratio requirement to be implemented in a regulation by the end of 2025, in line with international practices; (ii) develop and oversee the gradual implementation of a market risk regulation; and (iii) develop new methodologies to assess operational risks. Finally, the CNBS is developing, with technical assistance from the Fund, a model for quantifying expected credit losses to improve its risk-based banking supervision. The CNBS will ensure that the necessary resources and personnel are available to carry out its functions effectively.

42. We are committed to financial inclusion as a vehicle to contribute to economic growth. We plan to adopt measures that promote financial inclusion while preserving the stability of the financial system and ensuring consumer protection. We have completely relaxed the documentation requirements for lending, which in the past had hindered access to credit, especially for many small entrepreneurs and farmers. To encourage financial inclusion and facilitate access to resources for micro-, small, and medium-sized enterprises, agricultural and industrial production sectors, as well as social housing and the middle class, we will also continue to strengthen the loan facilities funded by Banadesa, Banhprovi, and rural savings banks. After providing some 1 billion lempiras in new loan funds to Banadesa in 2022, this year we have budgeted 2.4 billion lempiras. Considering the marked increase in poverty (74 percent), we believe that our policies should also promote access to credit in order to achieve significant economic growth, especially in the country's productive sector. The government is prepared to assist the financial sector in the placement of credit resources to develop agriculture, livestock, agroforestry and agroindustry, and micro-, small, and medium-sized enterprises by developing a collateral policy that minimizes credit risk, with the understanding that this policy will be more efficient than the payment of quasi-fiscal losses, which are ultimately incurred through the absorption of liquidity by the Central Bank of Honduras.

43. We are working on a new law for the insurance and reinsurance sectors. The law, which is already being shared with the sector, will create a regulatory framework in line with international standards that will contribute to development of the market and financial inclusion, incorporating risk-based capital requirements. We plan to continue the discussion of this law with the Ministry of Finance prior to its submission to Congress, which is envisaged for late 2023.

44. We will protect the confidentiality of banking information, appropriately limiting access by the tax authorities. Once passed, the Law on Tax Justice will provide for access to bank records by tax authorities, which is appropriate. We do, however, recognize the importance of maintaining access limited to that required for tax purposes and will protect the confidentiality of data once the law enters into force.

45. Improve preparedness for crisis situations. We are continuing to advance measures to strengthen the system of financial early warning indicators of the CNBS. The Financial Stability Council (CEF) – composed of the Central Bank, the Ministry of Finance, the CNBS, and the Deposit Guarantee Fund – allows for the coordination and exchange of information among public sector entities involved in the prevention and monitoring of systemic risks in the financial system. We have already developed contingency plans with each bank. The regulation on bank recovery plans has already been issued and banks have been submitting their plans to the CNBS. The Financial Stability Council, which is chaired by the CNBS, meets every three months to update the country's monitoring of the liquidity and macroeconomic situations in order to prevent the financial sector risks.

I. Governance, Rule of Law, and Business Climate

46. Improving the environment for investment and job creation is key to fostering inclusive growth. In this context, we are continuing to work on the simplification of administrative procedures. We evaluated 839 procedures at 64 institutions and prioritized 16 for digitization. We plan to prepare and submit to the National Congress a Law on Simplification of Administrative Procedures by ***June 2024 (structural benchmark).*** In addition, our Directorate of Results-Based Management (DIGER) is working on an update of the Digital Signature Law, a law to regulate telework Regulation, a Cybersecurity Law, a Data Protection Law, and an update of the Open Data Access Law. Finally, we will consider the creation of a single office for handling the various administrative procedures related to investment, including international trade.

47. Improving the public procurement and contracting process is important to speed up budget execution and obtain savings on purchases. The Ministry for Transparency and Combating Corruption and the Association of Municipalities of Honduras (AMHON) submitted to the National Congress a new public procurement law to streamline procedures, strengthen procurement and contracting processes, and include powers to detect fraud. The Ministry of Finance will issue its opinion once this law is presented to the plenary of Congress and referred to the expert committee. This law should be passed by the end of 2023. In addition, we are working on evaluating alternatives for the modernization of our procurement portal Honducompras, which will also be key.

48. With regard to combating public-private corruption, our administration has already made significant progress. Congress repealed the Secrecy Law, which had blocked access to public information. It also repealed the arrangement of the trust funds. In addition, we have created a Ministry for Transparency and Combating Corruption, which has prepared a proposal for a Honduran National Transparency and Anti-Corruption Strategy (ENTAH), which is awaiting discussion by the Council of Ministers. Furthermore, we are implementing results-based management for the entire government to ensure that the public administration is accountable to the people. As a culmination of these efforts, we are working to regain access to the Millennium Challenge Account, from which Honduras was removed in 2010 due to high levels of corruption. Reactivation will be possible with an improvement in the corruption control indicator, which we hope to achieve through our efforts. To allow for an evaluation of the performance of our ministries and government, DIGER has created the Public Results-Based Management and Transparency System, with transparent quarterly evaluations of institutional targets and semi-annual evaluations of sectoral targets, and it is working on a version of this system that could also be published to improve transparency and accountability.

49. The President's commitment to eliminating public-private corruption is reflected in the signing of the memorandum of understanding with the United Nations and the terms of reference for the arrival of experts for the establishment of the International Commission against Corruption and Impunity in Honduras (CICIH). The CICIH will be an international mechanism to support the Honduran government in combating high-impact public-private corruption, with independent investigations and criminal prosecution. We are currently working with the UN to implement the phases of the memorandum of understanding signed in December 2022. In July 2023, a group of United Nations experts arrived in Honduras for the implementation of the first phase of the agreement.

50. We have been taking measures to reduce the risk of corruption within the government. In the Council of Ministers, we approved an executive decree on Financial Transparency and Combating Illicit Enrichment in order to facilitate the investigation of assets of government officials through the National Banking and Insurance Commission. The pursuit of investigations will be confidential and for use by the country's judicial and supervisory bodies. In addition, the Superior Court of Auditors has been working on an electronic asset declaration system for public officials with high salaries or decision-making power over significant amounts of public funds. A pilot system is already operational for officials of the Superior Court of Auditors. We will implement the electronic system nationwide for the 2024 sworn asset declaration to be processed from January to April 2024 ***(structural benchmark, February 2024).*** This 2024 cycle will be one of transition and we will provide substantial training for civil servants to ease their adjustment to the electronic system. This should facilitate the complete elimination of paper forms starting with the 2025 cycle.

51. We are moving forward on several fronts to strengthen our anti-money laundering and combating the financing of terrorism (AML/CFT) framework. We recognize that it is important to significantly strengthen our legal anti-money laundering framework. The National Congress approved in July this year the repeal of Decree 57-2020 and modification of Decree 93-2021, approved under the previous regime, which greatly weakened the framework. In elaborating these changes, the National Congress worked, together with the CNBS and the United Nations Office on Drugs and Crime (UNODC), to ensure that this new AML framework is in better alignment with our international obligations, including by incorporating revised definitions of money laundering and politically exposed persons (PEPs). Furthermore, the penalties for corruption and money laundering offenses were revised, which had been reduced by Decree 93-2021. Technical standards for the prevention of money laundering risks are already in operation for the banking sector through the CNBS. To ensure that this is also the case for cooperatives, the National Supervisory Council for Cooperatives (CONSUCOOP) is working with the UNODC to develop analogous technical standards for this sector. They are expected to be approved this year by the director of CONSUCOOP. Finally, we will advance other legal initiatives to further strengthen the AML framework. These include drafts of a Counter-Terrorist Financing Law and updates to the Special Law against Money Laundering and the Law on the Regulation of Designated Non-Financial Businesses and Professions to bring them fully into line with the standards of the Financial Action Task Force of Latin America (GAFILAT). We will submit these laws to the National Congress before the end of 2023.

52. We will create a business registry with information on firms' beneficial owners. We have already submitted to Congress, together with the Law on Tax Justice, a Law on Beneficial Ownership to ensure timely access to accurate information on beneficial ownership of all types of legal entities in Honduras, including requiring legal entities to submit updates, providing for the centralization of information on beneficial ownership, and establishing actions to ensure compliance. We expect Congress to pass the Law on Beneficial Ownership by ***December 2023 (structural benchmark).*** In addition, we will soon submit a Law on the Superintendence of Commercial Companies. These laws will create the legal basis for establishing a single national registry of commercial companies, including information on their beneficial owners. This registry will be administered by the Tax Administration and we will put it into operation soon after the approval of the legal framework. We will launch the new registry with information on commercial companies and their beneficial owners by the end of ***December 2024 (structural benchmark).*** Much of the required information is already available in scattered databases, but we will also obtain additional information directly from the commercial companies.

J. Statistics

53. **We are improving government finance and public debt statistics by harmonizing definitions with the 2014 *Government Finance Statistics Manual*.** We will continue to publish periodic fiscal risk reports, including updated data on any contingent debt. With technical assistance from the Fund, we are working to incorporate International Public Sector Accounting Standards (IPSAS) in the compilation of fiscal data, and to enhance SEFIN's capacity to develop macroeconomic and fiscal projections and conduct debt sustainability analysis. Finally, we will work on aligning ENEE's accounting with international standards so that ENEE regularly publishes duly audited financial statements.

54. **We are working to improve price and economic activity statistics, which are essential for assessing the monetary stance and forecasting inflation.** In April 2023, the BCH, working together with the National Institute of Statistics (INE), launched the National Household Income and Expenditure Survey (ENIGH), which was postponed due to the pandemic. The survey will be conducted over the course of 12 months among 9,000 households in urban and rural areas nationwide. The results are expected to be available by the end of 2024 and will be used to update our national accounts. The ENIGH will lay the groundwork for the compilation of new national accounts series and consumer and producer price indices.

K. Climate Change

55. **Our country is highly exposed and vulnerable to extreme weather events, with negative socio-economic and health consequences, which aggravate social outcomes.** With respect to climate disasters, Honduras continues to be one of the most vulnerable countries in the world, which poses the risk of aggravating an already challenging situation. The Global Climate Risk Index ranked Honduras as one of the countries most affected in the world by extreme weather events during the period 2000-2019. Extreme weather events in Honduras have caused average annual losses equivalent to 6.3 percent of GDP during 1960 to 2022, mainly due to floods, tropical storms/hurricanes, and droughts, all of which are likely to increase in frequency and severity due to climate change. The impact of the current drought, with considerable adverse consequences for the agricultural and energy sectors, demonstrates our extreme vulnerability.

56. **Our country's climate change mitigation and adaptation agenda is guided by the Nationally Determined Contribution of Honduras (NDC-HN), which includes saving Lake Yojoa and the reforestation program.** The NDC-HN, approved in 2019 and ratified in 2021, details the strategic guidelines for the adoption of measures aimed at developing policies and actions for the country's contribution to global climate action. It also defines the basis for a long-term low-carbon development strategy and compliance with the 2030 agenda, which includes, among other things, the recovery of Lake Yojoa and the restoration program for degraded and deforested landscapes, water protection, and forest conservation covering 24,000 hectares. With awareness of the importance of this issue for the growth and development of our country, operates the *Climate Change Committee*, which is made up of government ministers and members representing academia, civil society, and the private sector. Our country also has a Law

on Climate Change that is in the process of being reviewed by the Ministry of Natural Resources and Environment. In order to better account for the resources allocated for combating the adverse effects of climate change, we have taken steps to identify the budgetary resources earmarked for this purpose.

57. We plan to develop a Climate Change Financing Strategy. The strategy will be consistent with our Nationally Determined Contribution under the Paris Agreement. In addition, we are considering seeking climate change financing from the IMF through the Sustainability and Resilience Fund, given the country's high vulnerability. We will also continue to explore issuance of green bonds and a debt-for-nature swap.

L. Safeguards Assessment and Program Monitoring

58. Fund staff will update the BCH's safeguards assessments. The updating will be completed prior to the first program reviews. We will evaluate the recommendations of this assessment with a view to incorporating them into our program, in consultation with the IMF.

59. Program supervision. The program is subject to semi-annual reviews and will be monitored through quantitative performance criteria, indicative targets, and structural benchmarks, as set out in Tables AI.1 and AI.2. To facilitate the monitoring of the program, we commit to providing detailed information as specified in the Technical Memorandum of Understanding (TMU). The relevant definitions and reporting procedures are further specified in the attached TMU.

