**Statement by Mr. Moreno, Executive Director and Mr. Cartagena, Advisor to the Executive Director on Honduras**
**September 13, 2021**

On behalf of our Honduran authorities, we would like to thank Ms. Wong and her team for their hard work and proactive engagement in program negotiations. We also thank Management and the Board for their continued support during these challenging times.

## I. General remarks

**Honduras has underpinned its reform agenda with the Fund's supported programs since 2010**. Authorities attach high value to the engagement with the Fund, which continues to help anchor Honduras' economic policy agenda and reforms. The Fund's supported programs of the period 2010-2012 and 2014-2017, which were treated as precautionary, helped the country lift structural reforms, strengthen institutions and improve market and investor's confidence. Building on the progress achieved in those programs, Honduras has been engaged in a new Stand-by Agreement (SBA/SCF) since July 2019 to continue implementing economic and institutional reforms, increasing the quality of fiscal policy, strengthening its monetary policy framework and financial stability, and improving governance and the business environment.

**The authorities maintain a strong commitment to the program objectives even after the dual COVID-19 and climate shock.** The Fund's close dialogue and policy advice were instrumental in the country's satisfactory execution of the fourth review, amid the 2020 twin shocks. In this vein, Honduras continued implementing the policy agenda and objectives that authorities agreed with the Fund, with a few caveats in the timing of the reforms given the extraordinary circumstances. Going forward, the authorities remain firmly committed to fiscal sustainability. They intend to build on previous program achievements to strengthen the policy and institutional frameworks and to continue with the revenue mobilization agenda that will increase fiscal space to foster growth, reduce poverty, and put debt on a downward trajectory over the medium term. Honduras has been using the flexibility window in the Fiscal Responsibility Law (FRL) since 2020, and it has been extended through 2021-2022 to mitigate the impact of the lasting effects that the twin shocks have created.

**Technical Assistance has been instrumental in achieving the program's outcomes**. The authorities underline the importance of the Fund's support in fiscal, monetary, financial, and other areas that have facilitated moving ahead with the reform agenda set out in the program and to comply with the program's objectives and targets for this review. The Honduran authorities truly recognize the Fund as a trusted advisor.

## II. Recent Developments

**The financial support that Honduras has received through the SBA has allowed the country to achieve the program's objectives and support the recovery of its economy, which is expected to regain momentum in 2021**. The largest part of the country's economic contraction in 2020 was related to the effects of the COVID-19 pandemic, as well as the necessary policy response to protect human lives and businesses and mitigate the crisis' effects. The authorities deployed a well-targeted fiscal response to the pandemic, strengthened transparency and accountability frameworks, and reallocated nonpriority expenditures to finance the emergency needs caused by the virus and tropical storms. The economy is expected to recover in 2021 with economic growth closer to the upper limit of 3.2-5.2 percent, while inflation is in the band of 3.0-5.0 percent, closer to the midpoint of the band.

**The country is investing to overcome the impact of the two tropical storms that aggravated the economic shock**. As highlighted in Box 1 of the staff paper, Honduras has a history of climate change effects and natural disasters that have periodically affected the economy and well-being of the population. The most recent tropical storms, Eta and Iota, affected the country in November 2020 and caused infrastructure damages that deepened the economic contraction of that year. The Central Bank's estimates accounted for 1.3 percentage points of the 9.0 percent GDP contraction in 2020 as a result of the two tropical storms, and the country is still struggling to rebuild the damage caused up to this year.

**Vaccination advances are key to reducing the human impact of the pandemic and contributing to economic recovery.** With one of the highest cumulative confirmed and fatality rates among its closest regional neighbors (close to 3.5 confirmed cases and 0.1 fatalities per 100 habitants as of September 1st), Honduras continues struggling with the effects of the crisis. To face these challenges, the government has prioritized accelerating the vaccination process in order to reduce fatalities and promote a swifter economic recovery. The vaccination process has been speeding up to catch-up with some of its regional peers. As of September 1st, around 30 percent of Hondurans had received at least their first dose. To reduce contagion rates, the government continues to promote the use of facemasks, maintaining social distance, and other health measures.

