FOR
AGENDA

EBS/82/184

CONFIDENTIAL

October 12, 1982

To: Members of the Executive Board

From: The Acting Secretary

Subject: Honduras - Use of Fund Resources - Compensatory Financing Facility

Attached for consideration by the Executive Directors is a paper on a request expected to be received from Honduras for a purchase equivalent to SDR 23.1 million under the compensatory financing facility. A draft decision appears on page 13.

It is proposed that this subject, the staff report for the 1982 Article IV consultation with Honduras (SM/82/151, 7/28/82, and Supplement 1, 10/8/82), and Honduras' request for a stand-by arrangement (EBS/82/179, 10/7/82) be brought to the agenda for discussion on Friday, November 5, 1982.

Att: (1)

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

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 rise slightly to SDR 96.5 million, despite 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 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 valuation adjustments	-5.0	-8.2	2.1	7.4	11.7	-9.6
D. Overall balance (A+B+C)	43.1	6.9	18.3	-46.1	-91.2	-96.5
Changes in net official international reserves	-43.1	-6.9	-18.3	46.1	82.8	87.5
Of which Fund credit:	(-6.3)	(-10.5)	(--)	(11.8)	(20.6)	(61.7)
Defaults	--	--	--	--	--	-9.0
Rescheduling	--	--	--	--	--	9.0
Arrears	--	--	--	--	--	9.0
Memorandum items:						
International reserves of the Central Bank at year end						
Net	112.6	119.5	137.8	91.7	8.9	-78.6
Gross	156.6	149.2	166.5	127.1	101.9	104.5
Equivalent weeks of imports 1/						
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				
				Projected Exports 1/	
	1980	1981	1982	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.

projected for the two post-shortfall years. On the basis of these movements, the shortfall for the year ended June 1982 is estimated at SDR 23.1 million, the amount of the proposed purchase (Table 2). 1/

3. Causes of the shortfall and earnings prospects

The total export shortfall of SDR 23.1 million is due largely to shortfalls for beef (SDR 7.1 million), metals (SDR 6.4 million), and "other exports" (SDR 6.3 million). Smaller shortfalls of about SDR 3 million each are estimated for sugar, tobacco, and coffee, while excesses are estimated for bananas (SDR 13.5 million) and shellfish (SDR 1.4 million).

Low volume was almost entirely responsible for the shortfall in beef exports, and both volume and price factors were responsible for the shortfall in metals (silver and lead). Export supply of beef was temporarily reduced because of a domestic pricing dispute between cattle breeders and meat packers. In the case of metals, a decline in export unit values caused by the world recession coincided with sharply lower volume resulting from a dispute between the mining company and the Government over taxes and other regulations. The fall in sugar exports was caused both by low export prices and reduced volume following the imposition of import quotas by the United States, which has been the only outlet for Honduran sugar exports in recent years. The shortfall in tobacco was caused entirely by lower volume as output was adversely affected by plant disease. Other exports suffered from depressed world demand and trade disputes with neighboring countries.

a. Bananas

Banana exports, which account for about 34 per cent of total exports, increased by 27 per cent in the shortfall year after rising by only 4 per cent in 1980/81. The large increase in the shortfall year was partly due to a recovery in volume, which had declined by 8 per cent in 1980/81 as a result of labor unrest, unfavorable weather conditions, and the incidence of disease (sigatoka).

Unit values in the shortfall year increased by about 4 per cent in U.S. dollar terms, roughly in line with the increase in the world price of bananas. Export earnings are projected to increase by 6 per cent in 1982/83 and by 8 per cent in 1983/84. The increase projected for 1982/83 would have been larger had exportable supplies not been affected by recent floods. As a result of these movements, an excess of SDR 13.5 million is estimated for bananas.

1/ Honduras made a CF purchase equivalent to SDR 23.3 million in January 1981 on account of a shortfall of that amount estimated for the year ended June 1981 (EBS/81/249). The total amount of that purchase is still outstanding.