Table AI.1. Honduras: Prior Actions and Structural Benchmarks 2023-2025					
	Measure	**Test Date**	**Objective**	**Status**	**MEFP ¶**
Prior Action	Increase interest rate on BCH's overnight lending facility (Facilidad Permanente de Crédito, FPC) by 50 basis points	Prior Action	Strengthening monetary policy transmission	Met on August 24, 2023	33
1.	Prepare and approve in the Public Credit Committee (Comisión de Crédito Público) an annual Public Borrowing Policy (Política de Endeudamiento Público, PEP) and publish it on the website of the Ministry of Finance.	End-September 2023	Deepen domestic debt markets; improve government financing and debt service profile		24
2.	Prepare a Medium-Term Debt Strategy and publish it on the Ministry of Finance website.	End-December 2023	Deepen domestic debt markets; improve government financing and debt service profile		24
3.	Approve the Law on Tax Justice (Ley de Justicia Tributaria) in the National Congress.	End-December 2023	Make the tax system more equitable and reduce tax expenditures		10
4.	Approve the decree to ratify the Convention on Mutual Administrative Assistance in Fiscal Matters (MAAC) in the National Congress.	End-December 2023	Improve tax administration		10
5.	Approve a law that ensures timely access to beneficial ownership information for all types of legal persons in Honduras—including requiring legal entities to submit updates, ensuring the centralization of beneficial ownership information, and establishing measures to ensure compliance.	End-December 2023	Improve transparency and governance, and reduce corruption vulnerabilities		52
6.	Publish an issuance schedule for treasury bonds on the Ministry of Finance's website.	End-January 2024	Deepen domestic debt markets		24
7.	Make the electronic asset declaration system for public officials operational nationwide.	End-February 2024	Improve transparency and governance, and reduce corruption vulnerabilities		50
8.	Prepare a Special Law to Strengthen the Single Treasury Account and submit it to the National Congress for approval.	End-March 2024	Improve governance and transparency in public spending		21
9.	Create the Single Social Sector Information System (SUISS) and populate it with the data (according to ¶18 of the MEFP).	End-June 2024	Combat poverty and inequality		18
10.	In consultation with IMF staff, prepare a draft law on Simplification of Administrative Procedures and submit it to the National Congress for approval.	End-June 2024	Improve efficiency in the public		46

Table AI.1. Honduras: Prior Actions and Structural Benchmarks 2023-2025 (Concluded)					
			administration and the business climate		
11.	Complete the census of urban households in extreme poverty and register the resulting data in the Honduran Beneficiary Information and Registration System (SIRBHO).	End-September 2024	Combat poverty and inequality		15
12.	To implement the Law on Beneficial Ownership, make operational a comprehensive beneficial ownership registry	End-December 2024	Improve transparency and governance, and reduce corruption vulnerabilities		52
13.	Conclude liquidation and audit of all trust funds, and their complete integration into the budget processes and the central government balance sheet, including INVEST-H, Tasa de Seguridad and Instituto de la Propiedad (IP-SITEC), and share the associated audit documents with IMF staff. Quantify and register their debts (including accounts payable) as part of the public debt stock.	End-December 2024	Improve governance and transparency in public spending		20
14.	Operationalize the Special Law to Strengthen the Single Treasury Account.	End-December 2025	Improve governance and transparency in public spending		21

Table AI.2. Honduras: Performance Criteria

(Cumulative flows; millions of Lempiras, unless specified)

	2023	2024		
	End-Dec.	End-Mar.	End-Jun.	End-Sep.
	PCs	ITs	PCs	ITs
QUANTITATIVE PERFORMANCE CRITERIA 1/				
Fiscal and public debt targets				
Net lending/borrowing of the nonfinancial public sector (-= borrowing, floor) 2/	-16,970	-1,897	-3,843	-6,170
Stock of domestic arrears of ENEE (ceiling)	10,500	10,500	9,451	9,148
Accumulation of new external arrears (ceiling, in million US$) 3/	0	0	0	0
Monetary targets				
Stock of non-borrowed net international reserves of the Central Bank (floor, in million US$)	5,465	5,477	5,500	5,371
Stock of net domestic assets of the central bank (ceiling)	-62,794	-62,593	-61,685	-61,459
Monetary financing (ceiling) 3/	0	0	0	0
INDICATIVE TARGETS 1/				
Tax revenue of the central government (floor) 2/	145,070	30,500	77,000	116,500
Current primary spending of the SNPF excluding priority social spending (ceiling) 2/	203,395	44,685	97,877	143,672
Priority social spending (floor) 2/	7,000	856	2,472	4,851
Percentage of energy lost by ENEE in energy distribution (ceiling)	34.5	33.8	33.1	32.4

1/ Definitions as specified in the Technical Memorandum of Understanding (TMU).
2/ Cumulative from the start of the calendar year.
3/ Continuous PC.

Attachment II. Technical Memorandum of Understanding

1. **This memorandum sets out technical understandings between the Honduran authorities and the Fund staff for monitoring of the economic program agreed for the period September 2023-September 2026.** It defines the concepts used to assess observance of quantitative performance criteria, structural benchmarks, and indicative targets specified in Tables AI.1 and AI.2 of the Memorandum of Economic and Financial Policies (MEFP). It also specifies the frequency of the data to be provided to the Fund to monitor the developments under the program.

2. **For program monitoring purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined below, except for items related to fiscal operations which will be measured at current exchange rates.** The program rates are those that prevailed on May 25, 2023. Accordingly, the exchange rates for the purposes of the program are shown in Table AII.1. If any needed exchange rates are not listed in this table, the exchange rate for May 25, 2023 from the IMF website will be used (https://www.imf.org/external/np/fin/data/param_rms_mth.aspx).

Table AII.1. Honduras: Program Exchange Rates

Lempira to the U.S dollar	24.56
SDR to the U.S dollar	0.75
Yen to the U.S dollar	139
Euro to the U.S dollar	0.93
Canadian dollar to the U.S dollar	1.36
British Pound to the U.S dollar	0.81
Renminbi to the U.S dollar	7.07

3. **Standard performance criteria.** In addition to the performance criteria listed in Tables AI.2 the arrangements will include the performance criteria standard to all Fund arrangements, namely:

i. no imposition or intensification of restrictions on the making of payments and transfers for current international transactions;

ii. no introduction or modification of multiple currency practices;

iii. no conclusion of bilateral payments agreements that are inconsistent with Article VIII of the IMF Articles of Agreement;

iv. no imposition or intensification of import restrictions for balance of payments reasons.

These four performance criteria will be monitored continuously.

4. **Any variable that is mentioned herein for the purposes of monitoring a PC or IT and that is not explicitly defined, is defined in accordance with the Fund's latest statistical manuals.**

A. Quantitative Performance Criteria: Definition of Variables

5. Definitions:

- **a.** The central government for the purposes of the program consists of the budgetary central government (*Administración Central*) and decentralized agencies (*instituciones desconcentradas*).
- **b.** The nonfinancial public sector (NFPS) for the purposes of the program consists of the central government as defined above, the social security institute (IHSS), all state-owned public pension funds, local governments, other decentralized agencies, and nonfinancial public enterprises.
- **c.** The Honduran public sector for the purposes of the program is considered to be made up of the NFPS and all other entities that are either (i) controlled by the central government or other NFPS entities or (ii) that have a majority participation in their own capital by the central government or other NFPS entities. In particular, this is the case for the public financial sector of Honduras, including the National Bank for Agricultural Development (*Banco Nacional de Desarrollo Agrícola; Banadesa*) and the Honduran Bank for Production and Housing (*Banco Hondureño para la Producción y la Vivienda; Banhprovi*).

Cumulative Floor of NFPS' Net Lending/Borrowing

6. Definitions: Net lending of the NFPS calculated from above-the-line and is defined as the difference between revenue and expenditure of the NFPS.

7. NFPS' revenues are recorded on a modified cash basis: taxes, grants and other revenues are recorded on a cash basis; and the income of non-financial public companies and social contributions will be recorded on an accrual basis. Payments from private users of public-private partnerships (PPPs) facilities will be considered public revenue.

8. NFPS' expenditure is recorded on an accrual basis and includes expenses and the net acquisition of nonfinancial assets. Private investments for PPPs are treated as expenses and measured as part of NFPS net lending as they occur.

9. NFPS' net lending will be measured at each test date as the cumulative value starting from the beginning of each calendar year.

10. Monitoring. All fiscal data referred to above and needed for program monitoring purposes will be provided to the Fund with a lag of no more than 45 calendar days after the end of each month.

Adjustors

11. Adjustor for external financing disbursements for productive investment projects. The cumulative floor of NFPS' net lending/borrowing will be adjusted downward by the excess in external program and project disbursements from official multilateral and bilateral institutions, relative to the baseline projection reported in Table AII.2. The value of the adjustor would be capped at a cumulative 12 billion Lempiras in 2024. Project disbursements are defined as external loan and grant disbursements from official multilateral and bilateral creditors that will be used to finance specific productive investment projects.

Table AII.2. Honduras: External Program and Project Disbursements

Cumulative flows per year (Millions of US$)

	End-Dec 2023	End-March 2024	End-June 2024	End-Sep 2024	End-Dec 2024
Loans	752.6	250.7	499.9	875.8	1,215.1
Grants	50.7	8.8	22.8	34.5	50.5

Ceiling on ENEE's Stock of Domestic Arrears

12. Definition: ENEE's domestic arrears are defined as overdue payments of ENEE to all entities that are not part of the Honduran public sector. Technical delays stemming from the payment process will not be considered arrears. Technical delays are defined as unpaid claims still under the maximum period allowed for payment stated in the law on state contracts (Decree 74-2001). This decree states a deadline up to 45 days starting from the submission of appropriate documents for payment. This definition does not preclude payment before the deadline if it is agreed by both parties.

13. Monitoring. The data on ENEE's stock of domestic arrears will be provided to the Fund with a lag of no more than 45 calendar days after the end of each month.

Ceiling on the Non-Accumulation of External Debt Payment Arrears

14. Definition of debt: External debt is determined according to the residency criterion. The term "debt"[1] will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of financial and nonfinancial assets (including currency) or services, and which requires the obligor to make one or more

[1] As defined in paragraph 8(a) in Guidelines on Public Debt Conditionality in Fund Arrangements attached to IMF Executive Board Decision No. 16919-(20/103), adopted October 28, 2020.

payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take several forms; the primary ones being defined as follows:

a. Loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

b. Suppliers' credits, i.e., contracts where the supplier allows the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided, and

c. Leases, i.e., arrangements under which the lessee has the right to use the provided property for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the program, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

15. Definition of external arrears: External debt payments arrears for program monitoring purposes are defined as external debt obligations (principal and interest) falling due after June 30, 2023, that have not been paid, considering the grace periods specified in contractual agreements. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

16. Coverage: This performance criterion covers the NFPS. This performance criterion does not cover (i) arrears on trade credits, (ii) arrears on debt subject to renegotiation and restructuring and (iii) arrears resulting from the nonpayment of commercial claims that are the subject of litigation initiated prior to November 30, 2022. For the purposes of this performance criterion, nonpayment of external debt service to Venezuela will not give rise to arrears when the government cannot pay or settle based on the contractual terms solely due to factors outside the debtor's control such as the existence of sanctions on Venezuela, as long as the debt service payments have been paid in full into an escrow account held at the Central Bank of Honduras by the contractual due date, taking into account any contractual grace period. Funds in such escrow accounts will be used only to satisfy the related external debt obligations, and their use or withdrawal for other purposes would constitute a breach of the PC.

17. Monitoring: This performance criterion will be monitored on a continuous basis.

Floor on the Stock of Non-Borrowed Net International Reserves

18. Definitions: Non-Borrowed Net International Reserves (NIR) of the BCH are equal to the balance of payments concept of NIR defined as the U.S. dollar value of gross international reserves of the BCH minus gross official liabilities as defined below. Non-U.S. dollar denominated foreign assets and liabilities will be converted into U.S. dollar at the program exchange rates.

19. Gross official reserves are defined consistently with the Sixth Edition of the Balance of Payments and International Investment Position Manual (BPM6) as readily available claims on nonresidents denominated in foreign convertible currencies. They include the (i) monetary claims, (ii) free gold, (iii) holdings of SDRs, (iv) the reserve position in the IMF, and (v) holdings of fixed income instruments. Excluded from reserve assets are any assets that are pledged, collateralized or otherwise encumbered, claims on residents, claims in foreign exchange arising from derivatives in foreign currency *vis-à-vis* domestic currency (such as futures, forwards, swaps and options), precious metals other than gold, assets in nonconvertible currencies and illiquid assets.

20. Gross official liabilities in foreign currencies include (i) all borrowed reserves, including foreign currency swaps, loans, and repo operations with all counterparties (domestic and foreign), regardless of maturity, (ii) other foreign currency liabilities including deposits of financial institutions, (ii) all liabilities outstanding to the IMF, (iii) any deliverable forward foreign exchange (FX) liabilities on a net basis—defined as the long position minus the short position payable in foreign currencies. The stock of non-borrowed net international reserves will be measured as each test date. SDR allocations are not netted out from gross international reserves for the calculation of net international reserves.

21. Monitoring: Foreign exchange asset and liability data will be provided to the Fund at a daily frequency, with a lag of no more than 3 business days.

Adjustors

22. The NIR target will be adjusted upward (downward) by the surplus (shortfall) in disbursements (loans and grants) for programs and projects from official multilateral and bilateral institutions, relative to the baseline projection reported in Table AII.2. In case Honduras participates in a new SDR allocation, the floor on NIR will be adjusted upward by the amount of the additional SDR allocation up to the test date.

Ceiling on the Stock of the BCH's Net Domestic Assets

23. Definitions. Net Domestic Assets (NDA) of the BCH are defined as the difference between currency issued and non-borrowed NIR measured at program exchange rates.

24. The ceiling applies to the stock of NDA measured at each test date.

25. Monitoring: Data will be provided to the Fund monthly with a lag of no more than 2 weeks after the end of each month.

26. Adjustor for multilateral loans. Consistent with the NIR adjustor, the NDA target will be adjusted downward (upward) by the surplus (shortfall) in disbursements (loans and grants) for programs and projects from official multilateral and bilateral institutions, relative to the baseline projection reported in Table AII.2. In case Honduras participates in a new SDR allocation, the ceiling on NDA will be adjusted downward by the amount of the additional SDR allocation up to the test date.

Ceiling on Monetary Financing of the Central Bank to the Non-Financial Public Sector (NFPS)

27. Definition: Monetary financing is defined as any disbursement from the BCH to the NFPS after January 1, 2023, under any loan between these entities, whether the loan is repayable or not or interest-bearing or not. The only exception is the on-lending loan between BCH and SEFIN under which the BCH will on-lend IMF disbursements received as part of this program to SEFIN.

28. Measurement and monitoring: This program establishes a ceiling of zero on net monetary financing in accordance with Attachment I (Memorandum of Economic and Financial Policies), section E, paragraph 23; this PC will be monitored on a continuous basis. For the purposes described above, the BCH balance sheet, with detail on the net credit balance to the NFPS, will be provided to the Fund on a daily basis with a lag of no more than one business day.