**Consistent with the needs raised by the twin shocks, the authorities have maintained an expansive fiscal stance**. The fiscal deficit in the Non-Financial Public Sector (NFPS) is expected to rise to 5.4 percent of GDP in 2021, close to the rate registered in 2020 (5.5 percent of GDP). As shared in the authorities' Letter of Intent (LOI), the Honduran Congress approved increases in the ceilings on the NFPS deficit and current expenditure growth for 2020-2021, following the shock from the tropical storms. Authorities will pursue returning to the deficit ceiling in 2023, keeping public debt on a sustainable path and remaining committed to fiscal prudence, as well as working on the revenue mobilization agenda and preventing new tax incentives, including through special economic zones.

**The authorities continue to closely monitor the financial sector and are committed to preserving financial stability.** Despite the effects of the pandemic in the financial system and slight increases in Non-Performing Loans (NPL), bank liquidity, profitability and capital adequacy are currently adequate and NPLs are adequately provisioned. Authorities are committed to take the necessary regulatory measures according to the circumstances to guarantee liquidity, solvency, and disclosure of losses in the financial system. The authorities maintain their commitment to further strengthen the regulatory framework and supervisory practices.

## III. Program Performance and Authorities' Commitment

**Authorities stand committed to the program, as well as to continue implementing prudent macroeconomic policies and deep structural reforms.** As stated in the LOI, they are firmly committed to the program, including the main objectives of: (i) improving the quality of fiscal policy through reforms that protect investment and social spending while maintaining debt sustainability; (ii) strengthening monetary policy and financial institutions to buffer shocks and maintain stability; and (iii) improving the business environment and governance to foster inclusive growth, including by stepping up efforts to fight against corruption.

**Honduras' program remained broadly on track, despite the heavy tolls caused by the COVID-19 pandemic and the impact of climate change.** Honduras met the majority of end-December and end-June quantitative performance criteria and all but two indicative targets. The lasting effects of the twin shocks affected the performance of a few targets, such as the non-financial public sector balance because of higher-than-expected pandemic and storm-related emergency spending; ENEE's domestic arrears given liquidity pressures; the social spending target, due to slightly slower take-up of one measure on pandemic-related support and a shift to storm-related support; and the continuous PC on non-accumulation of external arrears due to a technical delay. Authorities request waivers of nonobservance given the extraordinary exogenous and endogenous shocks that have affected the performance of some of the program's outcomes.

**The Central Bank of Honduras (BCH) remains committed to the modernization and further enhancement of the monetary policy framework**. Authorities continue a policy dialogue with Congress to get support for the new central bank law that was submitted to Congress last year. This law is instrumental in strengthening CB's autonomy, transparency, and accountability, as well as governance structure. They are also making progress in reforming the monetary policy framework and in the transition to inflation targeting. Authorities support the transition to a more flexible exchange rate in the medium term and are already taking steps in this direction, including: continuing to adjust FX intervention rules to mitigate sharp moves in the exchange rate over time; introducing regulations to support the development of an FX derivatives market. The authorities will continue to work on the recommendations of the 2019 safeguard assessment as well as the reforms contained in the central bank's law and the steps towards the adoption of IFRS.

**A number of measures have been taken on the structural reform front, including on: (i) governance.** As acknowledged in the staff report, authorities continue to make progress on

governance and are committed to further developments. Authorities are improving transparency of public purchases, including submission of a new procurement law to Congress and measures related to COVID-19 spending; (**ii) the electricity sector**, authorities continue taking steps to implement the approved electricity sector law and reassessing generation contracts that had not come into effect. They are also addressing inconsistencies to ensure that new power purchase agreements can only be approved within the competitive framework under the sector law. The reform agenda is focusing on strengthening supervision, reducing losses, and strengthening governance, audit and scissions of the state-owned enterprise (ENEE).

As stated in the LOI, given the twin shocks of last year, our authorities have requested the extension of the SBA and SCF arrangements by two months to January 14, 2022, and a rephasing of the last availability date to allow for additional time to complete the last disbursement under the arrangements. Our authorities have also requested an aggregate augmentation of access by SDR149.88 million under the SBA and SCF arrangements to finance some of the lasting scares from the dramatic economic and social impact from the combined shock (COVID-19 pandemic and the economic impact of the two tropical storms of end 2020).