Table 3. Honduras: Export Earnings and Shortfalls by Major Commodities

	Years Ending June								Shortfall	
	1977	1978	1979	1980	1981	1982	1983	1984	Geometric	Arithmetic
	(In millions of SDRs)									
Total	411.4	496.8	501.3	620.2	604.1	609.7	632	703	23.1	24.1
Bananas	100.0	114.6	140.3	158.1	165.2	210.3	223	241	-13.5	-10.8
Coffee	132.4	186.9	133.9	179.2	114.4	133.0	126	136	3.1	4.7
Beef	19.2	23.0	40.8	44.3	44.6	32.9	36	44	7.1	7.5
Wood	37.5	38.2	34.3	28.4	30.7	36.8	42	49	-0.2	0.6
Shellfish	13.2	13.3	13.0	19.4	18.1	26.0	29	34	-1.4	-0.7
Sugar	4.6	3.8	9.2	16.2	41.8	17.9	16	22	3.3	4.9
Tobacco		7.9	7.2	10.7	11.6	10.2	17	20	3.2	3.7
Cotton		10.1	11.2	9.9	8.9	7.2	7	7	0.7	0.8
Metals		27.2	30.5	36.6	37.0	27.5	31	39	6.4	6.7
Silver		(9.8)	(11.2)	(18.9)	(19.6)	(9.4)	(13)	(14)	(5.1)	(5.6)
Lead		(6.4)	(9.7)	(9.6)	(8.0)	(4.4)	(6)	(9)	(2.7)	(3.0)
Zinc		(11.0)	(9.6)	(8.1)	(9.4)	(13.7)	(12)	(16)	(-2.2)	(-1.9)
Others	104.5	71.8	80.9	117.4	131.8	107.9	105	111	6.3	6.7
	(Percentage Change)									
Total		21	1	24	-3	1	4	11		
Bananas		15	22	13	4	27	6	8		
Coffee		41	-28	34	-36	16	-5	8		
Beef		20	77	9	1	-26	9	22		
Wood		2	-10	-17	8	20	14	17		
Shellfish		1	-2	49	-7	44	12	17		
Sugar		-17	142	76	158	-57	-11	38		
Tobacco			-9	49	8	-12	67	18		
Cotton			11	-12	-10	-19	-3	--		
Metals			12	20	1	-26	13	26		
Silver			(14)	(69)	(4)	(-52)	(38)	(8)		
Lead			(52)	(-1)	(-17)	(-45)	(36)	(50)		
Zinc			(-13)	(-16)	(16)	(46)	(-12)	(33)		
Others		-31	13	45	12	-18	-3	6		

Table 4. Honduras: Value, Volume and Unit Value by Major Commodities

(In millions of SDRs)