B. Quantitative Indicative Targets: Definition of Variables

Floor on the Central Government's Tax Revenues

29. Definition: Tax revenue will be measured on a cash basis at the level of the central government. All compulsory and unrequited receivables by the government will be considered taxes as stated in the Governance Finance Statistics Manual (GFSM) 2014.

30. For compliance with this indicative target the central government will be considered equivalent to the budgetary central government (*Administración Central*).

31. The central government's tax revenues will be measured at each test date as the cumulative value starting from the beginning of each calendar year.

32. Monitoring. Monthly data will be provided to the Fund no more than 2 weeks after the end of the month.

Ceiling on current primary spending of the NFPS excluding priority social spending

33. Primary current spending excluding priority social spending is defined as total current spending minus interest spending minus priority social spending, as defined below.

34. Current expenditure is defined as the total expenditures of the SNPF minus the capital expenditures (i.e., the net acquisition of non-financial assets) of the SNPF. As defined above, all expenditures are recorded on an accrual basis.

35. Primary current spending of the NPFS excluding priority social spending will be measured at each test date as the cumulative value starting from the beginning of each calendar year.

36. Monitoring. Monthly data will be provided to the Fund within 45 days of the end of each month.

Floor on Priority Social Spending

37. Priority social spending is defined for program purposes as the interventions by the central government with high impact on poverty reduction and long-term influence on beneficiaries that are listed in Table AII.3.

38. Priority social spending will be measured at each test date as the cumulative value starting from the beginning of each calendar year.

39. Monitoring. Monthly data will be provided to the Fund within 45 days of the end of each month.

Table AII.3. Honduras: Priority Social Spending
• Red Solidaria
• Becas SEDESOL
• Ciudad Mujer
• Merienda Escolar
• Bono Tecnológico
• Bono Cafetalero
• Bono Ganadero
• Becas PROASOL
• Bonos PROASOL

Ceiling on Percentage of Energy Lost by ENEE in Energy Distribution

40. Definition: The percentage of energy lost by ENEE in energy distribution is defined as the energy injected into the distribution network minus the sales invoices issued to its customers (both in GWh) during the 12 months prior to the test date, divided by the energy injected into the distribution network during the same period.

41. Monitoring. Monthly data will be provided to the Fund within 45 days of the end of each month.

INTERNATIONAL MONETARY FUND

HONDURAS

September 5, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION AND REQUESTS FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

Approved By
Patricia Alonso-Gamo and Natalia Tamirisa (IMF) and Oscar Calvo-Gonzalez and Manuela Francisco (IDA)

Prepared by staff of the International Monetary Fund and the International Development Association.

Honduras: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	Low
Overall risk of debt distress	Moderate
Granularity in the risk rating	Tool not applicable
Application of judgment	No

Honduras' risk of external debt distress is low, while the risk of overall public debt distress is moderate.[1,2] *Honduras maintains a strong debt-carrying capacity and while none of the external debt burden indicators breach their respective thresholds, the PV of public debt-to-GDP ratio breaches its threshold under the most severe stress test scenario. Going forward, the authorities should remain committed to prudent policies, including by continuing to strike a sound balance between addressing Honduras' social and investment needs and preserving fiscal and debt sustainability. Sustained efforts to develop the domestic debt market, improve debt management practices, enhance monetary and foreign exchange policy frameworks, and strengthen the energy sector are important safeguards to debt sustainability. The debt sustainability outlook remains vulnerable to policy slippages and risks of exogenous shocks, such as adverse weather events and a deterioration of the global outlook.*

[1] This DSA updates the previous joint IMF/WB DSA prepared in August 2021 in the context of Fourth Review under the Stand-By Arrangement and Arrangement under the Standby Credit Facility (IMF Country Report No. 21/207).

[2] Honduras's debt carrying capacity is assessed to be strong based on a composite indicator of 3.13 that uses the April 2023 WEO vintage and the 2021 World Bank CPIA.

PUBLIC DEBT COVERAGE

1. **The debt coverage of the public sector is comprehensive (Text Table 2).** The debt sustainability analysis (DSA) covers the non-financial public sector (NFPS), which includes the general government and non-financial state-owned enterprises (SOEs). Debt from extrabudgetary trust funds is also included, with the authorities having abolished through legislation all trust funds in 2022.[3] Debt from decentralized agencies such as public universities, public pension funds, and central bank borrowing on behalf of the government is also covered. In addition, the baseline 2022 debt stock includes 2.6 percent of GDP in domestic debt that was previously unaccounted for (Text Table 1), of which (i) 0.3 percent of GDP relates to central government arrears to domestic suppliers; (ii) 1.1 percent of GDP consists of trust funds' debt liabilities,[4] and (iii) 1.2 percent of GDP pertains to arrears to private electricity generators accumulated by the state electricity utility *Empresa Nacional de Energía Eléctrica* (ENEE) owing to continued liquidity shortages given ongoing losses and impacts by the pandemic and the 2020 tropical storms.[5] External debt is defined on a currency basis.[6]

Text Table 1. Honduras: Domestic Debt Regularization

	Lempiras (million)	% GDP
Domestic Debt	**20,500**	**2.6**
Central government	2,165	0.3
Trust funds	8,547	1.1
ENEE	9,788	1.2

Source: Country authorities; and IMF staff calculations.

2. **The contingent liability tailored stress test is calibrated to account for public sector debt coverage gaps and risks from contingent liabilities (Text Table 2).** First, the default shock of 0 percent of GDP for other entities of the general government is kept unchanged as these are already captured in the coverage of public debt. Second, the default shock of 2 percent of GDP for SOE debt and government-guaranteed private debt is maintained to reflect risks from lawsuits linked to a highway concession project (0.4 percent of GDP) and the electricity utility (1.5 percent of

[3] While trust funds were treated as private entities under Honduran legislation, they should be registered as general government units according to the 2014 GFSM.

[4] The authorities have already recognized and fully repaid the "Tasa de Seguridad" trust fund's debt liabilities of 0.2 percent of GDP by contracting bank loans in January 2023.

[5] Total electricity demand in Honduras increased owing to the COVID-19 lockdown measures in 2020. As part of mitigation measures, the government prohibited ENEE to suspend household electricity services during the crisis and allowed deferred payments. This action contributed to increasing ENEE's accounts receivable and jeopardized the company's ability to pay to private power generators. Additionally, tropical storms Eta and Iota caused extensive damage to the country's power electric infrastructure, including transmission lines, and distribution networks. As a result, ENEE incurred significant expenses to repair and replace the damaged infrastructure, which added to its already considerable debt burden. In addition to the direct costs of repairing the damage caused by the storms, ENEE also experienced significant revenue losses due to the disruption of power supplies. The estimated cost of Eta and Iota is estimated at 246 million lempiras (0.1 percent of GDP) of which 109 million lempiras correspond to damages to infrastructure and 146 million lempiras to losses.

[6] There is no material difference between the residency- and currency-based definitions of external debt as non-residents do not hold domestic debt.

GDP) and to capture the publicly-guaranteed external debt of a financial SOE (0.1 percent of GDP).[7] Third, the default shock to account for risks stemming from public private partnerships (PPPs) is revised to 5.7 percent of GDP to reflect potential liabilities from PPP projects.[8] Fourth, the default minimum value of 5 percent of GDP for the financial market shock is kept unchanged since Honduras' financial sector does not exhibit significant vulnerabilities warranting an upward adjustment.

Text Table 2. Honduras: Public Debt Coverage and Calibration of Contingent Liability Stress Test

	Subsectors of the public sector	Sub-sectors covered
1	Central government	X
2	State and local government	X
3	Other elements in the general government	X
4	o/w: Social security fund	X
5	o/w: Extra budgetary funds (EBFs)	X
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	X

1	The country's coverage of public debt	The entire public sector, including SOEs			
		Default		Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0	percent of GDP	0.0	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	2.0	
4	PPP	35	percent of PPP stock	5.7	
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5	percent of GDP	5.0	
	Total (2+3+4+5) (in percent of GDP)			12.7	

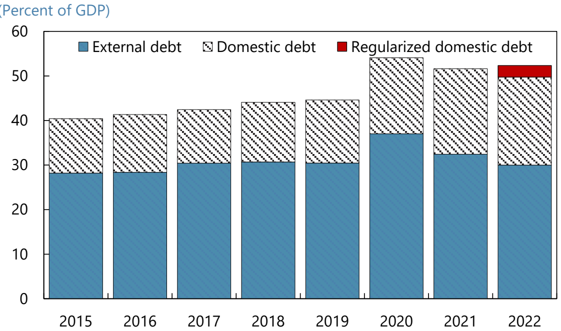
1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

BACKGROUND ON DEBT

3. **Public and publicly guaranteed (PPG) debt stood at 52.3 percent of GDP in 2022, with external debt accounting for 30 percent of GDP (Table 2).** The strong recovery in 2021 led to a moderation in gross public debt, which reached 51.6 percent of GDP in 2021, down by 2.5 percentage points of GDP from 2020. Following growth of 12.5 percent in 2021, real GDP expanded by 4 percent in 2022 on the back of strong domestic demand buoyed by robust remittances flow and a resilient export sector. The

Text Figure 1. Honduras: Public and Publicly Guaranteed Debt

(Percent of GDP)



Sources: Country authorities; and IMF staff calculations.

[7] Please refer to the World Bank Honduras Public Expenditure Review (2022) for a discussion of key fiscal risks and way to strengthen fiscal resilience.

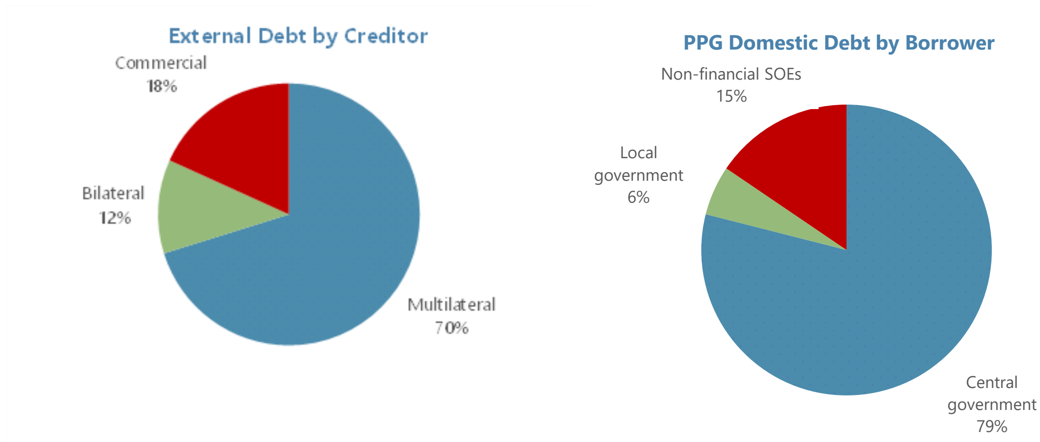
[8] Consistent with the LIC DSF guidance note, the PPP stock is calculated as 35 percent of the country's PPP capital stock from the World Bank database, further updated to account for a PPP project worth 1.6 percent of GDP.

slight uptick in the 2022 debt stock to 52.3 percent of GDP is explained by the recognition of 2.6 percent in domestic debt that was previously unaccounted for.[9]

4. Total external debt moderated from 40.7 percent of GDP in 2021 to 37.1 percent of GDP in 2022 (Table 1). PPG external debt-to-GDP ratio declined to 30.0 percent of GDP in 2022, from 32.5 percent of GDP in 2021, amid higher GDP growth and inflation. 70.4 percent of PPG external debt is owed to multilateral creditors, 11.6 percent to official bilateral creditors, while the remainder is owed to commercial banks or Eurobond holders (Text Figure 2). In nominal terms, total multilateral debt increased by about US$432 million or 6.4 percent y/y in 2022, driven by the public sector. Private external debt declined by US$66.7 million or 2.9 percent y/y in 2022, owing to a moderation in the stock of debt owed to multilateral and commercial creditors.

5. Public debt is mostly held by foreign creditors (Text Figure 2). The main creditors to Honduras are international bondholders and official multilateral creditors, such as the Inter-American Development Bank (IDB), the Central American Bank for Economic Integration (CABEI), and the World Bank. The multilateral institutions provide lending at relatively long maturities. Public domestic debt, which is mainly held by domestic commercial banks, has a shorter—though rising—maturity (over 4 years) and carries a higher real interest rate. Domestic issuances were replaced by borrowing from the Central Bank in 2022. This change in the Debt Management Strategy negatively impacted domestic debt market development and reduced investment opportunities, including for pension funds.

Text Figure 2. Honduras: PPG Debt Stock Composition (Percent, 2022)



Source: Country authorities and staff elaboration.
Note: NFPS domestic debt excluding IMF debt and including regularized domestic debt.

[9] Without the recognition of new domestic debt, the 2022 PPG debt stock would have been 49.7 percent of GDP, i.e., lower than in 2021.

MACROECONOMIC AND POLICY ASSUMPTIONS

6. **The main macroeconomic assumptions are based on staff projections and EFF/ECF program targets.** Text Table 3 summarizes baseline macroeconomic projections compared to the last published DSA, from August 2021, with the revised baseline reflecting a more benign (than expected) global environment.

- **Real sector.** Real GDP growth is projected to decelerate to 2.9 percent in 2023—in line with lower U.S. and remittances growth— and to gradually converge toward potential (just under 4 percent) supported by strong public investment and the implementation of reforms, as part of the EFF/ECF program and support from other international financial institutions.[10] This is slightly higher than recent historical trend growth,[11] as the Honduran economy is projected to benefit from the program's reform agenda and investment in critical infrastructure, in particular for climate adaptation that will have long-term benefits on growth and poverty.

