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AGENDA**

EBS/82/184  
Correction 1

CONFIDENTIAL

October 29, 1982

To: Members of the Executive Board  
From: The Secretary  
Subject: Honduras - Use of Fund Resources - Compensatory Financing Facility

The following corrections have been made in EBS/82/184 (10/12/82):

Page 2, last para., line 2: for "rise slightly to SDR 96.5 million,  
despite an"  
read "decline slightly to SDR 87.4 million,  
reflecting an"  
Page 3, column 1981, line 19: for "--" read "8.5"

column 1982, line 15: for "-9.6" read "-0.5"

line 16: for "-96.5" read "-87.4"

line 17: for "87.5" read "78.4"

line 22: for "-78.6" read "-69.5"

Corrected pages are attached.

Att: (2)



CONFIDENTIAL

INTERNATIONAL MONETARY FUND

HONDURAS

Use of Fund Resources--Compensatory Financing Facility

Prepared by the Research and Western Hemisphere Departments

(In consultation with the Exchange and Trade Relations,  
Legal and Treasurer's Departments)

Approved by Wm. C. Hood and E.W. Robichek

October 8, 1982

The Managing Director has been informed that the Honduran authorities will shortly request a purchase equivalent to SDR 23.1 million (45.3 per cent of quota) under the compensatory financing decision. The request is being made with respect to a shortfall in export earnings for the 12 months ended June 1982, and is expected to be considered by the Executive Board together with a request for a stand-by arrangement in an amount equivalent to SDR 76.5 million (150 per cent of quota). If approved, the proposed CF purchase would raise the member's purchases outstanding under the facility from 45.7 per cent to 91.0 per cent of quota, and the Fund's holdings of the member's currency from 209.2 per cent to 254.5 per cent of quota. A waiver of the limitation in Article V, Section 3(b)(iii) of the Fund's Articles of Agreement will be required and is being proposed.

This paper, which is being circulated in advance of the formal request from Honduras, is presented in four sections and an annex. The sections deal with: (1) the balance of payments position and cooperation with the Fund; (2) estimation of the export shortfall; (3) causes of the shortfall and earnings prospects; and (4) staff appraisal and proposed decision. The relations of Honduras with the Fund are summarized in the annex.

1. Balance of payments position and cooperation with the Fund

a. Balance of payments position 1/

After several years in which the overall balance of payments was in surplus, Honduras' external position weakened considerably in 1980 and

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1/ Developments in the balance of payments for 1981 and prospects for 1982 are reviewed in detail in the staff report on use of Fund resources under a stand-by arrangement expected to be considered by the Executive Board concurrently with this request.

1981, registering overall deficits of SDR 46.1 million and SDR 91.3 million, respectively (Table 1). Gross official international reserves, which had averaged SDR 157 million, or 12 weeks of imports during 1977-79, declined to SDR 102 million, or 6.5 weeks of imports, by the end of 1981.

The swing into overall deficit in 1980 reflected a sharp deterioration in the current account deficit which more than offset the rise in total capital inflows. The deficit in the current account doubled from an average of about SDR 128 million in 1977-79 to SDR 243 million in 1980, or from the equivalent of around 8 per cent of GDP in 1977-79 to nearly 13 per cent in 1980. This was a consequence of an acceleration in the rate of growth of imports at a time when the rate of increase of exports was decelerating, as well as of a sharp rise in net factor payments. The increase in imports reflected the combination of an expansionary fiscal policy, a sharp rise in the oil import bill, and an acceleration in the public investment program. Net capital inflows were higher because of an increase in official foreign financing associated with the public investment program but this increase was partly offset by a decline in foreign liabilities of the domestic banking system. The latter development reflected a reluctance of foreign banks to increase their exposure in the politically volatile Central American region, as well as delays in the adjustment of maximum lending rates in Honduras at a time when foreign rates of interest were rising sharply.

The deficit in the current account was reduced from around 13 per cent of GDP in 1980 to 11 per cent in 1981. This improvement, however, was more than offset by the large fall in net capital inflows. Although export income grew by only 2 per cent, the improvement in the current account position, in relation to GDP, resulted from a large deceleration in the rate of growth of imports and a decline in the value of net service payments. The deceleration in import growth was a consequence of a slowdown in both the public investment program and in overall economic growth, while the reduction in the deficit on net service payments was principally due to the fall in profit remittances abroad associated with a decline in income generated from mineral and banana exports. Net capital inflows declined from SDR 190 million in 1980 to SDR 154 million in 1981, with net capital outflows of SDR 11 million occurring from the financial sector. This outcome reflected a further curtailment of foreign commercial financing and the repayment of both medium- and short-term liabilities as a result of the adverse external reactions to the unsettled political situation in the region and the deterioration in the financial position of Honduras.