	Value Share in Total Exports in 1981 (In Per Cent)	Years Ending June								Shortfall in Per Cent of Level in Shortfall Year
		1977	1978	1979	1980	1981	1982	1983	1984	
Value	82.2	61	85	84	100	94	100	105	118	3.1
Bananas	34.5	48	54	67	75	79	100	106	115	-6.3
Coffee	21.8	100	141	101	135	86	100	95	102	2.4
Beef	5.4	58	70	124	135	136	100	109	132	21.4
Wood	6.0	102	104	93	77	83	100	114	133	0.6
Shellfish	4.3	51	51	50	75	70	100	112	129	-5.4
Sugar	2.9	26	21	51	91	234	100	92	125	19.6
Tobacco	1.7	—	77	71	105	114	100	171	193	31.6
Cotton	1.2	—	140	156	138	124	100	90	101	9.2
Metals	4.4	—	99	111	133	134	100	114	140	23.3
Silver	(1.5)	(—)	(104)	(119)	(201)	(209)	(100)	(140)	(146)	(53.7)
Lead	(0.7)	(—)	(145)	(220)	(218)	(182)	(100)	(139)	(200)	(61.6)
Zinc	(2.2)	(—)	(80)	(70)	(59)	(69)	(100)	(88)	(116)	(-16.1)
Volume		73	99	109	107	100	100	99	105	2.2
Bananas		75	84	98	98	90	100	100	106	-1.3
Coffee		68	102	113	111	98	100	89	91	-2.5
Beef		98	107	148	155	149	100	97	110	19.8
Wood		158	150	130	105	97	100	108	117	5.2
Shellfish		76	90	59	76	85	100	100	103	-7.8
Sugar		32	26	66	101	117	100	104	116	7.3
Tobacco		—	127	107	133	130	100	155	161	34.0
Cotton		—	168	160	135	111	100	93	93	5.3
Metals		—	155	154	128	116	100	116	125	16.6
Silver		(—)	(199)	(192)	(165)	(143)	(100)	(156)	(140)	(38.8)
Lead		(—)	(208)	(234)	(195)	(171)	(100)	(136)	(168)	(50.1)
Zinc		(—)	(109)	(103)	(81)	(80)	(100)	(83)	(101)	(-11.5)
Unit Value		84	85	77	93	95	100	106	112	1.0
Bananas		64	65	68	77	88	100	106	108	-5.0
Coffee		147	138	89	122	88	100	107	112	5.2
Beef		59	66	84	87	91	100	112	121	1.4
Wood		65	69	72	74	86	100	106	114	-5.1
Shellfish		67	57	85	98	82	100	112	125	2.4
Sugar		79	81	78	89	199	100	88	108	11.0
Tobacco		—	61	66	79	87	100	110	120	-1.9
Cotton		—	83	97	102	112	100	97	109	3.8
Metals		—	64	72	104	116	100	98	112	5.8
Silver		(—)	(53)	(62)	(122)	(146)	(100)	(90)	(104)	(10.8)
Lead		(—)	(70)	(94)	(112)	(106)	(100)	(102)	(119)	(7.6)
Zinc		(—)	(74)	(68)	(73)	(86)	(100)	(106)	(115)	(-5.2)

b. Coffee

Coffee, the second largest source of export earnings, accounted for 22 per cent of total earnings in the shortfall year ended June 1982. After declining by 36 per cent in 1980/81, earnings from coffee increased by 16 per cent in the shortfall year, largely on account of a 14 per cent increase in export unit values; export volume increased by 2 per cent in the shortfall year even though exports were constrained by quotas imposed under the International Coffee Agreement (ICA).

Although production is expected to increase by 12 per cent in the 1982/83 coffee year (October/September), the volume of exports will continue to be constrained by ICA quotas and by the increasing competition for nonquota markets. Though the total global quota for the 1982/83 coffee year has been set at the same level as at the beginning of the 1981/82 coffee year (56 million bags), Honduras' quota has been reduced from 960 thousand bags to 772 thousand bags, mainly because the share of the other milds group of coffee in the total global quota was reduced from 23.5 per cent in the 1981/82 coffee year to 21.6 per cent in the 1982/83 coffee year. In addition, Honduras' share within the other milds group was reduced from 7.3 per cent in 1981/82 to 6.4 per cent in 1982/83. The recovery in export unit values experienced in the shortfall year, which is attributable to the regulation of exports by ICA quotas, is expected to continue, but at a more moderate rate, and export unit values are projected to increase at an annual rate of 6 per cent during the two post-shortfall years. On the basis of these volume and export unit value projections, earnings from coffee are expected to decline by 5 per cent in the first post-shortfall year and to recover by 8 per cent in the second to a level slightly higher than that in the shortfall year. The average level of earnings from coffee in the two post-shortfall years (SDR 131 million) is expected to be 8 per lower than the average value (SDR 143 million) in the pre-shortfall years.

c. Beef

Beef export earnings declined by 26 per cent in the shortfall year, as a result of a 33 per cent fall in export volume which was only partially offset by a 10 per cent increase in price. The volume decline was caused by a domestic pricing dispute between cattle breeders and meat packers. The cattle breeders, dissatisfied with the price being offered by the meat packers, reduced sharply the numbers of cattle that they were willing to sell.

