EXECUTIVE BOARD MEETING

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To: Members of the Executive Board

From: The Secretary

Subject: **Honduras—Second Reviews Under the Stand-By Arrangement and Arrangement Under the Standby Credit Facility, Requests for Augmentation and Rephasing of Access, and Modification of Performance Criteria—Debt Sustainability Analysis**

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Prepared By:	The staffs of the Fund and the International Development Association
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***The authorities have indicated that they consent to the Fund's publication of this paper.**

INTERNATIONAL MONETARY FUND

HONDURAS

May 26, 2020

SECOND REVIEWS UNDER THE STAND-BY ARRANGEMENT ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY, REQUESTS FOR AUGMENTATION AND REPHASING OF ACCESS, AND MODIFICATION OF PERFORMANCE CRITERIA—DEBT SUSTAINABILITY ANALYSIS

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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	Low
Granularity in the risk rating	Tool not applicable
Application of judgment	No

The Debt Sustainability Analysis (DSA) indicates that Honduras remains at low risk of debt distress both for public external debt and overall debt.[1,2] *Honduras' proven record of compliance with the Fiscal Responsibility Law (FRL) provides confidence that the response to the COVID-19 pandemic will not jeopardize debt sustainability. Going forward, continuous adherence to the FRL and institutional reforms to boost inclusive growth and increase the economy's potential are critical to recover quickly from the crisis and maintain debt sustainability.*

[1] This DSA updates the previous joint IMF/WB DSA prepared in July 2019 in the context of the Honduras Article IV staff report (IMF Country Report No. 19/236).

[2] Honduras's debt carrying capacity is assessed to be strong based on a composite indicator of 3.21 that uses the April and October 2019 WEO vintages and the 2018 CPIA.

BACKGROUND

1. Total public debt increased in 2019 due mainly to higher domestic borrowing.[3] Gross public debt stood at 43.1 percent of GDP at end-2019, up by 1.1 percentage points of GDP since 2018, of which 30.8 percentage points corresponded to external public and publicly guaranteed (PPG) debt and 12.3 percentage points to domestic debt (Text Table 1). Domestic debt explained most of the increase, reflecting in part the financial imbalances faced by the state-owned electricity company (ENEE).

2. PPG external debt has increased slightly since 2016. Following a US$700 million international bond issuance in 2017, the PPG external debt-to-GDP ratio increased to 30.8 percent in 2019. Total external debt reached 38.5 percent of GDP—up from 38.1 percent in 2018—mainly driven by an increase in private external debt of 0.4 percent of GDP. Private external debt has rebounded to the level shown five years ago.

Text Table 1. Honduras: PPG Debt Stock Composition by Level of Government

(End-of-year stock, in percent of GDP)

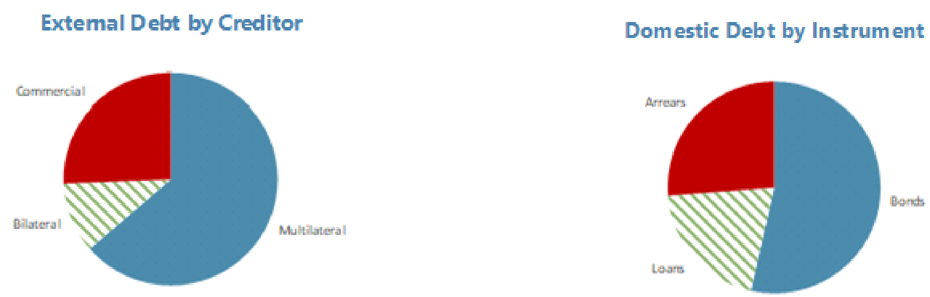
	2015	2016	2017	2018	2019
Domestic Debt					
Central government	8.1	8.9	7.4	8.4	9.2
Local governments	0.8	0.9	1.0	1.2	1.4
Nonfinancial public companies	2.1	1.9	1.2	1.7	1.7
Total	**11.0**	**11.7**	**9.6**	**11.3**	**12.3**
External Debt					
Central government	27.3	27.3	29.3	29.5	29.7
Local governments	0.0	0.0	0.0	0.0	0.0
Nonfinancial public companies	0.9	1.1	1.1	1.3	1.0
Total	**28.2**	**28.4**	**30.5**	**30.7**	**30.8**
Total Debt					
Central government	35.4	36.3	36.7	37.8	39.0
Local governments	0.8	0.9	1.0	1.2	1.4
Nonfinancial public companies	3.0	3.0	2.3	3.0	2.8
Total	**39.2**	**40.1**	**40.1**	**42.0**	**43.1**
Memorandum item					
Private External Debt	7.9	7.0	6.7	7.4	7.8

Source: Country authorities. Preliminary data for 2019.

[3] 2019 data used in this DSA is preliminary and subject to change.

3. Public debt is mostly held by foreign creditors (Text Figure 1). The share of PPG external debt stood at 71.4 percent of total public debt as of end 2019. The main creditors to Honduras are international bondholders, the Inter-American Development Bank (IDB), the Central American Bank for Economic Integration (CABEI), and the World Bank, which provide lending at long maturities, particularly in the case of the multilaterals. Public domestic debt is mainly held by commercial banks, has a shorter—though rising—maturity (over 4 years), and carries a higher real interest rate. In March 2018, the government placed a 15-year bond in the local market at a fixed interest rate of 11 percent raising 154 million Lempiras (around US$6 million). This reflects a broader strategy by the authorities to increase Lempiras-denominated debt with longer maturities, to be held increasingly by pension funds and other institutional investors.