For 1982 the overall balance of payments deficit is estimated to decline slightly to SDR 87.4 million, reflecting an improvement in the capital account. Despite an expected decline in imports associated with a drop in real economic activity, the deficit in the current account is forecast to rise from SDR 257 million in 1981 to SDR 295 million in 1982 because of a decline in export income and a sharp rise in net service payments. The increase in net capital inflows this year is mainly a reflection of the

Table 1. Honduras: Balance of Payments, 1977-82

(In millions of SDRs)

|   | 1977     | 1978     | 1979     | 1980     | 1981     | 1982<br>Estimates |
|---|----------|----------|----------|----------|----------|-------------------|
| A. Current account  | -110.2   | -124.5   | -148.6   | -243.4   | -256.7   | -294.6            |
| Trade balance   | -59.3    | -67.0    | -73.9    | -145.4   | -162.5   | -167.8            |
| Exports, f.o.b.   | (453.8)  | (501.3)  | (585.5)  | (653.3)  | (664.7)  | (635.5)           |
| Imports, c.i.f.   | (-513.1) | (-568.3) | (-659.4) | (-798.7) | (-827.2) | (-803.3)          |
| Net services and transfers                                | -50.9    | -57.5    | -74.7    | -98.0    | -94.2    | -126.8            |
| B. Capital account  | 158.2    | 139.6    | 164.8    | 189.9    | 153.7    | 207.7             |
| Nonfinancial private sector                               | 42.4     | 46.0     | 42.5     | 64.8     | 31.1     | 9.0               |
| Nonfinancial public sector                                | 65.6     | 83.6     | 77.7     | 110.7    | 133.5    | 136.0             |
| Central Government  | (33.7)   | (63.9)   | (53.9)   | (96.4)   | (95.8)   | (111.9)           |
| Rest of public sector                                     | (31.9)   | (19.7)   | (23.8)   | (14.3)   | (37.7)   | (24.1)            |
| Financial intermediaries                                  | 50.3     | 10.0     | 44.6     | 14.4     | -10.9    | 23.8              |
| Central Bank  | (10.9)   | (11.7)   | (25.5)   | (20.7)   | (5.7)    | (21.0)            |
| Other   | (39.4)   | (-1.7)   | (19.1)   | (-6.3)   | (-16.6)  | (2.8)             |
| Debt relief   | --       | --       | --       | --       | --       | 38.9              |
| C. Allocation of SDRs and<br>valuation adjustments        | -5.0     | -8.2     | 2.1      | 7.4      | 11.7     | -0.5              |
| D. Overall balance (A+B+C)                                | 43.1     | 6.9      | 18.3     | -46.1    | -91.2    | -87.4             |
| Changes in net official<br>international reserves         | -43.1    | -6.9     | -18.3    | 46.1     | 82.8     | 78.4              |
| Of which Fund credit:                                     | (-6.3)   | (-10.5)  | (--)     | (11.8)   | (20.6)   | (61.7)            |
| Defaults  | --       | --       | --       | --       | 8.5      | -9.0              |
| Rescheduling  | --       | --       | --       | --       | --       | 9.0               |
| Arrears   | --       | --       | --       | --       | --       | 9.0               |
| <u>Memorandum items:</u>                                  |          |          |          |          |          |                   |
| International reserves of<br>the Central Bank at year end |          |          |          |          |          |                   |
| Net   | 112.6    | 119.5    | 137.8    | 91.7     | 8.9      | -69.5             |
| Gross   | 156.6    | 149.2    | 166.5    | 127.1    | 101.9    | 104.5             |
| Equivalent weeks of imports <u>1/</u>                     |          |          |          |          |          |                   |
| Net   | 10.3     | 9.4      | 9.0      | 5.8      | 0.6      | --                |
| Gross   | 14.3     | 11.8     | 10.8     | 8.0      | 6.6      | 6.5               |

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

1/ Imports of goods during following 12-month period.

disbursement of bilateral aid under the U.S. Caribbean Initiative and debt relief provided from the renegotiation of a part of the foreign commercial debt. No improvement is expected in gross international reserves.

b. Cooperation with the Fund

Since the proposed purchase by Honduras would raise outstanding CF purchases above 50 per cent of its quota, the request may be approved only if the Fund is satisfied that Honduras has been cooperating with it in efforts to find appropriate solutions for the member's balance of payments difficulties. The staff considers that this requirement is met by the adoption by Honduras of a financial program in support of which the authorities are requesting use of Fund resources under a stand-by arrangement in the upper credit tranches. In conjunction with the request for the stand-by arrangement, which is to be considered by the Board concurrently with the compensatory financing request, the staff is proposing Board approval of Honduras' exchange restrictions until the end of 1983 or the next Article IV consultation, whichever is earlier.

2. Estimation of the export shortfall

After increasing by 24 per cent in 1979/80, total export earnings declined by 3 per cent in 1980/81 and then grew by only one per cent in the shortfall year 1981/82. They are projected to recover slowly by 4 per cent in 1982/83 and then more strongly by 11 per cent in 1983/84.

Total exports in the shortfall year ended June 1982 amounted to SDR 609.7 million, about one per cent below the average level of the two pre-shortfall years and 9 per cent below the average of export earnings

Table 2. Honduras: Estimation of the Export Shortfall  
(In millions of SDRs)

|                   | Years Ending June |       |       |                                   |
|-------------------|-------------------|-------|-------|-----------------------------------|
|                   | 1980              | 1981  | 1982  | Projected Exports 1/<br>1983 1984 |
| Exports           | 620.2             | 604.1 | 609.7 | 632 703                           |
| Shortfall         |                   |       | 23.1  |                                   |
| Proposed purchase |                   |       | 23.1  |                                   |

1/ Based on the judgmental forecast of earnings given in Table 3.