In June 1982, the price offered to cattle breeders was increased by 13 per cent and beef production has been increasing during July and August. Export prices are expected to continue to improve at about the same rate as hitherto, and the value of beef exports is expected to recover in 1982/83 and 1983/84 by 9 per cent and 22 per cent, respectively, but the level of earnings in 1983/84 is still not expected to reach the levels attained in 1979/80 and 1980/81. A shortfall of SDR 7.1 million is estimated.

d. Wood

Wood exports increased by 20 per cent in the shortfall year mainly as a result of higher prices; volume rose by only 3 per cent. Volume would have increased more sharply, except that in the first half of 1982 it dropped by 11 per cent relative to the first half of 1981, mainly as a result of unfounded concern abroad (particularly in the Caribbean, the major market) that Honduran wood was diseased.

Export earnings from wood are expected to recover by 14 per cent in 1982/83 and to increase 17 per cent in 1983/84. Prices are forecast to rise steadily at between 6 and 7 per cent per year as world demand improves, and volume is expected to increase by 8 per cent in each of the two post-shortfall years, as an increased sawmill capacity comes on stream. An excess of SDR 0.2 million is estimated for wood exports.

e. Sugar

Earnings from sugar exports fell by 57 per cent in the shortfall year because of a 50 per cent drop in export unit values and a 15 per cent decline in export volumes. The world free market price of sugar fell by 51 per cent in the shortfall year because of the large world surplus which was brought about by the sharp increase in world production in response to the very high prices of 1980. The average price of sugar, which peaked at 41 cents per pound in October 1980, dropped to an average of 12 cents for the twelve months ended June 1982; by early October 1982, it had fallen to only 6.5 cents per pound. The decline in export volume in the shortfall year is largely attributable to the introduction in May 1982 of import quotas by the United States, which has been the sole market for Honduran sugar exports for the last six years. 1/ The U.S. quota system is intended to support domestic producers by maintaining prices at levels nearly three times as high as those currently ruling on the free market.

Sugar exports to the United States are expected to be subject to quota restrictions during the two post-shortfall years. However, the Honduran authorities have succeeded in finding alternative markets for all of the expected exportable production surplus displaced from the U.S. market during the 1982/83 season (November/June), and they expect to do likewise in the following year. Honduras is a member of the International Sugar Agreement (ISA), but it is classified as a small exporter and hence is not subject to export quotas, nor is it obligated to accumulate special stocks of sugar.

1/ Between May 11 and June 30, 1982, Honduras was only permitted to export 1,996 tons to the United States, while in the previous three years an average of 19,000 tons was exported to the United States during the two months May and June.

The volume of sugar exports is expected to recover by 4 per cent in the first post-shortfall year and by a further 12 per cent in the second. About 30 per cent of Honduras' sugar exports will have preferential access to the U.S. market where they will be sold at a price substantially higher than the world market. The rest will be sold on the world market where prices are expected to remain depressed during the first post-shortfall year owing to the continuing global sugar surplus. As a result, export unit values which averaged 15 cents per pound in 1981/82 are expected to decline by 12 per cent in the first post-shortfall year. In the second post-shortfall year, the world sugar surplus is expected to ease, and average export unit values are projected to rise by 23 per cent. On the basis of these price and volume projections, earnings from sugar exports are expected to decline by 11 per cent in the first post-shortfall year but to recover by 38 per cent in the second.

f. Shellfish

The value of shellfish (shrimp and lobster) exports increased by 44 per cent in the shortfall year as a result of sizable increases in both export unit values and volumes. The increase in unit values of 9.5 per cent in U.S. dollar terms (22 per cent in terms of SDRs) was in line with the rise in prices in the United States, the major outlet for Honduran exports. The volume of exports increased by 18 per cent largely on account of an agreement permitting Honduran boats to operate in Colombian waters, as well as some increase in the size of the Honduran fishing fleet.