Text Figure 1. Honduras: PPG Debt Stock Composition by Instrument



Source: Country authorities.

4. The debt coverage for the public sector is comprehensive. The DSA covers the nonfinancial public sector (NFPS). Therefore, it includes general government debt and non-financial state-owned enterprises' debt, both guaranteed and non guaranteed. Debt from extrabudgetary funds such as trust funds[4]—which are treated as private entities under Honduran legislation but should be registered as general goverment units according to the 2014 GFSM—are also included (Text Table 2).[5] Decentralized agencies such as public universities, among others, are included. Public pension funds debt and central bank debt borrowed on behalf of the government are also covered in the debt stock. Among debt for non-financial SOEs, in the case of ENEE, this includes arrears to energy generators. The contingent liability test includes lawsuits in international courts in the amount of 3.5 percent of GDP,[6] PPPs for 3 percent of GDP, and the default financial market shock (5 percent of GDP). Since the DSA coverage does not include public banks, an additional 2 percent of GDP is added to the contingent liability test. The DSA uses a currency-based definition of external debt—non-residents do not hold domestic debt, hence there is no material difference between the residency-based and the currency-based concepts. Whereby, lempiras-denominated debt is

[4] Only the trust fund "*Fondo de Protección y Seguridad Poblacional*" has contracted debt.

[5] Where complete details on the debt service for local governments and trust funds are not available, conservative, commercial bank financing assumptions are used.

[6] Disputed amounts reach 8.1 percent of GDP, but contingent liabilities are 3.5 percent after factoring lawsuit-specific probabilities of resolution according to estimations prepared by the Treasury's contingency unit.

considered public domestic debt and public foreign currency-denominated debt is accounted as public external debt.

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	3.5	It includes contingent liabilities for international lawsuits.
3 SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	2.0	It includes financial state-owned enterprises.
4 PPP	35	percent of PPP stock	3.0	
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)			13.5	

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%.

MACROECONOMIC AND POLICY ASSUMPTIONS

5. **The main macroeconomic assumptions are based on the authorities' policy targets and staff projections.** The medium-to long-term macroeconomic outlook assumes that the FRL is fulfilled and that structural reforms envisaged in the Fund-supported program are implemented, while accommodating the response to the COVID-19 shock this year. As a result, the baseline macroeconomic projections are revised compared to the last DSA update dated July 2019 (Text Table 3).

Text Table 3. Honduras: Selected Economic Indicators, Current vs Previous DSA

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2029	2039
Real GDP growth (percent)											
Current DSA	4.8	3.7	2.7	-3.3	4.7	4.2	3.9	3.9	3.9	4.0	4.0
Previous DSA	4.9	3.7	3.4	3.5	3.6	3.7	3.9	3.9	3.9	3.9	3.9
GDP deflator growth (percent)											
Current DSA	4.5	1.9	4.3	4.5	6.0	4.7	4.7	4.7	4.7	4.0	4.0
Previous DSA	4.3	1.8	3.2	3.4	3.2	3.5	3.6	3.7	3.8	4.1	4.0
Primary balance (% of GDP)											
Current DSA	0.1	0.0	0.2	-3.0	-1.5	0.4	0.2	0.0	0.5	0.5	0.5
Previous DSA	0.1	0.0	0.6	0.7	0.8	1.0	0.9	0.7	0.8	0.7	0.5
Current account balance (% of GDP)											
Current DSA	-0.8	-5.4	-1.4	-2.1	-2.5	-3.4	-3.9	-4.0	-4.0	-4.4	-4.4
Previous DSA	-1.8	-4.2	-4.2	-4.3	-4.2	-4.1	-3.9	-3.9	-3.9	-3.7	-3.2
Net FDI (% of GDP)											
Current DSA	4.5	3.7	2.0	1.4	2.5	2.7	3.0	3.5	4.1	4.1	4.1
Previous DSA	4.4	4.8	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9

Source: IMF staff estimates and projections.

- **Real sector.** In the short term, GDP growth downward revisions reflect the slowdown of 2019 and the expected hit of the COVID-19 shock in 2020. In particular, the economy is expected to be hit by negative external shocks through weaker export demand as economic conditions deteriorate in the main trade partners (WEO April 2020), lower remittances due to the record high unemployment levels in the U.S., and a sharp decline in tourism revenues. In addition, containment and mitigation measures are expected to remain in place until June. A recovery in economic activity is envisaged for the second half of the year, with a stronger rebound — above potential — in 2021. GDP growth converges around 4 percent in the long term, unchanged with respect to the previous DSA. Inflation is projected to stabilize at 4 percent, in line with the Central Bank's target, but the deflator over the next few years is affected by the oil price dynamics. Naturally, given the high uncertainty surrounding the pandemic, risks are tilted to the downside.

- **Fiscal variables.** Fiscal projections assume compliance with the FRL. The escape clause of the FRL was called for 2020 and 2021 on the grounds of emergency (Art. 4 of the FRL, item 1) leading to a NFPS deficit of 4 and 3 percent of GDP, respectively. A return to the deficit limit of 1 percent of GDP is assumed from 2022 onwards.

- **Debt issuance assumptions.** The share of external borrowing from multilateral and bilateral institutions is expected to grow in response to the COVID-19 shock. The deterioration in global market conditions raise risks about the rollover of the Eurobonds maturing this year, which will be nonetheless covered by concessional financing instead.[7] Rollover of Eurobonds maturing later on and increased commercial borrowing lead to a decline in concessionality over the long run. The projections also envisage that the authorities succeed in deepening the domestic debt market, increasing maturities and issuing predominantly at fixed rates. These assumptions are consistent with the Honduran Debt Management Strategy.