- **Inflation.** Inflation is projected to continue to fall and return to the BCH reference range (3-5 percent) in 2024, driven mainly by a normalization of global commodity prices and the strengthening of monetary and FX policies. The authorities are committed to further enhancing monetary policy transmission through improvement in liquidity management and strengthening the crawling band exchange rate regime to function properly as a nominal anchor while supporting external competitiveness.

- **Fiscal sector.** The non-financial public sector (NFPS) deficit is expected to widen to 2.0 percent of GDP in 2023 as spending, including capital expenditure, begins to normalize following the restructuring of ministries and elimination of trust funds, which, temporarily aggravated capacity constraints in the public administration and lowered overall capital spending. Thereafter, a gradual fiscal consolidation is assumed to return the NFPS deficit to 1 percent of GDP by 2026, underpinned by the revenue efforts expected during the program, including a major reform of tax exemptions, to create space for investment and priority spending. The envisaged consolidation path would be further supported by an expenditure adjustment to return to pre-pandemic levels, including with the reprioritization of current spending towards social spending.

[10] The authorities are seeking to jumpstart capital investment projects and have identified a list of projects (hospitals, schools, dams, roads) and corresponding potential financing sources. The energy sector will also require large investments over the next few years, in generation, transmission, and distribution. The authorities' public investment agenda includes reforms to strengthen the planning, selection, and monitoring of infrastructure projects in addition to structural reforms strengthening institutions, transparency, combating public-private corruption, and governance, together with improving the management of public finances. An updated Public Investment Management Assessment is planned for late 2023 to help improve investment management including procurement processes.

[11] Real GDP growth averaged 3.9 percent over 2001-19 and 3.7 percent over 2010-2019.

Furthermore, the baseline assumes the gradual reduction of ENEE's stock of domestic arrears.[12] The primary balance is projected to turn positive in the medium term.

- **External sector.** The current account deficit is projected to widen to 5.2 percent in 2023, consistent with the expected deceleration in U.S. and remittance growth, and the adverse ramifications of the energy crisis linked to the regional drought. Reserve adequacy is expected to remain within the recommended 100-150 percent range of the ARA metric and close to 5 months of import cover over the medium term.

- **Financing assumptions.** The DSA assumes that financing needs would be covered by external sources and by domestic borrowing.

    - ***External.*** The baseline assumes net positive financing from international financial institutions (IFIs) over the medium term, with budget and project support provided both by official multilateral and bilateral sources. The baseline also assumes that Honduras would tap international capital markets—as implementation of the ECF/EFF program would further underpin confidence—with Eurobond placements of USD 700 million in 2026 and USD 600 million in 2030 to meet external bond redemptions coming due. The grant element of new external public sector borrowing is projected to average 18.5 percent over 2023-27.

    - ***Domestic.*** In 2022, the authorities resorted to US$1 billion (3.2 percent of GDP) in monetary financing,[13] largely to address liquidity strains. As such, for 2023, the DSA assumes some drawdowns of treasury deposits remaining from this contracting of a loan from the Central Bank and gradual resumption of the regular issuance of Treasury bonds at market rates. Amortizations are assumed to be rolled over as they come due. The baseline also assumes that the authorities will work on deepening the domestic debt market to mitigate liquidity risks in the wake of possible tightening of global financing conditions, and consistent with a sound debt management strategy. This includes issuing domestic debt instruments with increasing maturities and predominantly at fixed rates. The authorities have committed to preparing an annual borrowing plan and a Medium-term Debt Management Strategy (MTDS) at the time of the 2024 budget, underpinned by the recommendations of a joint IMF/World Bank Technical Assistance on debt management.

[12] ENEE has adopted a bond issuance strategy to repay arrears (around 2 percent of GDP at end-2022) to private generators. A first issuance of close to 1 percent of GDP took place in December 2022, with issuance proceeds used to reduce the stock of arrears by an equivalent amount. Further issuances are planned for the remainder of 2023 to finance ENEE's operational deficit and forestall new arrears accumulation.

[13] Contracting of a loan from the from Central Bank of Honduras by the central government in 2022 which was issued following the "exceptional circumstances" provision of the Central Bank law, given declaration of a national emergency in early 2022 due to liquidity shortages in the public administration.

Text Table 3. Honduras: Assumptions for Key Economic Indicators, 2021-43

	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043
Real GDP growth (percent)										
Current DSA	12.5	4.0	2.9	3.2	3.5	3.7	3.8	3.8	3.9	3.9
August 2021 DSA	4.9	4.4	3.5	3.6	3.7	3.9	…	…	…	…
Inflation, Period Average (percent)										
Current DSA	4.5	9.1	6.4	4.7	4.1	4.0	4.0	4.0	4.0	4.0
August 2021 DSA	4.6	3.7	4.0	4.0	4.0	4.0	…	…	…	…
GDP deflator growth (percent)										
Current DSA	3.8	9.1	6.4	4.7	4.1	4.0	4.0	4.0	4.0	4.0
August 2021 DSA	4.6	3.7	4.0	4.0	4.0	4.0	…	…	…	…
Primary balance (percent of GDP)										
Current DSA	-2.3	1.2	-0.7	-0.2	0.0	0.4	0.4	0.5	0.5	0.5
August 2021 DSA	-4.3	-1.3	0.5	0.7	0.3	0.5	…	…	…	…
Overall balance (percent of GDP)										
Current DSA	-3.7	-0.2	-2.0	-1.7	-1.4	-1.0	-0.9	-0.9	-0.6	-0.4
August 2021 DSA	-5.4	-2.3	-1.0	-1.0	-1.0	-1.0	…	…	…	…
Current account balance (percent of GDP)										
Current DSA	-4.6	-3.2	-5.2	-4.9	-4.7	-4.3	-4.1	-3.9	-4.0	-4.0
August 2021 DSA	-3.2	-3.4	-3.6	-3.8	-3.9	-4.0	…	…	…	…
Net FDI (percent of GDP)										
Current DSA	1.8	2.0	2.1	2.2	2.3	2.4	2.5	2.6	2.7	2.8
August 2021 DSA	2.0	2.4	2.7	3.1	3.5	3.8	…	…	…	…

Source: Country authorities and staff elaboration.

7. Tools for assessing the realism of the baseline scenario do not flag significant and systematic deviations from historical experience (Figures 3 and 4).

- **Drivers of debt dynamics**. The contributions of past and projected debt-creating flows for PPG external debt remain broadly unchanged, although the current account and FDI are expected to positively contribute to PPG external debt accumulation relative to historical experience. For total public debt, gradual fiscal adjustment under the EFF/ECF program should curb the contribution of the primary deficit to public debt accumulation more than in the past. A comparison with the distribution of past forecast errors for LICs shows that unexpected changes in debt for Honduras are within the interquartile range for both public and PPG external debt.

- **Realism of planned fiscal adjustment**. The projected three-year fiscal adjustment in the primary balance stands at 1.2 percentage points of GDP between 2023 and 2025 and falls comfortably below the top quartile of the distribution of past adjustments of the primary fiscal deficit derived from the sample of LICs, hence alleviating concerns of credibility of baseline assumptions.

- **Consistency between fiscal adjustment and growth**. The projected growth path for 2023 and 2024 is broadly in line with the multiplier-based projections. The realism of the expected adjustment is predicated on the authorities' commitment to fiscal consolidation, supported by revenue and spending measures, as well as efforts to strengthen the financial position of ENEE.

- **Consistency between public investment and growth**. The contribution of public investment to real GDP growth remains marginal across the previous and current DSA. Public investment is expected to increase to around 4 percent of GDP in the medium term.

COUNTRY CLASSIFICATION AND STRESS TESTS

8. **Honduras' debt-carrying capacity is classified as strong (Text Table 4).** Debt-carrying capacity is determined by a composite indicator (CI) that combines the World Bank's Country Policy and Institutional Assessment (CPIA) score, external conditions captured by world economic growth, and country-specific factors. Based on the April 2023 WEO vintage and the 2021 CPIA, the CI score for Honduras stands at 3.13, which is above the threshold of 3.05 applicable for a "strong" rating. The CI score reflects positive contributions from the CPIA (42 percent), international reserves (32 percent), world growth (12 percent), remittances (10 percent), and Honduras' real growth rate (3 percent). The debt burden thresholds implied by the strong debt-carrying capacity are summarized in Text Table 5.

Text Table 4. Honduras: CI Score Summary Table

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.39	3.39	1.31	42%
Real growth rate (in percent)	2.72	3.56	0.10	3%
Import coverage of reserves (in percent)	4.05	48.12	1.95	62%
Import coverage of reserves^2 (in percent)	-3.99	23.16	-0.92	-30%
Remittances (in percent)	2.02	15.49	0.31	10%
World economic growth (in percent)	13.52	2.86	0.39	12%
CI Score			3.13	100%
CI rating			Strong	

Source: IMF staff calculations. The CI cutoff for strong debt-carrying capacity is CI>3.05.

Text Table 5. Honduras: Debt Thresholds and Total Public Debt Benchmarks under Strong Debt-Carrying Capacity

Applicable thresholds

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	240
GDP	55
Debt service in % of	
Exports	21
Revenue	23

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	70

Source: IMF staff calculations.

9. **The DSA relies on standardized, tailored, and contingent liability stress tests.** While all six standardized stress tests apply to Honduras, only the natural disaster and market financing tailored stress tests are triggered. Honduras qualifies for a natural disaster tailored shock due to its exposure to frequent natural catastrophes such as hurricanes and droughts that have been exacerbated by climate change.[14] Honduras also qualifies for the market financing shock due to its outstanding Eurobonds.[15] However, the country does not qualify for a commodity price shock, which requires commodities to constitute at least 50 percent of total goods and services exports over the previous three-year period. While the default settings for the standardized and tailored shocks are considered appropriate for Honduras, the contingent liabilities test is customized as described in paragraph 2.

EXTERNAL DSA

10. **None of the PPG external debt burden indicators breach their respective thresholds under the baseline or the most extreme stress test (Figure 1, Tables 1 and 3).**

- ***Under the baseline scenario***, all the PPG external debt burden indicators are projected to remain comfortably below their prescribed thresholds throughout the DSA horizon. The PV of PPG external debt ratios to GDP and exports are expected to decline gradually from 2026, averaging 21 and 57 percent over the projection horizon (2023-33). The two peaks observed in 2027 and 2030 on debt service indicators are linked to the repayments of Eurobonds issued in 2017 and 2020.

[14] Specifically, Honduras meets the frequency criteria (2 disasters every 3 years) and economic loss criteria (above 5 percent of GDP per year) that trigger the natural disaster shock under the DSA.

[15] The market financing shock applies to LICs with market access, i.e., those that: (i) have outstanding Eurobonds; or (ii) meet the market access criterion for PRGT graduation but have not graduated due to serious short-term vulnerabilities.

- ***Under the customized stress test scenarios***, none of the PPG external debt burden indicators breaches its threshold. Under the most extreme shock in the standardized stress test – a scenario that combines shocks to growth, the primary balance, exports, other balance of payments flows, and the exchange rate – the PV of PPG external debt-to-GDP ratio is projected to sharply increase to 45.7 percent of GDP in 2026 before gradually receding over the projection horizon. Similarly, the PV of PPG external debt-to-exports peaks to 131.9 percent in 2026 before declining gradually. Both the PV of PPG external debt-to-GDP ratio and debt service-to-revenue ratios appear most sensitive to the stress test scenario that combines various shocks, while the PV of debt-to-exports and debt service-to-exports ratios are most adversely impacted by a shock to exports.

PUBLIC DSA

11. The PV of public debt-to-GDP ratio remains below its benchmark under the baseline but breaches it under the most extreme stress test (Figure 2, Tables 2 and 4).

- ***Under the baseline scenario***, the PV of public debt-to-GDP ratio is projected to gradually decline from 47.4 percent of GDP in 2023 to 42.6 percent of GDP in 2028 and thereafter, reaching 29.3 percent of GDP by 2043. This path is expected to be supported by reforms underpinning the ECF/EFF program which would open fiscal space for investment, while ensuring the return to a fiscal deficit of below 1 percent by 2026. All public debt indicators, including the PV of debt-to-revenue and the debt service-to-revenue ratios remain below their levels suggested in the historical scenario.
- ***Under the customized stress test scenarios,*** the PV of public debt-to-GDP ratio breaches its benchmark in the most extreme scenario—a growth shock—from 2028 onwards, illustrating the vulnerability of public debt dynamics to growth shocks. The growth shock also emerges as the most extreme stress test scenario for the PV of debt-to-revenue and the debt service-to-revenue ratios.

12. Market-financing risk indicators suggest low liquidity risks (Figure 5). The maximum gross financing needs over a 3-year period under the baseline projection horizon are expected to be around 6 percent of GDP, well below the benchmark value of 14 percent. EMBI spreads stood at 376 basis points as of August 18, 2023, below the benchmark level of 570 basis points.[16]

RISK RATING AND VULNERABILITIES

13. Honduras' risk of external debt distress remains low, while the risk of overall public debt distress is moderate. All PPG external debt burden indicators remain below their prescribed thresholds under the baseline and stress scenarios, thereby signaling a low risk of external distress.

[16] In the LIC DSF market financing module, near-term liquidity risks as measured by the projected baseline public gross financing needs over the next three years and current market sentiment as measured by the latest EMBI spread are compared against their respective benchmarks of 14 percent of GDP and 570 bps, respectively. A breach of both benchmarks would signal high market financing pressures.

However, the overall risk of public debt distressed is assessed as moderate—from low in the August 2021 published DSA—as the PV of debt to GDP ratio breaches its benchmark under the most extreme stress test scenario. Notwithstanding, debt-to-GDP ratios are expected to decline in the projection period as the overall fiscal balance gradually adjusts back to below 1 percent of GDP by 2026 in the baseline scenario. Nonetheless, with significant downside risks to the outlook, largely driven by a challenging global environment and adverse weather events, it would be important to consistently adhere to the reform agenda of the ECF/EFF program and continue to strike a balance between urgent investment and social spending needs and safeguarding debt sustainability.