In the post-shortfall period, export unit values are expected to increase at an annual rate of 12 per cent, but the average volume of exports is expected to be virtually the same as in the shortfall year because of fishing restrictions in coastal waters shared with Nicaragua. Earnings from shellfish exports are projected to increase at an annual rate of 13 per cent per annum. A small excess of SDR 1.4 million is estimated for earnings from shellfish exports.

g. Tobacco

The volume of tobacco exports declined by 23 per cent in the shortfall year because the crop was reduced by plant disease. Export earnings declined by 12 per cent in 1981/82 following increases of 49 per cent and 8 per cent in each of the two pre-shortfall years.

Export earnings are expected to recover strongly in 1982/83, as the disease is now under control and three new tobacco areas have been brought into production by a new tobacco company. The price of tobacco is expected to maintain its upward trend. A shortfall of SDR 3.2 million is estimated.

h. Cotton

Since 1977/78 the volume of cotton exports has been declining steadily as a result of the reallocation of acreage toward more profitable basic grains. This trend is expected to continue through 1983. Prices, after rising in 1980/81, fell by 11 per cent in the shortfall year. Export earnings declined by 19 per cent in the shortfall year compared to an annual average rate of decline of 11 per cent in the two pre-shortfall years. Exports are expected to decline further by 3 per cent in 1982/83 and to remain at that level in 1983/84. A shortfall of SDR 0.7 million is estimated.

i. Metals

Silver, lead and zinc, the three main metals exported by Honduras, are all produced by a single company which is a subsidiary of a large international mining corporation. The volume of silver and lead exports declined sharply in the shortfall year, partly because of a dispute between the company and the Government over taxes, employment levels and social benefits, and partly because of weak world demand conditions. In the case of zinc, increases were recorded for both export volume (25 per cent) and export unit value (16 per cent). The movement in export unit value was in line with world zinc prices, which increased by 16 per cent in the shortfall year because of a shortage of zinc concentrate due to labor unrest in a major producing country during the second half of 1981.

The dispute has now been resolved, and a recovery in output of silver and lead, coupled with better demand conditions are the basis for an expected sharp recovery in the volume of metal exports in the post-shortfall period. Silver export unit values are expected to remain depressed during the two post-shortfall years, while both lead and zinc export unit values are expected to increase at an average annual rate of about 7 per cent. Aggregate earnings from metals, which declined by 26 per cent in 1981/82, are projected to increase at an annual rate of 17 per cent in the two post-shortfall years. A shortfall of SDR 6.4 million is estimated for the group as a whole.

j. Other exports

This category, consisting of diverse products such as cement, soap, organic compounds, wood products and light manufactures, accounted for 18 per cent of total exports in the shortfall year. The neighboring countries in the Central American region are the main markets for these exports. Earnings from this group declined by 18 per cent in the shortfall year due to depressed market conditions and the unsettled political situation in the region, as well as trade disputes which limited access to markets in Guatemala and Costa Rica. Earnings are projected to decline by a further 3 per cent in the first post-shortfall year and to recover by 6 per cent in the second, as demand conditions improve. The trade dispute between Honduras and Guatemala has now been resolved, and in September 1982, bilateral trade between Honduras and El Salvador was reopened after an interval of thirteen years.

4. Staff appraisal and proposed decision

The Honduran authorities are expected to request a purchase of SDR 23.1 million (equivalent to 45.3 per cent of quota) under the compensatory financing facility in respect of a shortfall of the same amount estimated for the year ended June 1982. The proposed purchase would raise Honduras' outstanding purchases under the facility to 91.0 per cent of quota.