- **Debt service suspension initiative (DSSI).** The authorities are considering whether to request debt service suspension from official bilateral creditors as envisaged under the Debt Service Suspension Initiative, supported by the G-20 and Paris Club.[8]

- **External sector.** With respect to the previous DSA, an improvement of the current account is now expected over the next few years reflecting the drop in economic activity induced by the COVID-19 shock and the lower oil prices. However, this still represents a worsening of the current account deficit in 2020 with respect to 2019. The current account deficit would hover

[7] The World Bank accelerated preparation of a Disaster Risk Management development policy credit with a Deferred Drawdown Option (CAT-DDO) of US$119 million, with a Board approval on April 10, 2020; that credit is fully disbursed. The CAT-DDO is a contingent DPO support product linked to disaster risk response, and, as a result, represents a departure of the Bank's preference to use the Investment Project Financing (IPF) instrument in Honduras. The Bank also approved a US$20 million COVID-19 Fast Track Facility on April 15, 2020 aimed at the prevention, containment and response to the pandemic, and temporarily waived the school-attendance condition under the Social Protection Integration Project to ensure that eligible families continue receiving a transfer while schools remain closed to contain the spread of COVID-19. The WBG is currently working with the Government to determine the need to activate emergency components of existing projects (CERCs) of some of its operations and discussing Pandemic Emergency Financing Facility (PEF) allocation for US$1.3 million.

[8] Participation in the DSSI which provides a time-bound suspension of official bilateral debt service payments to IDA-eligible and least developed countries as defined by the UN would provide additional fiscal space in the near term.

around 4 percent of GDP over the long term. In the outer years, the current account deficit is still expected to be financed primarily by foreign direct investment.[9] FDI is expected to increase in critical economic sectors such as electricity as the authorities move forward with their reform agenda for the sector.

6. **The realism tools suggest that the projections are reasonable** (Figures 3 and 4).[10] The baseline assumes an improvement of the primary balance of 0.2 percentage points of GDP over the next three years, which falls around the median of the distribution for LICs. This improvement in the primary balance is warranted by compliance with the FRL, which serves as an anchor to guide fiscal sustainability, with the loosening of 2020 expected to be reverted promptly as the economy recovers and temporary measures expire. Compared to the previous DSA, both growth projections and the evolution of investment are similar, after excluding the COVID-19 shock. The projected contribution of the government's capital stock to growth remains very low, in line with historical levels. The growth path is consistent with reasonable levels for the fiscal multiplier, as it is mostly driven by the COVID-19 shock.

COUNTRY CLASSIFICATION AND STRESS TESTS

7. **Honduras debt carrying capacity is classified as strong.** Debt carrying capacity is determined by a composite indicator (CI) that includes the World Bank's Country Policy and Institutional Assessment (CPIA) score, world economic growth, and Honduras's real growth rate, import coverage of reserves, and remittances. Two consecutive signals are needed to modify the classification. For this DSA, the April and October 2019 WEO vintages and the 2018 CPIA are used. Both the current and previous vintages yield a rating of strong debt carrying capacity, leading to no changes with respect to the previous DSA (Text Table 4). A strong debt-carrying capacity implies higher thresholds for the stress tests (Text Table 5).

Text Table 4. Honduras: Debt Carrying Capacity Country Classification

Debt Carrying Capacity	Strong

Final	Classification based on current vintage	Classification based on the previous vintage	Classification under old methodology based on the two vintages preceding the last two ones
Strong	Strong	Strong	Strong
	3.21	3.22	3.21

Note: Until the April 2019 WEO vintage is released, the two previous vintages ago classification and corresponding score are based solely on the CPIA per the previous framework.

[9] The lower levels assumed for the long term reflect methodological changes that led to a revision of the estimates for 2018 and 2019.

[10] Realism tools are designed to encourage examination of baseline assumptions and cover (i) drivers of debt dynamics, (ii) realism of planned fiscal adjustment, (iii) fiscal adjustment-growth relationship, and (iv) public investment-growth relationship.

8. Honduras qualifies for several stress tests. All standard stress tests apply without any changes to the default settings. The calibration of the contingent liabilities stress test is as discussed in paragraph 4. In addition, Honduras qualifies for a natural disaster tailored shock due to its exposure to frequent natural catastrophes such as hurricanes and droughts that are being exacerbated by climate change. Honduras does not qualify for a commodity price shock. Honduras qualifies for the market financing shock because it has outstanding Eurobonds. The default settings for the tailored shocks are considered appropriate for Honduras.

Text Table 5. Honduras: Public and Publicly Guaranteed (PPG) External Debt Thresholds and Total Public Debt Benchmarks

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

EXTERNAL DSA

9. Honduras's risk of external debt distress is assessed to be low. The PV of PPG external debt-to-GDP ratio is projected to peak at 32 percent in 2020, below the 55 percent threshold (Table 3). The PPG external debt to exports and PPG external debt service-to-revenue also peak in 2020, well under their respective thresholds of 240 percent and 23 percent, respectively. The PPG external debt service-to-exports ratio reaches 13 percent in 2027, below the threshold of 21. Consequently, all solvency and liquidity indicators under the baseline scenario and under various stress tests remain below their respective thresholds (Figure 1). The peaks observed on debt service indicators are explained by the repayments of Eurobonds in 2027.