Authorities' Views

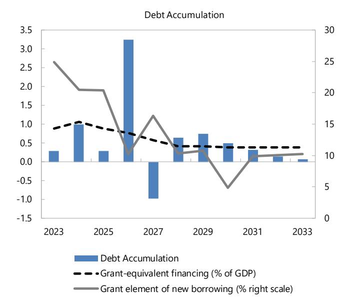
14. The authorities broadly agreed with the assumptions and results of the DSA. They acknowledged downside risks to the outlook, including from climate shocks and a deceleration of the maquila sector, given lower external demand. They noted that market financing risks have been abating, with EMBI spreads for Honduras gradually declining over the past few months. They also reiterated their commitment to transparency with the regularization of domestic debt that was previously unaccounted.

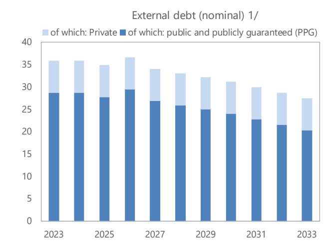
Table 1. Honduras: External Debt Sustainability Framework, Baseline Scenario, 2020-43

(In percent of GDP, unless otherwise indicated)

	Actual			Projections												Average 8/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2043	Historical	Projections
External debt (nominal) 1/	45.6	40.7	37.2	35.9	35.8	34.8	36.6	34.0	33.0	32.2	31.1	29.9	28.7	27.5	18.8	38.2	32.7
of which: public and publicly guaranteed (PPG)	37.0	32.5	30.0	28.7	28.6	27.7	29.5	26.9	25.9	25.0	23.9	22.8	21.5	20.3	11.7	30.4	25.5
Change in external debt	6.9	-5.0	-3.5	-1.3	-0.1	-1.0	1.8	-2.6	-1.0	-0.8	-1.1	-1.2	-1.2	-1.2	-0.7		
Identified net debt-creating flows	-2.3	-4.6	-3.0	2.1	1.7	1.2	0.7	0.3	0.1	0.1	0.2	0.2	0.2	0.2	0.5	-1.7	0.6
Non-interest current account deficit	-4.3	3.6	2.2	4.2	3.9	3.7	3.3	3.1	2.9	3.0	3.1	3.0	3.1	3.1	3.5	2.8	3.3
Deficit in balance of goods and services	15.4	23.1	23.8	25.2	25.1	24.7	23.9	23.2	22.7	22.4	22.1	21.9	21.5	21.1	17.9	18.5	23.1
Exports	35.2	38.9	41.9	38.9	37.8	37.7	37.6	37.2	36.9	36.9	36.9	36.9	36.9	36.9	36.9		
Imports	50.6	62.1	65.6	64.1	62.8	62.3	61.5	60.4	59.7	59.3	59.0	58.8	58.4	58.0	54.8		
Net current transfers (negative = inflow)	-25.1	-26.8	-28.2	-27.0	-26.8	-26.6	-26.2	-25.8	-25.4	-24.9	-24.5	-24.1	-23.7	-23.3	-19.6	-21.9	-25.3
of which: official	-0.3	-0.4	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	0.0		
Other current account flows (negative = net inflow)	5.4	7.2	6.6	5.9	5.6	5.5	5.6	5.6	5.5	5.5	5.5	5.3	5.3	5.3	5.2	6.2	5.5
Net FDI (negative = inflow)	-1.6	-1.8	-2.0	-2.1	-2.2	-2.3	-2.4	-2.5	-2.6	-2.6	-2.6	-2.6	-2.7	-2.7	-2.8	-3.6	-2.5
Endogenous debt dynamics 2/	3.6	-6.3	-3.1	0.1	0.0	-0.2	-0.2	-0.3	-0.2	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2		
Contribution from nominal interest rate	1.5	1.1	1.0	1.1	1.1	1.0	1.0	1.0	1.0	1.0	0.9	0.9	0.9	0.9	0.5		
Contribution from real GDP growth	3.7	-4.8	-1.5	-1.0	-1.1	-1.2	-1.2	-1.3	-1.2	-1.2	-1.2	-1.2	-1.1	-1.1	-0.7		
Contribution from price and exchange rate changes	-1.6	-2.6	-2.7	...	...	...	...	...	...	...	...	...	...	...	...		
Residual 3/	9.2	-0.4	-0.5	-3.5	-1.8	-2.2	1.1	-2.8	-1.1	-1.0	-1.3	-1.3	-1.4	-1.5	-1.2	2.8	-1.5
of which: exceptional financing	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators																	
PV of PPG external debt-to-GDP ratio	...	...	25.4	23.9	23.6	22.7	24.5	22.2	21.6	21.1	20.4	19.5	18.5	17.6	10.2		
PV of PPG external debt-to-exports ratio	...	...	60.6	61.4	62.5	60.2	65.2	59.7	58.5	57.1	55.1	52.8	50.2	47.5	27.6		
PPG debt service-to-exports ratio	12.7	5.0	5.3	6.6	7.6	7.8	5.2	9.6	4.6	4.3	7.8	4.9	5.1	5.0	2.9		
PPG debt service-to-revenue ratio	17.3	6.9	8.0	9.6	10.5	10.6	7.1	12.8	6.1	5.7	10.3	6.4	6.7	6.6	3.8		
Gross external financing need (Billion of U.S. dollars)	2.1	3.7	3.6	4.2	4.4	4.5	4.1	4.7	4.0	4.1	4.9	4.5	4.7	4.9	6.8		
Key macroeconomic assumptions																	
Real GDP growth (in percent)	-9.0	12.5	4.0	2.9	3.2	3.5	3.7	3.8	3.8	3.9	3.9	3.9	3.9	3.9	3.9	3.2	3.7
GDP deflator in US dollar terms (change in percent)	4.3	6.0	7.1	4.2	2.3	1.8	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.5	2.4	2.2
Effective interest rate (percent) 4/	3.8	2.8	2.8	3.1	3.1	3.0	3.0	3.0	3.0	3.1	3.0	3.2	3.2	3.2	3.0	3.3	3.1
Growth of exports of G&S (US dollar terms, in percent)	-15.9	31.9	19.8	-0.2	2.3	5.0	5.6	4.8	5.0	6.0	6.0	6.0	6.0	6.0	6.5	4.3	4.8
Growth of imports of G&S (US dollar terms, in percent)	-17.1	46.4	17.8	4.8	3.4	4.5	4.4	4.0	4.5	5.4	5.4	5.6	5.3	5.3	5.8	5.9	4.8
Grant element of new public sector borrowing (in percent)	...	...	...	24.9	20.5	20.4	10.2	16.3	10.3	10.8	4.9	9.9	10.0	10.3	0.0	...	13.5
Government revenues (excluding grants, in percent of GDP)	25.9	28.0	28.0	26.9	27.5	27.8	27.8	27.8	27.8	27.9	27.9	27.9	27.9	27.9	27.9	28.5	27.7
Aid flows (in Billion of US dollars) 5/	0.4	0.3	0.4	0.3	0.2	0.3	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.3		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	0.9	1.1	0.9	0.8	0.6	0.4	0.4	0.4	0.4	0.4	0.4	0.3	...	0.6
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	34.6	28.4	29.8	16.3	28.5	25.4	25.7	14.6	26.9	27.6	28.5	38.3	...	26.0
Nominal GDP (Billion of US dollars)	24	28	32	34	36	38	40	42	45	47	50	53	57	60	108		
Nominal dollar GDP growth	-5.0	19.3	11.4	7.2	5.6	5.3	5.8	5.9	5.9	6.0	6.0	6.0	6.0	6.0	6.5	5.7	6.0
Memorandum items:																	
PV of external debt 7/	...	...	32.5	31.1	30.8	29.8	31.7	29.4	28.8	28.2	27.5	26.7	25.7	24.7	17.4		
In percent of exports	...	...	77.7	79.8	81.5	79.3	84.2	79.0	77.9	76.5	74.6	72.2	69.6	67.0	47.0		
Total external debt service-to-exports ratio	42.3	29.2	26.7	26.4	27.9	28.2	25.0	28.5	23.0	22.2	25.2	21.7	21.4	20.8	15.2		
PV of PPG external debt (in Billion of US dollars)			8.0	8.1	8.5	8.6	9.8	9.4	9.7	10.0	10.2	10.4	10.5	10.5	11.0		
(PVt-PVt-1)/GDPt-1 (in percent)				0.3	1.0	0.3	3.2	-1.0	0.6	0.7	0.5	0.3	0.1	0.1	0.0		
Non-interest current account deficit that stabilizes debt ratio	-11.2	8.5	5.7	5.5	4.0	4.6	1.5	5.6	3.9	3.8	4.2	4.2	4.3	4.3	4.2		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**No**





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. The sizable 2020 residual is largely explained by the IMF and other IFI financing.

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

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

6/ 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).

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

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

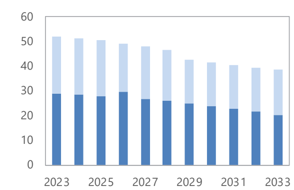
Table 2. Honduras: Public Debt Sustainability Framework, Baseline Scenario, 2020-43

(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
Public sector debt 1/	54.1	51.6	52.3	51.9	51.3	50.4	49.1	47.8	46.6	38.5	30.7	44.7	45.4
of which: external debt	37.0	32.5	30.0	28.7	28.6	27.7	29.5	26.9	25.9	20.3	11.7	30.4	25.5
Change in public sector debt	9.5	-2.5	0.7	-0.4	-0.7	-0.9	-1.2	-1.3	-1.2	-0.9	-0.9		
Identified debt-creating flows	6.5	-4.6	-6.4	-0.9	-0.7	-0.8	-1.2	-1.2	-1.2	-0.9	-0.9	-0.5	-1.0
Primary deficit	4.2	2.3	-1.2	0.7	0.2	0.0	-0.4	-0.4	-0.5	-0.5	-0.5	1.5	-0.2
Revenue and grants	26.6	28.6	28.4	27.2	27.9	28.2	28.1	28.1	28.1	28.2	28.2	29.2	28.0
of which: grants	0.6	0.5	0.4	0.3	0.4	0.3	0.3	0.3	0.3	0.3	0.3		
Primary (noninterest) expenditure	30.7	30.9	27.1	27.9	28.1	28.1	27.8	27.7	27.6	27.7	27.7	30.7	27.8
Automatic debt dynamics	2.7	-6.6	-4.9	-1.4	-0.7	-0.6	-0.7	-0.7	-0.6	-0.5	-0.4		
Contribution from interest rate/growth differential	4.5	-7.0	-4.7	-1.4	-0.7	-0.6	-0.7	-0.7	-0.6	-0.5	-0.4		
of which: contribution from average real interest rate	0.1	-1.0	-2.7	0.1	0.9	1.1	1.2	1.1	1.1	1.0	0.8		
of which: contribution from real GDP growth	4.4	-6.0	-2.0	-1.5	-1.6	-1.7	-1.8	-1.8	-1.8	-1.5	-1.2		
Contribution from real exchange rate depreciation	-1.8	0.4	-0.2	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	-0.4	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.1	0.0	0.0	-0.4	-0.1
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (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		
Debt relief (HIPC and other)	-0.4	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.1	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	2.9	2.2	7.1	0.5	0.0	-0.1	0.0	-0.1	0.0	0.0	0.0	3.0	-0.2
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	47.8	47.4	46.5	45.6	44.4	43.4	42.6	35.9	29.3		
PV of public debt-to-revenue and grants ratio	...	...	168.5	174.1	166.7	162.0	158.0	154.5	151.5	127.7	104.2		
Debt service-to-revenue and grants ratio 3/	16.9	6.8	7.9	20.6	23.0	23.1	18.6	23.1	19.0	18.1	16.8		
Gross financing need 4/	8.3	3.9	0.7	6.0	6.4	6.3	4.7	6.0	4.7	4.6	4.3		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	-9.0	12.5	4.0	2.9	3.2	3.5	3.7	3.8	3.8	3.9	3.9	3.2	3.7
Average nominal interest rate on external debt (in percent)	4.0	2.9	2.9	3.2	3.3	3.2	3.2	3.3	3.4	3.9	4.3	3.6	3.4
Average real interest rate on domestic debt (in percent)	-5.1	-3.5	-8.4	1.4	2.7	3.4	3.6	3.6	3.8	3.8	2.7	-4.5	3.4
Real exchange rate depreciation (in percent, + indicates depreciation)	-5.1	1.3	-0.7	...	...	...	...	...	...	...	...	0.0	...
Inflation rate (GDP deflator, in percent)	5.4	3.6	9.1	5.8	4.7	4.1	4.0	4.0	4.0	4.0	5.1	4.8	4.2
Growth of real primary spending (deflated by GDP deflator, in percent)	-6.0	13.1	-8.6	5.7	4.1	3.5	2.3	3.8	3.4	3.9	3.9	1.6	3.9
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-5.3	4.8	-1.9	1.1	0.9	0.9	0.8	0.9	0.8	0.5	0.4	-0.8	1.0
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/



Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The entire public sector, including SOEs . Definition of external debt is Currency-based. -0.7 -0.9 -1.2 -1.3 -1.2 -4.1

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

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

4/ 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 and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2023-33