In 1980, Honduras' current account deficit doubled from an average of about SDR 128 million in 1977-79 (8 per cent of GDP) to about SDR 243 million (12.5 per cent of GDP), and the overall balance moved from a surplus of SDR 18.3 million in 1979 to a deficit of SDR 46.1 million in 1980. In 1981 the current account deficit was reduced from 12.5 per cent of GDP to 11 per cent, but this improvement was more than offset by a large fall in net capital inflows as the overall deficit approximately doubled from SDR 46.1 million to SDR 91.3 million. The current account deficit is expected to rise from SDR 257 million in 1981 to SDR 295 million in 1982 because of a decline in export earnings and a sharp rise in net service payments. The overall deficit for 1982 is estimated to be SDR 96 million, slightly larger than for 1981. Gross international reserves at the end of 1982 are estimated to be SDR 104.5 million (equivalent to 6.5 weeks of imports). The staff considers that the balance of payments need of Honduras justifies the proposed purchase under the compensatory financing decision.

Export earnings in the shortfall year ended June 1982 were about one per cent below the average level of the two pre-shortfall years and 9 per cent less than the average export earnings projected for the two post-shortfall years. The shortfall of SDR 23.1 million in total exports is accounted for by shortfalls for beef (SDR 7.1 million), metals (SDR 6.4 million), sugar (SDR 3.3 million), tobacco (SDR 3.2 million), coffee (SDR 3.1 million) and other exports (SDR 6.3 million). Low volume due to a local pricing dispute between cattle breeders and meat packers was almost entirely responsible for the shortfall in beef, whereas lower volumes and prices contributed to the shortfall in earnings from metal exports; metal exports were adversely affected by the weakness of world demand, and reduced output of silver and lead because of a dispute between the Government and the mining company resulted in a sharp fall in export volume. The sugar shortfall was due to low prices and the imposition of import quotas by the United States, traditionally the sole outlet for Honduran sugar. The tobacco shortfall resulted from reduced output caused by plant disease. Total exports are expected to recover slowly by 4 per cent in 1982/83 and then more strongly by 11 per cent in 1983/84. The staff considers that the shortfall in export earnings, being related mainly to external factors and to unavoidable supply constraints, was largely attributable to factors beyond Honduras' control.

The staff also considers that Honduras has been cooperating with the Fund in efforts to find appropriate solutions for its balance of payments difficulties as evidenced by the adoption by Honduras of a financial program under a stand-by arrangement which is to be considered by the Executive Board concurrently with the request for a CF purchase. The request for a compensatory financing purchase is expected to include a statement that Honduras will cooperate with the Fund in efforts to find, where required, appropriate solutions for its balance of payments difficulties. The staff considers that the request meets all the requirements set forth in the compensatory financing decision. Accordingly, the following draft decision is proposed for adoption by the Executive Board after a duly authenticated request has been received:

1. The Fund has received a request from the Government of Honduras for a purchase of SDR 23.1 million under the Decision on Compensatory Financing of Export Fluctuations (Executive Board Decision No. 6224-(79/135), adopted August 2, 1979).

2. The Fund approves the purchase in accordance with the request.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Fund Relations with Honduras
(As of September 30, 1982)

Status:	Article VIII		
Quota:	SDR 51 million		
Fund holdings of Honduran lempiras:		Millions of SDRs	Per Cent of Quota
	Total	106.7	209.2
	Of which:		
	Credit tranches	(12.8)	(25.0)
	EFF	(19.6)	(38.5)
	CFF	(23.3)	(45.7)
SDR Department:		Millions of SDRs	Per Cent of Quota
	Net cumulative allocation	19.1	100.0
	Holdings	1.1	5.7
Trust Fund (second period):	Disbursed	SDR 14.1 million	
Gold distribution:	21,396 fine ounces		
Direct distribution of profits from gold sales:	US$4.0 million		
Exchange rate:	US$0.50 per lempira		
Last Article IV consultation:	May 1980, discussed by the Executive Board on August 4, 1980 (EBM/80/118).		
Resident representative and technical assistance:	In December 1981, a Fund staff member was assigned as resident representative in Honduras for a period of one year. In early April 1982, an expert from the Fund's fiscal panel completed a two-month assignment as advisor on tax policy and administration, and, in September another expert from the Fund's fiscal panel completed a two-week assignment as an advisor on customs tariff reform. Also in September, a CBD expert in bank supervision was assigned to the Central Bank for a period of one year.		