10. However, some debt indicators are sensitive to shocks. A negative shock to exports, equivalent to a one standard deviation decline in the nominal growth of exports in the second and third years of projection and a decline in real GDP growth, generates the largest increase in the PV of the PPG external debt-to-GDP ratio, leading to a peak of 43 percent in 2022 (Figure 1). Under the same shock, the PPG external debt-to-exports ratio would peak in 2023, reaching 158 percent (below the 240 percent threshold). Furthermore, the same shock would lead the PPG external debt-service-to-exports ratio to reach 20 percent in 2027. The most extreme shock for the PPG external debt-service-to-revenue ratio would be combined shock, under which the ratio would reach 19 in 2027. In both cases, the liquidity ratios remain below their risk thresholds.

PUBLIC DSA

11. Public debt ratios are expected to peak in 2020, and then decline over the medium term. Public debt is projected to peak at 51.6 percent of GDP in 2022 and start declining, supported by stable primary surpluses as well as declining interest payments, reaching 45.1 percent of GDP by 2030 (Table 4 and Figure 2). The FRL is the critical difference between baseline projections and the historical scenario, providing an anchor for a sound fiscal position. In present value terms, the debt-to-GDP ratio is expected to peak at 49 percent of GDP in 2022 and fall to 42 percent of GDP by 2030. Public debt dynamics remain vulnerable to contingent liabilities and exogenous shocks, especially to those related to natural disasters (Table 4). However, under no scenario does any of the indicators breach its benchmark.

12. Market-Financing Risk Indicators suggest low liquidity risks given that the authorities do not plan to access the international market (Figure 5). The maximum gross financing needs over a 3-year period under the baseline projection horizon in Honduras are expected to be around 9 percent of GDP, which is below the benchmark value of 14 percent. EMBI spreads have increased from 252 basis points at the beginning of the year to 550 basis points on May 14, slightly below the benchmark level of 570 basis points. However, that increase reflects a general trend of massive capital outflows from emerging economies that have taken place over the last few months, rather than a Honduras-specific financial constraint. As Honduras is not assumed to rollover its Eurobonds maturing this year, the country is relatively insulated from the general trend. In addition, the PV of debt relative to GDP and to exports, as well as the ratios of debt service to exports and to revenue, are all expected to remain below the thresholds under the baseline projection and under the market financing scenario. Nevertheless, given significant uncertainty regarding global financial conditions, a cautious debt management approach is warranted.

RISK RATING AND VULNERABILITIES

13. The DSA indicates that Honduras's risks of external debt and public total debt distress are low, supported by strict observance of the FRL, even when leveraging its escape clause to deal with a temporary negative shock. This risk rating is unchanged from the 2019 DSA. PPG external debt burden indicators remain below the thresholds under the baseline scenario and stress tests. Nonetheless, shocks associated to exports or natural disasters showcase existing debt vulnerabilities, implying that adhering consistently to the FRL is a key element to ensuring debt sustainability. The results also highlight the importance of raising domestic revenue, addressing structural vulnerabilities in SOEs, and leveraging concessional sources of financing when available.

Authorities' Views

14. Authorities agreed with this debt sustainability assessment. They noted that the temporary activation of the escape clause of the FRL would allow them to address the challenges raised by the pandemic, but they will swiftly return to the target of 1 percent NFPS deficit by 2022 as mandated by the law. They reiterated their commitment to preserving the revenue mobilization efforts while implementing reforms in SOEs to resolve their imbalances, and to the further development of the domestic debt market. The contingency unit at SEFIN will continue addressing data limitations with the goal of improving the management of fiscal risks.

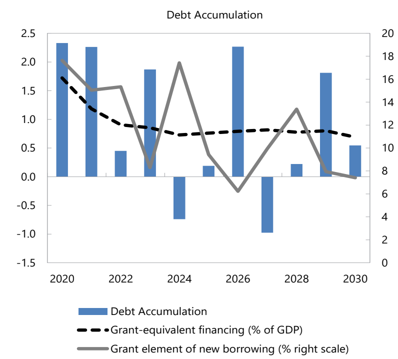
Table 1. Honduras: External Debt Sustainability Framework, Baseline Scenario, 2017-40

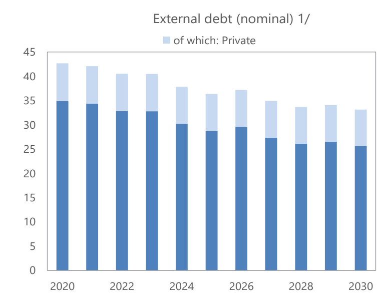
(In percent of GDP, unless otherwise indicated)