(In percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of debt-to GDP ratio											
Baseline	24	24	23	25	22	22	21	20	20	19	18
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	24	21	18	19	15	14	12	10	9	7	6
B. Bound Tests											
B1. Real GDP growth	24	26	27	29	26	25	25	24	23	22	21
B2. Primary balance	24	25	26	28	25	25	25	24	23	22	21
B3. Exports	24	29	38	40	37	36	36	34	33	31	29
B4. Other flows 3/	24	33	42	43	41	40	39	38	36	34	32
B5. Depreciation	24	30	20	23	20	19	19	18	17	17	16
B6. Combination of B1-B5	24	37	44	46	43	42	41	40	38	36	33
C. Tailored Tests											
C1. Combined contingent liabilities	24	27	26	28	26	25	26	26	25	24	23
C2. Natural disaster	24	27	26	28	26	25	26	26	25	24	24
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	24	26	25	27	25	24	24	23	22	21	20
Threshold	55	55	55	55	55	55	55	55	55	55	55
PV of debt-to-exports ratio											
Baseline	61	63	60	65	60	59	57	55	53	50	48
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	61	56	49	49	41	37	33	28	24	20	15
B. Bound Tests											
B1. Real GDP growth	61	63	60	65	60	59	57	55	53	50	48
B2. Primary balance	61	65	69	74	68	67	67	66	64	61	58
B3. Exports	61	86	126	132	125	123	120	116	111	105	99
B4. Other flows 3/	61	88	111	115	110	108	106	102	97	92	86
B5. Depreciation	61	63	43	48	43	41	40	38	37	36	34
B6. Combination of B1-B5	61	98	103	123	117	116	113	109	104	98	92
C. Tailored Tests											
C1. Combined contingent liabilities	61	72	70	75	70	69	72	70	68	65	62
C2. Natural disaster	61	73	71	76	71	70	73	72	70	67	65
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	61	63	60	65	60	59	58	56	53	50	48
Threshold	240	240	240	240	240	240	240	240	240	240	240
Debt service-to-exports ratio											
Baseline	7	8	8	5	10	5	4	8	5	5	5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	7	8	7	5	9	4	3	6	3	3	3
B. Bound Tests											
B1. Real GDP growth	7	8	8	5	10	5	4	8	5	5	5
B2. Primary balance	7	8	8	6	10	5	5	8	6	6	6
B3. Exports	7	9	11	9	15	8	8	13	10	11	10
B4. Other flows 3/	7	8	9	7	12	7	6	11	9	9	9
B5. Depreciation	7	8	8	4	9	4	4	7	3	4	4
B6. Combination of B1-B5	7	8	10	8	13	7	7	12	10	10	10
C. Tailored Tests											
C1. Combined contingent liabilities	7	8	8	6	10	5	5	8	5	6	6
C2. Natural disaster	7	8	8	6	10	5	5	9	6	6	6
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	7	8	8	5	10	5	4	8	9	5	5
Threshold	21	21	21	21	21	21	21	21	21	21	21
											Tal
Debt service-to-revenue ratio											
Baseline	10	10	11	7	13	6	6	10	6	7	7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	10	10	10	6	12	5	4	9	4	4	4
B. Bound Tests											
B1. Real GDP growth	10	11	12	8	15	7	7	12	8	8	8
B2. Primary balance	10	10	11	8	13	7	6	11	8	8	8
B3. Exports	10	11	12	10	16	9	8	14	11	11	11
B4. Other flows 3/	10	10	12	10	16	9	8	15	12	12	12
B5. Depreciation	10	13	13	8	15	7	6	12	6	6	6
B6. Combination of B1-B5	10	11	14	11	17	10	9	16	13	13	13
C. Tailored Tests											
C1. Combined contingent liabilities	10	10	11	8	13	7	6	11	7	8	7
C2. Natural disaster	10	10	11	8	13	7	6	11	7	8	7
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	10	10	11	7	13	6	6	11	11	7	7
Threshold	23	23	23	23	23	23	23	23	23	23	23

Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the threshold.

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

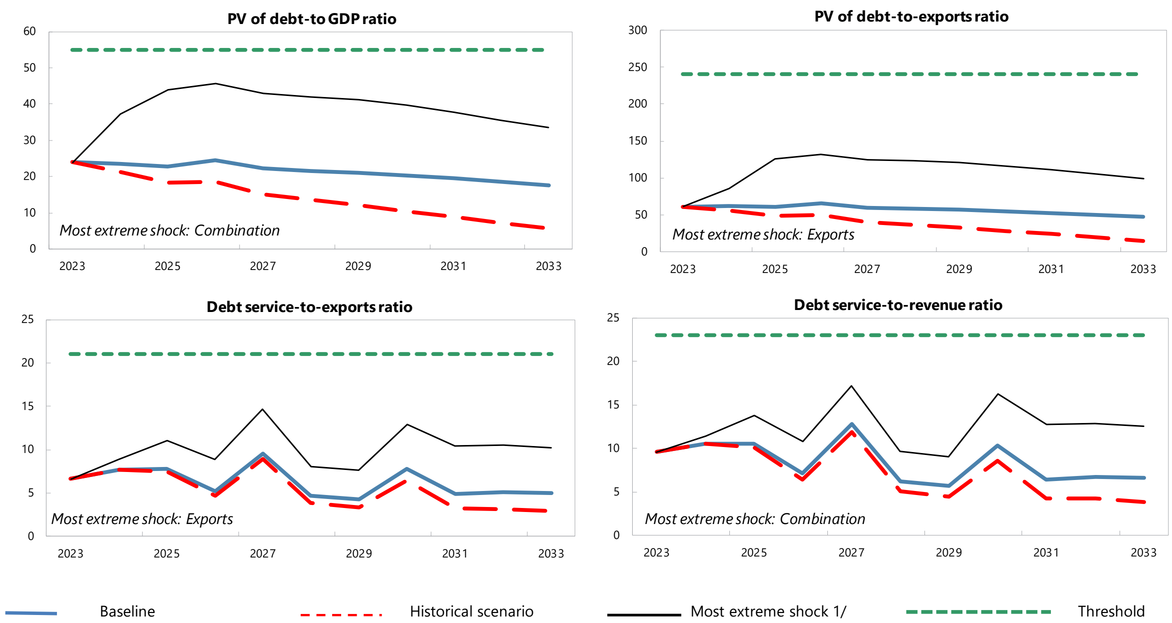
3/ Includes official and private transfers and FDI.

Table 4. Honduras: Sensitivity Analysis for Key Indicators of Public Debt, 2023-33
(In percent)

	Projections 1/										
	2023	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**	**2033**
	PV of Debt-to-GDP Ratio										
Baseline	47	47	46	44	43	43	39	38	37	37	36
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	47	48	48	49	49	50	48	49	51	52	53
B. Bound Tests											
B1. Real GDP growth	47	53	61	64	68	**72**	**72**	**76**	**79**	**83**	**87**
B2. Primary balance	47	50	54	53	52	51	48	47	46	45	45
B3. Exports	47	51	59	58	56	55	51	50	49	47	46
B4. Other flows 3/	47	56	65	63	62	61	57	56	54	52	50
B5. Depreciation	47	50	46	43	40	37	32	29	27	24	22
B6. Combination of B1-B5	47	48	51	51	51	51	48	47	47	47	47
C. Tailored Tests											
C1. Combined contingent liabilities	47	59	58	57	56	55	51	50	49	48	48
C2. Natural disaster	47	57	57	56	55	55	51	51	50	50	50
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	47	47	46	44	43	43	39	38	37	37	36
TOTAL public debt benchmark	70	70	70	70	70	70	70	70	70	70	70
	PV of Debt-to-Revenue Ratio										
Baseline	174	167	162	158	155	152	138	135	133	130	128
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	174	171	171	173	176	179	172	176	180	183	187
B. Bound Tests											
B1. Real GDP growth	174	189	216	228	241	255	255	268	282	295	308
B2. Primary balance	174	180	193	189	186	183	169	166	163	161	158
B3. Exports	174	183	209	204	200	197	182	179	173	168	163
B4. Other flows 3/	174	202	230	225	221	217	203	198	191	185	179
B5. Depreciation	174	178	165	153	143	133	113	104	95	86	77
B6. Combination of B1-B5	174	172	183	182	181	180	169	169	168	168	167
C. Tailored Tests											
C1. Combined contingent liabilities	174	211	206	202	198	195	181	178	175	172	170
C2. Natural disaster	174	206	202	199	197	195	182	181	179	178	176
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	174	167	162	158	155	152	138	136	133	130	128
	Debt Service-to-Revenue Ratio										
Baseline	21	23	23	19	23	19	18	25	17	18	18
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	21	23	23	19	24	20	22	30	23	25	26
B. Bound Tests											
B1. Real GDP growth	21	25	28	24	30	26	31	44	36	39	41
B2. Primary balance	21	23	24	21	25	21	27	35	20	22	22
B3. Exports	21	23	24	21	25	21	20	28	21	22	22
B4. Other flows 3/	21	23	25	21	26	22	21	30	23	24	23
B5. Depreciation	21	23	25	19	25	19	18	23	16	16	16
B6. Combination of B1-B5	21	23	25	22	27	22	22	29	21	23	23
C. Tailored Tests											
C1. Combined contingent liabilities	21	23	26	21	26	22	43	29	21	22	22
C2. Natural disaster	21	23	26	21	26	22	39	30	22	23	23
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	21	23	23	19	23	19	19	26	22	18	18

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the benchmark.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

Figure 1. Honduras: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2023-33



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	No	
Natural disaster	No	No
Commodity price	n.a.	n.a.
Market financing	No	No

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

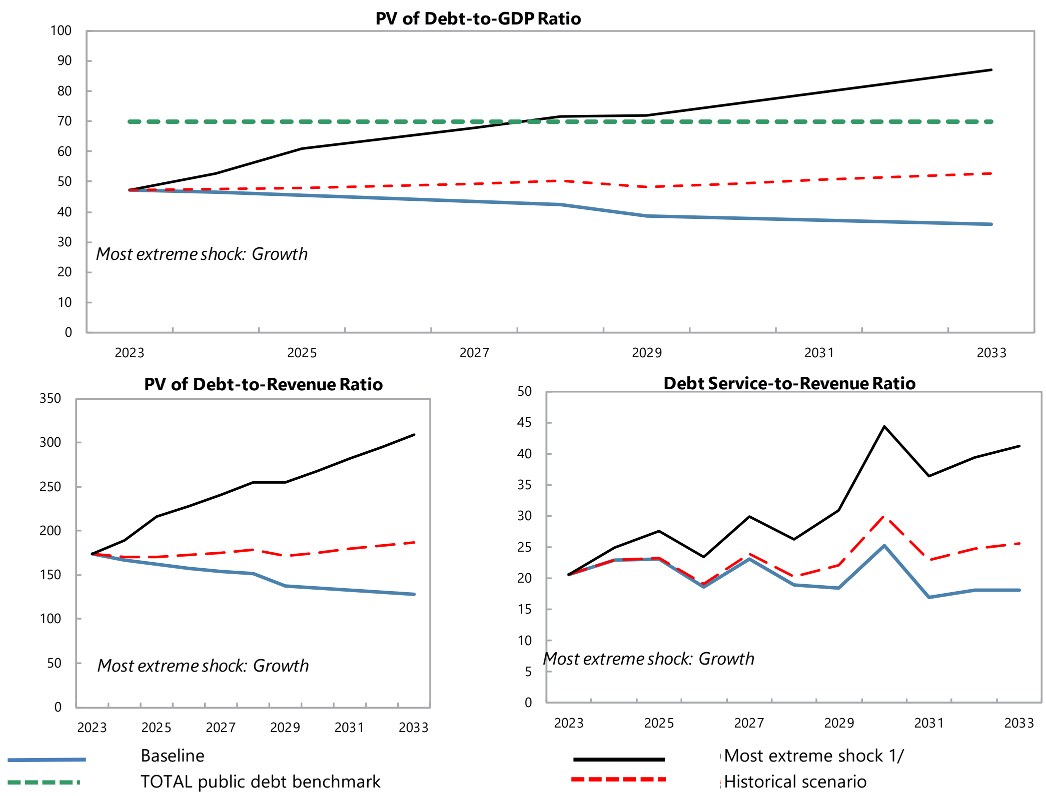
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	4.2%	4.2%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	5	5

* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 2. Honduras: Indicators of Public Debt Under Alternative Scenarios, 2023-33