(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030	2040	Historical	Projections
External debt (nominal) 1/	37.2	38.1	38.5	42.7	42.1	40.5	40.5	37.9	36.4	33.1	22.5	33.3	37.5
of which: public and publicly guaranteed (PPG)	30.5	30.7	30.8	34.9	34.3	32.8	32.8	30.2	28.7	25.6	15.0	25.9	29.9
Change in external debt	1.8	0.9	0.4	4.1	-0.6	-1.6	-0.1	-2.6	-1.5	-0.9	-1.1		
Identified net debt-creating flows	-5.9	0.3	-2.1	2.0	-1.8	-1.0	-0.6	-1.0	-1.5	-0.9	-0.7	-1.1	-0.8
Non-interest current account deficit	-0.5	4.0	0.2	0.8	1.1	2.0	2.5	2.6	2.6	3.2	3.5	4.4	2.4
Deficit in balance of goods and services	14.8	19.1	17.4	16.3	15.7	16.3	16.7	17.0	17.2	17.4	17.5	17.7	16.9
Exports	43.5	41.6	39.7	34.1	34.9	34.4	34.2	34.2	34.3	34.3	34.3		
Imports	58.2	60.7	57.1	50.4	50.7	50.7	50.9	51.2	51.4	51.7	51.8		
Net current transfers (negative = inflow)	-20.1	-21.6	-23.7	-20.3	-20.4	-20.1	-19.9	-20.0	-20.2	-20.2	-20.2	-19.3	-20.2
of which: official	-0.3	-1.3	-1.5	-1.2	-1.2	-1.2	-1.2	-1.2	-1.3	-1.3	-1.3		
Other current account flows (negative = net inflow)	4.8	6.5	6.5	4.7	5.8	5.7	5.8	5.6	5.6	6.0	6.1	6.0	5.7
Net FDI (negative = inflow)	-4.5	-3.7	-2.0	-1.4	-2.5	-2.7	-3.0	-3.5	-4.1	-4.1	-4.1	-4.7	-3.4
Endogenous debt dynamics 2/	-0.9	0.0	-0.3	2.6	-0.4	-0.2	-0.1	0.0	0.0	0.0	0.0		
Contribution from nominal interest rate	1.3	1.4	1.1	1.3	1.4	1.4	1.4	1.5	1.4	1.3	0.8		
Contribution from real GDP growth	-1.6	-1.3	-1.0	1.3	-1.8	-1.6	-1.5	-1.5	-1.4	-1.3	-0.9		
Contribution from price and exchange rate changes	-0.6	0.0	-0.5	...	...	...	...	...	...	...	...		
Residual 3/	7.7	0.7	2.5	2.1	1.2	-0.6	0.6	-1.7	0.0	0.0	-0.4	2.6	0.3
of which: exceptional financing	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	...	...	29.0	31.7	31.4	29.7	29.7	27.2	25.7	22.6	12.9		
PV of PPG external debt-to-exports ratio	...	...	73.0	93.0	89.9	86.3	86.7	79.4	75.0	66.0	37.6		
PPG debt service-to-exports ratio	9.1	9.6	10.4	12.5	6.8	8.6	8.5	8.6	9.0	6.9	5.2		
PPG debt service-to-revenue ratio	13.4	13.7	14.1	15.7	8.4	10.1	9.8	10.0	10.3	7.8	5.8		
Gross external financing need (Billion of U.S. dollars)	1.5	2.7	2.5	2.7	2.0	2.5	2.6	2.5	2.4	2.7	3.5		
Key macroeconomic assumptions													
Real GDP growth (in percent)	4.8	3.7	2.7	-3.3	4.7	4.2	3.9	3.9	3.9	4.0	4.0	3.6	3.4
GDP deflator in US dollar terms (change in percent)	1.6	0.0	1.2	2.0	3.5	2.9	2.4	2.4	2.4	1.7	1.7	1.8	2.2
Effective interest rate (percent) 4/	3.9	3.9	3.1	3.4	3.6	3.6	3.7	3.9	4.0	3.9	3.8	2.7	3.8
Growth of exports of G&S (US dollar terms, in percent)	8.9	-0.7	-0.9	-15.2	10.8	5.6	5.8	6.5	6.6	5.8	5.8	6.0	4.5
Growth of imports of G&S (US dollar terms, in percent)	9.6	8.2	-2.3	-12.8	8.7	7.4	6.7	7.2	6.9	5.8	5.8	5.9	4.9
Grant element of new public sector borrowing (in percent)	...	...	...	17.6	15.0	15.3	8.3	17.4	9.4	7.4	3.1	...	11.6
Government revenues (excluding grants, in percent of GDP)	29.7	29.1	29.3	27.1	28.3	29.4	29.6	29.6	29.8	30.4	30.9	28.4	29.5
Aid flows (in Billion of US dollars) 5/	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3	0.4		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	1.7	1.2	0.9	0.9	0.7	0.8	0.7	0.6	...	0.9
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	25.0	28.4	32.3	20.9	47.8	28.4	30.1	41.9	...	28.7
Nominal GDP (Billion of US dollars)	23	24	25	25	27	29	30	32	34	46	80		
Nominal dollar GDP growth	6.6	3.7	3.9	-1.3	8.3	7.2	6.4	6.5	6.4	5.8	5.8	5.5	5.7
Memorandum items:													
PV of external debt 7/	...	...	36.7	39.5	39.1	37.4	37.3	34.8	33.3	30.2	20.3		
In percent of exports	...	...	92.5	115.7	112.0	108.7	109.2	101.8	97.3	88.0	59.3		
Total external debt service-to-exports ratio	26.6	26.2	29.7	33.5	25.7	27.4	26.1	25.1	25.0	20.0	14.5		
PV of PPG external debt (in Billion of US dollars)			7.2	7.8	8.4	8.5	9.0	8.8	8.8	10.3	10.3		
(PVt-PVt-1)/GDPt-1 (in percent)				2.3	2.3	0.5	1.9	-0.7	0.2	0.5	-0.2		
Non-interest current account deficit that stabilizes debt ratio	-2.4	3.0	-0.2	-3.3	1.7	3.5	2.6	5.2	4.1	4.1	4.6		

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.

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.

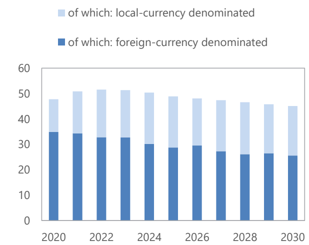
Table 2. Honduras: Public Debt Sustainability Framework, Baseline Scenario, 2017-40

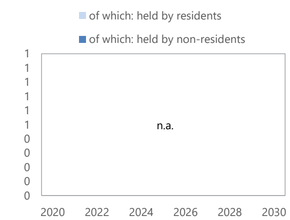
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030	2040	Historical	Projections
Public sector debt 1/	40.0	41.8	43.1	47.8	50.9	51.6	51.4	50.4	48.9	45.1	38.9	36.2	48.5
of which: external debt	30.5	30.7	30.8	34.9	34.3	32.8	32.8	30.2	28.7	25.6	15.0	25.9	29.9
Change in public sector debt	-0.1	1.8	1.3	4.6	3.1	0.7	-0.2	-1.0	-1.5	-0.7	-0.6		
Identified debt-creating flows	-1.6	0.5	-1.7	3.8	2.1	0.1	-0.9	-1.6	-2.2	-0.7	-0.6	1.4	-0.2
Primary deficit	-0.1	0.0	-0.2	3.0	1.5	-0.4	-0.2	0.0	-0.5	-0.5	-0.5	2.1	0.1
Revenue and grants	30.3	29.8	29.9	27.7	29.0	29.9	30.2	30.2	30.3	30.9	31.5	29.3	30.1
of which: grants	0.6	0.7	0.7	0.6	0.7	0.6	0.6	0.6	0.6	0.6	0.6		
Primary (noninterest) expenditure	30.2	29.8	29.8	30.7	30.5	29.6	29.9	30.2	29.8	30.4	31.0	31.4	30.2
Automatic debt dynamics	-1.1	1.0	-1.1	3.0	-1.8	-0.8	-0.6	-0.5	-0.4	-0.1	-0.1		
Contribution from interest rate/growth differential	-0.5	-0.1	-0.9	3.1	-0.9	-0.7	-0.5	-0.3	-0.3	-0.2	-0.1		
of which: contribution from average real interest rate	1.3	1.3	0.2	1.6	1.2	1.4	1.5	1.6	1.6	1.6	1.4		
of which: contribution from real GDP growth	-1.9	-1.4	-1.1	1.4	-2.1	-2.1	-2.0	-1.9	-1.9	-1.8	-1.5		
Contribution from real exchange rate depreciation	-0.6	1.1	-0.2	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	-0.4	-0.4	-0.4	-2.2	2.4	1.2	0.0	-1.2	-1.3	-0.1	0.0	-0.3	-0.2
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	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3	-0.1	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	-1.8	2.8	1.5	0.2	-0.9	-1.0	0.0	0.0		
Residual	1.5	1.3	3.0	0.8	0.1	0.5	0.5	0.5	0.5	0.1	0.0	0.5	0.3
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	41.5	45.2	48.1	48.8	48.6	47.7	46.1	42.4	36.9		
PV of public debt-to-revenue and grants ratio	...	...	138.5	162.9	166.2	163.1	161.0	158.1	152.2	137.0	117.2		
Debt service-to-revenue and grants ratio 3/	11.0	10.8	13.8	29.8	18.6	26.2	29.6	30.3	32.8	30.3	31.9		
Gross financing need 4/	2.9	2.8	3.6	9.1	9.3	8.7	8.7	8.0	8.2	8.8	9.5		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	4.8	3.7	2.7	-3.3	4.7	4.2	3.9	3.9	3.9	4.0	4.0	3.6	3.4
Average nominal interest rate on external debt (in percent)	3.5	3.4	3.6	4.0	4.2	4.2	4.3	4.6	4.7	4.7	5.0	2.8	4.5
Average real interest rate on domestic debt (in percent)	7.9	11.0	-3.6	4.2	3.7	4.4	4.3	4.6	4.5	4.8	4.2	3.7	4.6
Real exchange rate depreciation (in percent, + indicates depreciation)	-2.2	3.8	-0.7	...	...	...	...	...	...	...	...	0.0	...
Inflation rate (GDP deflator, in percent)	4.5	2.5	3.8	4.5	6.0	4.7	4.7	4.7	4.7	4.0	4.0	4.5	4.5
Growth of real primary spending (deflated by GDP deflator, in percent)	5.3	2.3	2.6	-0.3	3.8	1.1	5.3	4.7	2.8	4.3	4.1	2.7	3.6
Primary deficit that stabilizes the debt-to-GDP ratio 5/	0.0	-1.8	-1.5	-1.7	-1.6	-1.1	0.0	1.0	1.0	0.2	0.1	-1.1	-0.1
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.

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.