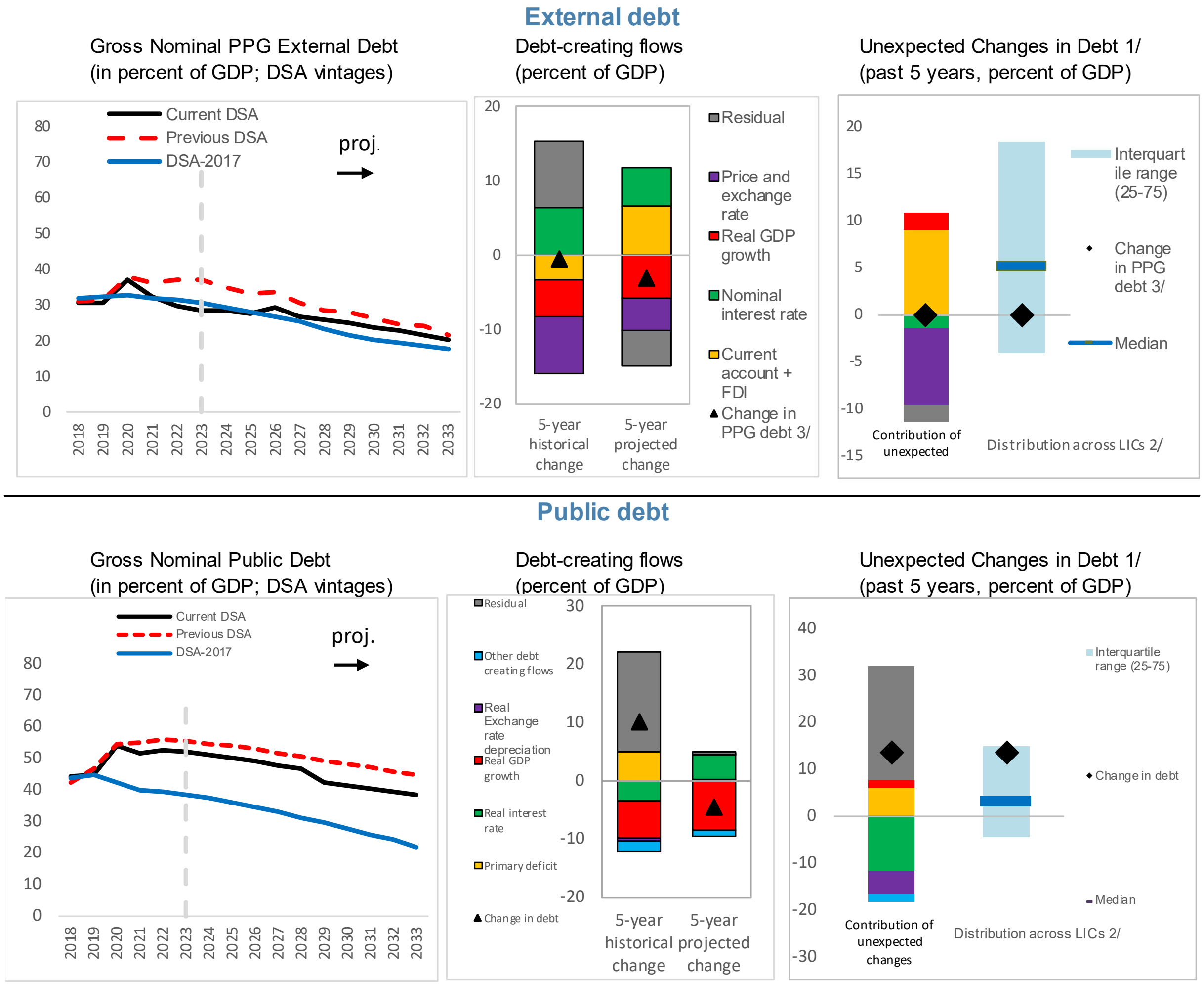
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	38%	30%
Domestic medium and long-term	62%	70%
Domestic short-term	0%	0%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	4.2%	4.2%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	5	5
Domestic MLT debt		
Avg. real interest rate on new borrowing	4.1%	4.1%
Avg. maturity (incl. grace period)	7	5
Avg. grace period	4	4
Domestic short-term debt		
Avg. real interest rate	0.0%	0.0%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Honduras: Drivers of Debt Dynamics—Baseline Scenario



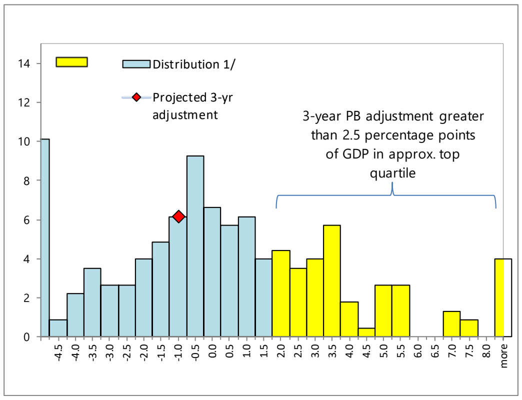
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

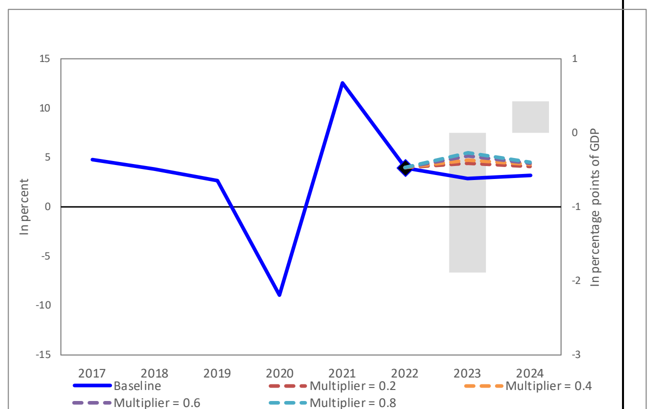
Figure 4. Honduras: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



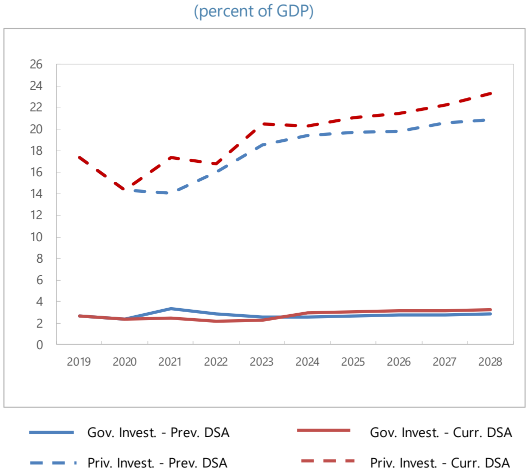
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(percent of GDP)



Contribution to Real GDP growth
(percent, 5-year average)

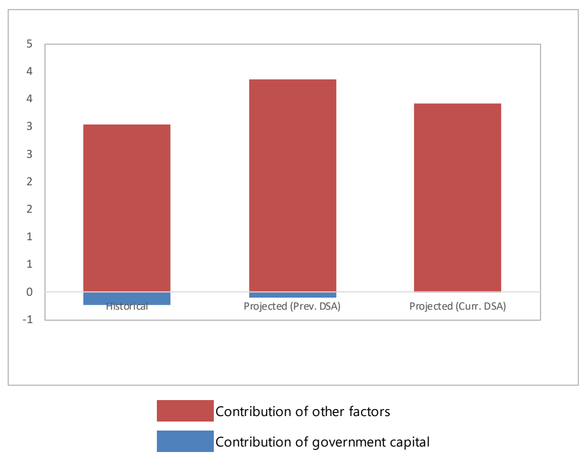
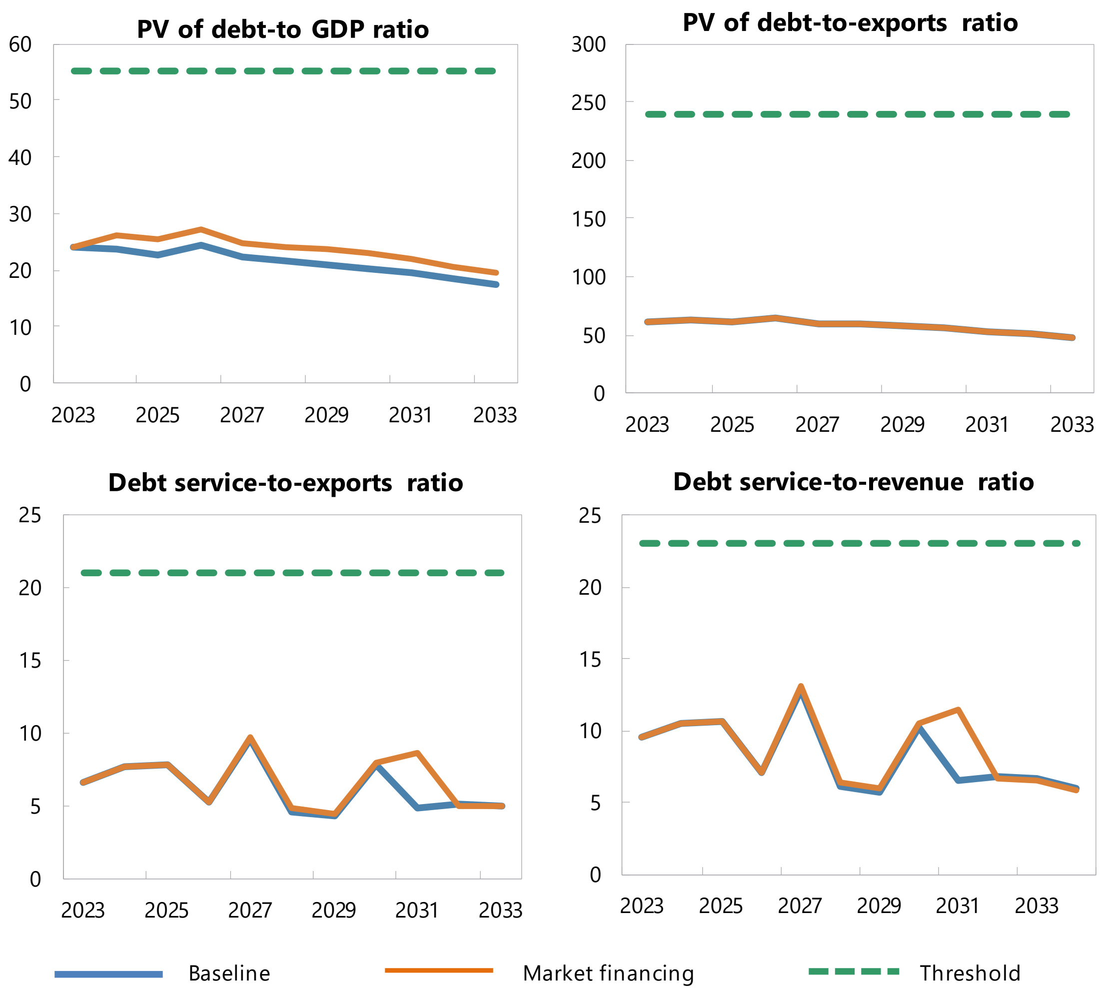


Figure 5. Honduras: Market Financing Risk Indicators

	GFN 1/	EMBI 2/
Benchmarks	14	570
Values	6	376
Breach of benchmark	No	No
Potential heightened liquidity needs	Low	

1/ Maximum gross financing needs (GFN) over 3-year baseline projection horizon.
2/ EMBI spreads correspond to the latest available data.



Sources: Country authorities; and staff estimates and projections.

INTERNATIONAL MONETARY FUND

HONDURAS

September 5, 2023

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION AND REQUESTS FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—INFORMATIONAL ANNEX

Prepared by: The Western Hemisphere Department (In Consultation with other Departments)

CONTENTS

FUND RELATIONS _____ 2

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS _____ 8

STATISTICAL ISSUES _____ 9

FUND RELATIONS

(As of July 31, 2023)

Financial Relations

Membership Status: Joined: December 27, 1945

General Resources Account:	**SDR Million**	**% Quota**
Quota	249.80	100.00
Fund holdings of currency (Exchange Rate)	482.55	193.17
Reserve Tranche Position	38.70	15.49

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	363.27	100.00
Holdings	30.37	8.36

Outstanding Purchases and Loans:	**SDR Million**	**% Allocation**
Stand-by Arrangements	271.45	108.67
SCF Arrangements	143.22	57.33

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
SCF	07/15/2019	01/14/2022	179.02	143.22
Stand-By	07/15/2019	01/14/2022	358.05	281.44
Stand-By	12/03/2014	12/02/2017	77.70	0.00

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

	Forthcoming				
	2023	2024	2025	2026	2027
Principal	45.17	141.99	114.14	53.68	31.83
Charges/Interest	13.37	23.35	17.34	14.19	13.43
Total	**58.54**	**165.34**	**131.48**	**67.88**	**45.26**

Implementation of Enhanced HIPC Initiative: Enhanced Framework

Commitment of HIPC Assistance	
Decision point date	June 2000[1]
Assistance committed (NPV terms)	
Total assistance (US$ million)	556.00
Of which: IMF assistance (US$ million)	30.30
Completion point date	April 2005

Disbursement of IMF Assistance (SDR million)

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

Implementation of MDRI Assistance

Total Debt Relieve (SDR million)[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.

Safeguards Assessment: The 2019 assessment found that the Banco Central de Honduras' (BCH) legal framework and governance arrangements have serious weaknesses that hamper the effectiveness of operations. While the revised central bank law that aimed at strengthening the institutional framework, transparency, governance, and financial autonomy of the BCH was submitted to Congress in 2021, it was not enacted. Consequently, the shortcomings in the legal framework seen in the last assessment are still evident. The bank continues to appoint good quality external auditors and has recently transitioned to the accounting framework based on International Financial Reporting Standards (IFRS). The authorities are also taking steps to align the BCH's internal audit function with international leading practices.

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

[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.

Nonfinancial Relations

Exchange Rate Arrangement:

Honduras' *de jure* exchange rate arrangement is classified as a crawling band. The de facto exchange rate arrangement was reclassified to "stabilized", since February 2022. The exchange rate of the lempira is determined in foreign exchange auctions of the BCH.

Honduras has accepted the obligations under Article VIII, Sections 2, 3, and 4 of the Articles of Agreement and currently maintains two multiple currency practices and an exchange restriction subject to Fund approval.

- An MCP subject to approval under Article VIII, Section 3 arises from a potential deviation of more than 2 percent between (i) the exchange rates required to be used for certain FX purchase/sale transactions (i.e., the TCR in force on the date of the specified previous day(s)) and (ii) the TCR in force on the day on which these FX purchase/sale transactions occur.

- A second MCP subject to approval under Article VIII, Section 3 arises from a potential deviation of more than 2 percent between (i) the exchange rates at which exchange agents (as well as customers via exchange agents) purchase FX at the BCH's FX auctions (i.e. the exchange rates offered to winning bids on the FX auction plus exchange commission of 0.4 percent for exchange agents and 0.5 percent for their customers) and (ii) the TCR in force on the day when the FX auction takes place (i.e. a weighted average exchange rate (WAR) of the winning bids of the previous business day's FX auction).

- In addition, Honduras maintains one exchange restriction subject to approval under Article VIII, Section 2(a). This arises from restrictions on the availability of FX for payments and transfers for current international transactions applied by the BCH by rejecting bids to purchase FX in the BCH FX auction made by exchange agents on behalf of customers who have not duly repatriated export proceeds of two export transactions in the defined repatriation timeframe.

Last Article IV Consultation:

On July 15, 2019 the Executive Board concluded the 2019 Article IV Consultation.