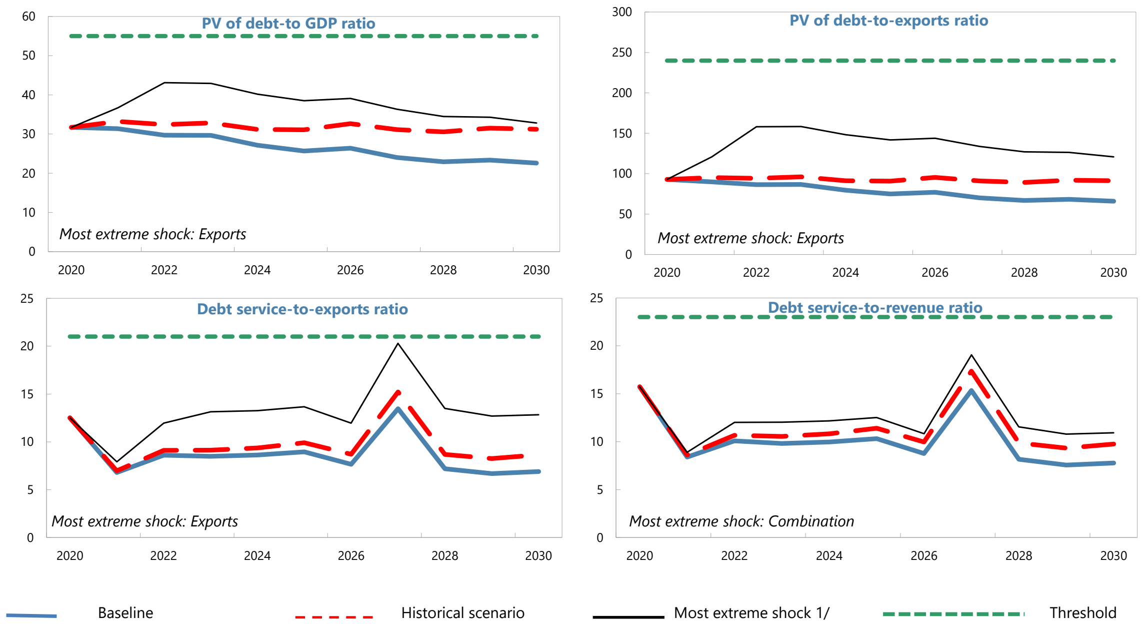
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

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.

Figure 1. Honduras: Indicators of Public and Publicly Guaranteed External Debt under Alternative Scenarios, 2020-30



Customization of Default Settings		
	Size	Interactions
Tailored Stress		
Combined CL	Yes	
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.

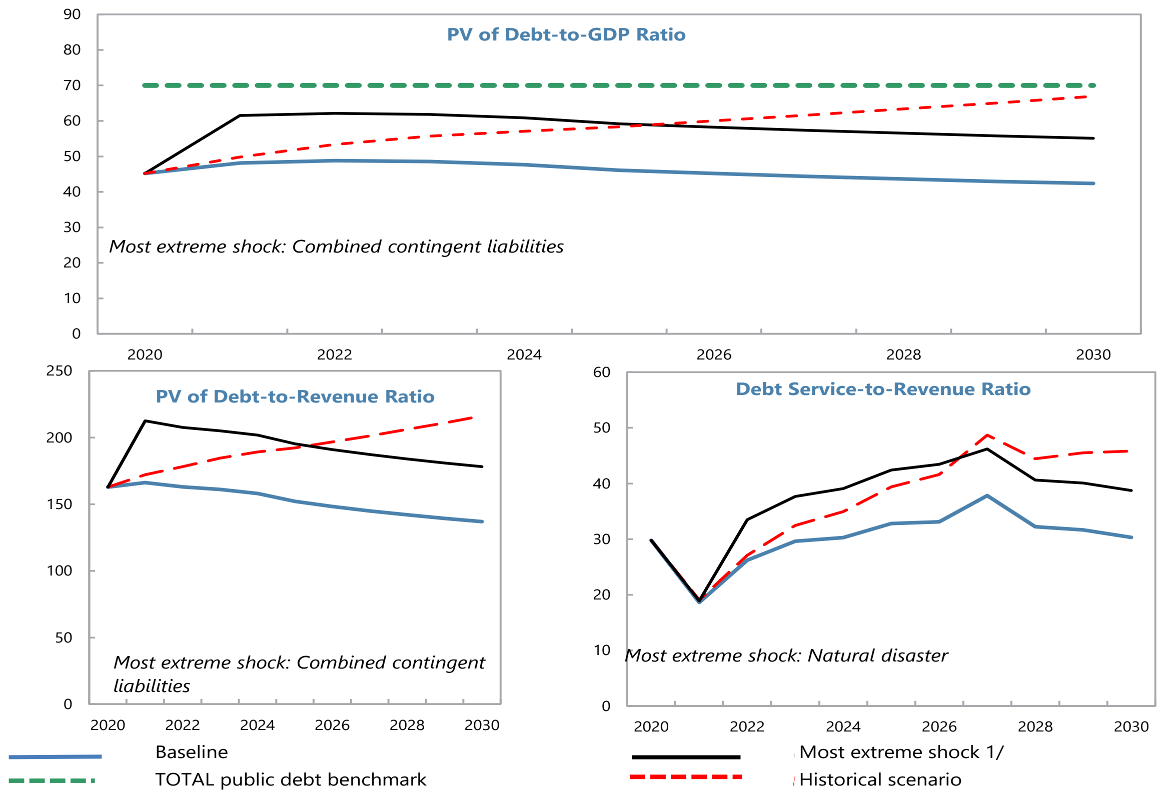
Borrowing assumptions on additional financing needs resulting from the stress tests*		
	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	4.8%	4.8%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	20	20
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 2030. 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, 2020-30



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	30%	30%
Domestic medium and long-term	70%	70%
Domestic short-term	0%	0%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	4.8%	4.8%
Avg. maturity (incl. grace period)	20	20
Avg. grace period	5	5
Domestic MLT debt		
Avg. real interest rate on new borrowing	4.1%	4.1%
Avg. maturity (incl. grace period)	5	5
Avg. grace period	0	0
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 2030. 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.