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 2019.

Department	Purpose	Time of Delivery
LEG	Governance Diagnostic	March, June 2019
MCM	CAPTAC: Operational Risk	March-19
	CAPTAC: Financial Supervision	May-19
	FPAS review	May-19
	Modernization of exchange rate policy and operations, and monetary policy implementation	May-19
MCM	CAPTAC: Monetary and FX Policy and interactions with Domestic Debt Market Development	February-20
	Developing FX Derivatives Regulatory Framework (Virtual)	October-20
	CAPTACDR: Expected Credit Loss model (Virtual)	November-20
	Accounting for FX Revaluations (Virtual)	December-20
	Nowcasting Tools Development	January-21
	CAPTACDR: Credit risk ECL model (Virtual)	February-21
	Honduras Central Bank's FX Derivatives Regulation Revision	May, June 2021
	Monetary Operations Scoping Mission (Virtual)	July, August 2021
	Derivatives Training (Virtual)	November-21
	Central Bank Liquidity Forecast and Management (Virtual)	January, March 2022
	Reference Exchange Rate New Methodology (Virtual)	February, March 2022
	Deciding on Introducing a retail CBDC I (Virtual)	March, April 2022
	ECL supervisory model phase II	April-22
	Semi Structural Model Update	November-22
	Drafting of Discussion Paper on CBDC	November, December 2022
	MTDS	January-23
	ECL supervisory model phase II	April-23
FAD	CAPTAC: Treasury - TSA	January-19
	CAPTAC: Post Clearance Process	March, April 2019
	CAPTAC: Workshop on Customs Intelligence	April-19

Department	Purpose	Time of Delivery
	CAPTAC: Strategic Planning	April-19
	Transparency of COVID-19 spending and the management of trust funds and on fiscal risks management	June-20
	Implementation of the trust funds action plan during COVID-19	March, October 2020
FAD	CAPTAC: support on budget preparation	April-20
	Compliance risk management	June-20
	Tax information management	July-20
	CAPTAC: Post clearance audits and risk management.	August-20
	CAPTAC: Internal Controls	December-20
	SOE's fiscal risks oversight	November-21
	Fiscal risks	August-2021
	Information management	October-21
	Tax gap estimation	November-21
	Managing compliance risks relative to tax incentives and construction	November, December 2021
	CIT incentives	February, 2023
	Trust funds	March-23
STA	CAPTAC: Quarterly data compilation and OSDS	January-19
	CAPTAC: National Accounts	March-19
	CAPTAC: National Accounts-Annual Accounts by Industry: Rebasing Project 2016 (I)	August-19
	CAPCTAC: National Accounts-Annual Accounts by Industry: Rebasing Project 2016 (II)	October-19
	CAPTAC: Sectoral Accounts	January-20

Department	Purpose	Time of Delivery
STA	CAPTAC: Consumer and Producer Price Index	January-20
	CAPTAC: Sectoral Accounts and Flow of Funds (remote)	November-20
	CAPTAC: Source Data for National Accounts (remote)	January-21
	CAPTAC: Balance of Payments (remote)	January-21
	CAPTAC: Producer Price Index (remote)	March-21
	CAPTAC: Sectoral Accounts and Flow of Funds (remote)	March-21
	CAPTAC: Household Income and Expenditure Survey Questionnaires (remote)	April-21
	CAPTAC: Employment Matrix (remote)	April-21
	CAPTAC: Supply and Use Tables (remote)	May-21
	CAPTAC: Quarterly National Accounts (remote)	August-21
	CAPTAC: Producer Price Index (remote)	October-21
	CAPTAC: Sectoral Accounts and Flow of Funds (remote)	October-21
	D4D: Residential Property Price Indices	April-22
	CAPTAC: Producer Price Index (remote)	May-22
	CAPTAC: Sectoral Account and Flow of Funds (remote)	June-22
	CAPTAC: QNA and seasonal adjustment (remote)	July-22
	CAPTAC: National Accounts: Backasting	February-23
	CAPTAC: Producer Price Index	March-23

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

A. Central American Bank of Economic Integration (CABEI)

https://www.bcie.org/en/member-countries/founders/republic-of-honduras

B. Inter-American Development Bank

https://www.iadb.org/en/countries/honduras/overview

C. World Bank

http://www.worldbank.org/en/country/honduras

STATISTICAL ISSUES

(As of July 2023)

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 the support of CAPTAC-DR. This project was planned to be concluded by 2021, however, due to the COVID-19 pandemic and the redefinition of priorities by the BCH's authorities, it is being redefined. Currently, the BCH is conducting a National Household Income and Expenditure Survey (N HIES), which will serve for the GDP and CPI rebasing at a date to be defined. **Labor statistics:** Honduras' National Institute of Statistics (INE) conducts its multipurpose household survey annually, which includes labor market information. More frequent data on employment and wages are required to better facilitate short-term policy analysis.
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 NHIES of 1998–99. A new NHIES for 2019 has been rolled out and is expected to be completed by end-2019. 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 August 18, 2023)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	August 2023	August 2023	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	August 2023	August 2023	D	D	D
Reserve/Base Money	June 2023	August 2023	M	M	M
Broad Money	June 2023	August 2023	M	M	M
Central Bank Balance Sheet	June 2023	August 2023	D	M	D
Consolidated Balance Sheet of the Banking System	June 2023	August 2023	M	M	M
Interest Rates[2]	May 2023	July 2023	W	M	M
Consumer Price Index	July 2023	August 2023	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	July 2023	August 2023	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	July 2023	August 2023	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	June 2023	August 2023	M	M	M
External Current Account Balance	March 2023	July 2023	Q	Q	Q
Exports and Imports of Goods and Services	May 2023	July 2023	Q	Q	Q
GDP/GNP	March 2023	July 2023	Q	Q	Q
Gross External Debt	June 2023	August 2023	M	M	M
International Investment Position[6]	March 2023	July 2023	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).

Statement by Mr. Guerra and Ms. Lankester Campos on Honduras
September 21, 2023

On behalf of our Honduran authorities, we would like to thank Mr. Llaudes and his team for their dedicated work, close engagement, and thorough analysis. We also thank Ms. Alonso-Gamo, management, and directors for their support and compromise with Honduras.

Honduras looks forward to a close and cooperative relationship with the Fund. The proposed program reflects the authorities' priorities towards supporting the most vulnerable population, increased public transparency, and a determined fight against corruption. Over the last two decades, Honduras has faced significant social and economic adversities, compounded by the COVID pandemic and recurrent adverse climate shocks.

Since the beginning of the administration of President Xiomara Castro in January 2022, the commitment to macroeconomic stability and social inclusion has been evident, despite the challenges posed by the complex international context, the fragile public financial situation left by past administrations, and climate shocks. The proposed program was designed to improve the social conditions of Hondurans by supporting the authorities' structural reform agenda, strengthening institutions, and increasing market and investor confidence while safeguarding macroeconomic stability. In this regard, the program will support the authorities' policies to reduce poverty and protect the most vulnerable population. The program also has an ambitious agenda to improve the quality of fiscal policy, strengthen its monetary policy framework, enhance financial stability, and, importantly, improve the governance framework and business environment.

The government recognizes the program with the Fund, as a financial catalyst to support their priorities, boost private sector investment, and reduce Honduras' lending costs. The authorities have a strong commitment to the program objectives and will maintain a close dialogue with the Fund to fulfill its objectives. The Honduran authorities recognize and appreciate the instrumental role that IMF technical assistance in fiscal, monetary, financial, and other areas will play going forward for the success of the program.

Recent Developments

Honduras' economy expanded 12.5 and 4.0 percent in 2021 and 2022, with strong domestic demand and manufacturing activity and robust remittance inflows. High-frequency data for July evidence an acceleration in economic activity. In 2023, the Central Bank expects the economy to grow between 3.0 and 3.5 percent, while in 2024, growth will be supported by domestic consumption and is expected to be 3.5 percent. Regarding staff's assessment, the authorities believe that there are potential upsides to growth coming, among other factors, from their efforts for enhanced public budget execution that will increase capital expenditure.

By the end of 2022, year-on-year inflation reached 9.8 percent, reflecting global inflationary pressures from rising commodity prices, disruptions in supply chains due to the pandemic, and price effects from the conflict in Ukraine. The impact of these shocks on the most vulnerable population was mitigated and minimized by the authorities' efforts. The government subsidized fuel prices and provided free energy to poor households; granted productivity-enhancing assistance in the form of seedlings and fertilizers; lowered interest rates for social and middle-class housing; and facilitated loans to the agricultural sector at low interest rates. Also, to assist households in extreme poverty and vulnerable groups in a focused manner, the authorities have, since late last year, implemented the flagship programs of Red Solidaria and Proasol.

Inflationary pressures have already declined significantly, from 10.4 percent in July 2022 to 5.15 percent in July 2023. The recent increase in oil prices in international markets impacted consumer inflation in August, reaching 5.71 percent, while the monthly variation was 0.5 percent. The Central Bank expects inflation to continue to decline as external supply shocks dissipate but will remain vigilant as upside risks remain. Inflation is expected to converge to the BCH's 4.0 percent (± 1.0 percentage point) upper limit by the end of 2023 and be within the target range by the first half of 2024.

The authorities want to reiterate their commitment to maintaining budgetary discipline and transparency. In fact, since the beginning of this administration, there is evidence that fiscal policy has remained prudent, with the deficit declining to near balance in 2022 and a recent slight increase to support their social agenda. In particular, the authorities have already taken significant decisions to strengthen budget administration and transparency. Last year, legislation to close public expenditure trust funds, a longstanding Fund recommendation, was approved in Congress. With the objective of reducing tax exemptions and strengthening controls for a fairer and more equitable tax system, the Law on Tax Justice was submitted to the National Congress. Also, to create more fiscal space and to create a solid and secure environment for private investment in the energy sector, the authorities are committed to the implementation of the necessary energy sector reforms, including the National Loss Reduction Plan for the national power company (Empresa Nacional de Energía Eléctrica, ENEE).

Moreover, they have a strong commitment to improving the fiscal and customs administration to lower smuggling and fiscal evasion and increase tax collection. In August, the system for asset declaration by public officials was activated. This platform will be used by sixty thousand public sector employees who must submit their annual asset declaration—a key change to fight corruption. This government has also implemented a geo-localization system for all investment projects in the country named "Honduras Inversiones." These measures have been internationally recognized: the Millennium Challenge Corporation announced in August that Honduras complies with the necessary requisites to receive their subvention support.

Despite the challenges from external shocks, the financial sector remains sound with a well-capitalized banking system. Credit growth has been robust, with its total stock reaching 67.5 percent of GDP by the end of 2022, compared to 64 percent in 2021. Non-performing loans (NPLs) in the banking system remained low at 2.3 percent of total loans, and provisioning remained adequate at 137 percent of NPLs. Recent stress tests by the National Banking and Insurance Commission (CNBS) confirm the resilience of the sector to significant shocks. The authorities have a strong commitment to further strengthen the regulatory framework and supervisory practices and increase financial deepening. Indeed, the CNBS has taken various measures, including streamlining documentation requirements for loan applications. Most of the recommendations of the 2016 Financial Sector Stability Review have been implemented.

Authorities' Commitment

The authorities consider the policies in the Memorandum on Economic and Financial Policies (Annex I) in accordance with their economic and social priorities and are suited to achieve the program's objectives. Moreover, the Government of Honduras stands ready to take any additional measures that may become appropriate.

The authorities acknowledge the importance of prudent fiscal policies to maintain debt sustainability and aim to mobilize external support to finance productive investment projects and adaptation to climate change. In this regard, the authorities will continue to gradually improve institutional implementation capacity through strengthened budget transparency and enhanced practices in public investment management. The authorities are aware of the efforts needed to further develop the domestic debt market and to diversify the sources of financing. Finally, the authorities recognize the importance of the Fiscal Responsibility Law (FRL) and are committed to enhancing its effectiveness.

The BCH is committed to the modernization and further enhancement of the monetary policy framework and will take the necessary measures to ensure that inflation remains on a downward path. To create more space for the interbank market and contribute to the disinflation process, on August 24th, the BCH modified the interest rate corridor, adjusting the Permanent Credit Facility (FPC) rate to 4.0 percent (prior action). Also, the program includes a quantitative performance criterion for the BCH's stock of domestic assets. The BCH would like to reinforce the message of its commitment to act, in accordance with its mandate and instruments, to ensure that exchange rate management maintains internal and external economic stability, supporting the country's productive capacity, trade, economic growth, and strengthening of international reserves.

The authorities are committed to implementing policies that support the crawling band regime and bolster financial inclusion while safeguarding the stability of the banking sector. Also, the authorities will proactively use macroprudential instruments as needed, considering high credit growth, a positive credit gap, and high household debt. They will monitor the associated risks of a significant credit expansion.

On the structural reform front, improvements to the governance framework are a key priority for the authorities. They are firmly committed to transparency and good governance and have already made significant progress to combat public-private corruption. Given the ambitious agenda on this front, there is a special interest in receiving TA from the Fund. Also, they recognize the importance of strengthening their legal AML/CFT framework. Regarding the governance weaknesses within EEH, the authorities are clear on the need to renegotiate the contracts as soon as possible to lower electricity prices for consumers as well as to improve the governance of the public electric company.

Honduras is one of the most vulnerable countries in the world to climate disasters. The authorities want to guarantee the protection of social investment in favor of the most vulnerable. The goal is to improve food security and increase sustainable public investment with a climate adaptation focus. There is a need to enhance the resilience of the energy sector and public infrastructure to climate events. Therefore, the authorities are interested in seeking additional Fund financing under the Resilience and Sustainability Fund (RSF) at a future program review to reduce the risks to the stability of the balance of payments related to climate change and the eventuality of pandemics.