Table 3. Honduras: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2020-30

(In percent)

	Projections 1/										
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
PV of debt-to GDP ratio											
Baseline	32	31	30	30	27	26	26	24	23	23	23
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	32	33	32	33	31	31	33	31	31	32	31
B. Bound Tests											
B1. Real GDP growth	32	32	31	31	28	27	28	25	24	24	24
B2. Primary balance	32	32	33	33	31	30	31	29	28	29	28
B3. Exports	32	37	43	43	40	38	39	36	34	34	33
B4. Other flows 3/	32	36	38	38	35	34	34	32	30	30	29
B5. Depreciation	32	39	31	31	28	26	27	24	23	24	23
B6. Combination of B1-B5	32	41	41	41	38	36	37	34	33	33	31
C. Tailored Tests											
C1. Combined contingent liabilities	32	35	34	35	33	32	33	31	31	31	31
C2. Natural disaster	32	35	34	34	32	32	33	31	30	31	31
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	32	35	33	33	30	29	30	27	26	26	25
Threshold	55	55	55	55	55	55	55	55	55	55	55
PV of debt-to-exports ratio											
Baseline	93	90	86	87	79	75	77	70	67	68	66
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	93	95	94	96	91	91	95	91	89	92	91
B. Bound Tests											
B1. Real GDP growth	93	90	86	87	79	75	77	70	67	68	66
B2. Primary balance	93	93	96	98	91	88	91	85	82	83	81
B3. Exports	93	121	158	158	148	142	144	134	127	126	121
B4. Other flows 3/	93	102	110	111	103	98	100	92	88	88	84
B5. Depreciation	93	90	72	72	65	61	63	56	54	56	55
B6. Combination of B1-B5	93	121	111	129	120	115	117	107	102	102	98
C. Tailored Tests											
C1. Combined contingent liabilities	93	101	99	102	96	93	97	91	89	91	90
C2. Natural disaster	93	102	100	102	96	94	98	92	90	93	92
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	93	90	86	87	80	75	78	71	68	69	66
Threshold	240	240	240	240	240	240	240	240	240	240	240
Debt service-to-exports ratio											
Baseline	13	7	9	8	9	9	8	13	7	7	7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	13	7	9	9	9	10	9	15	9	8	9
B. Bound Tests											
B1. Real GDP growth	13	7	9	8	9	9	8	13	7	7	7
B2. Primary balance	13	7	9	9	9	10	8	14	8	8	8
B3. Exports	13	8	12	13	13	14	12	20	13	13	13
B4. Other flows 3/	13	7	9	10	10	10	9	15	9	9	9
B5. Depreciation	13	7	9	8	8	8	7	13	6	5	6
B6. Combination of B1-B5	13	7	11	11	11	12	10	18	11	10	10
C. Tailored Tests											
C1. Combined contingent liabilities	13	7	9	9	9	10	8	14	8	8	8
C2. Natural disaster	13	7	9	9	9	10	9	15	8	8	8
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	13	7	9	9	9	9	8	14	11	7	7
Threshold	21	21	21	21	21	21	21	21	21	21	21
Debt service-to-revenue ratio											
Baseline	16	8	10	10	10	10	9	15	8	8	8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	16	9	11	11	11	11	10	17	10	9	10
B. Bound Tests											
B1. Real GDP growth	16	9	11	10	10	11	9	16	9	8	8
B2. Primary balance	16	8	10	11	11	11	10	16	9	9	9
B3. Exports	16	9	11	12	12	12	11	18	12	11	11
B4. Other flows 3/	16	8	11	11	11	12	10	17	11	10	10
B5. Depreciation	16	11	13	11	12	12	10	18	8	8	8
B6. Combination of B1-B5	16	9	12	12	12	13	11	19	12	11	11
C. Tailored Tests											
C1. Combined contingent liabilities	16	8	11	11	11	11	10	16	9	9	9
C2. Natural disaster	16	8	11	10	11	11	10	16	9	9	9
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	16	8	10	10	10	11	10	16	12	7	8
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, 2020-30

	Projections 1/										
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
PV of Debt-to-GDP Ratio											
Baseline	45	48	49	49	48	46	45	44	44	43	42
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	45	50	53	56	57	58	60	62	63	65	67
B. Bound Tests											
B1. Real GDP growth	45	50	53	54	54	54	55	55	56	56	57
B2. Primary balance	45	51	58	58	57	55	54	53	53	52	51
B3. Exports	45	53	61	61	60	58	57	56	55	53	52
B4. Other flows 3/	45	52	57	57	56	54	53	52	51	50	49
B5. Depreciation	45	54	52	49	46	43	39	36	33	31	28
B6. Combination of B1-B5	45	49	54	53	52	50	49	48	46	45	44
C. Tailored Tests											
C1. Combined contingent liabilities	45	62	62	62	61	59	58	57	57	56	55
C2. Natural disaster	45	59	60	60	60	59	58	58	57	57	57
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	45	48	49	49	48	46	45	45	44	43	42
TOTAL public debt benchmark	70	70	70	70	70	70	70	70	70	70	70
PV of Debt-to-Revenue Ratio											
Baseline	163	166	163	161	158	152	148	145	142	139	137
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	163	172	178	185	189	192	197	201	206	211	216
B. Bound Tests											
B1. Real GDP growth	163	173	177	179	181	179	179	179	181	182	184
B2. Primary balance	163	177	194	191	188	182	178	175	171	168	166
B3. Exports	163	183	205	202	199	192	187	183	178	172	168
B4. Other flows 3/	163	181	191	188	185	179	174	170	165	161	157
B5. Depreciation	163	187	174	164	154	141	129	119	109	99	90
B6. Combination of B1-B5	163	168	180	176	172	165	160	156	151	147	143
C. Tailored Tests											
C1. Combined contingent liabilities	163	213	208	205	202	195	191	187	184	181	178
C2. Natural disaster	163	204	201	200	198	193	190	188	186	184	183
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	163	166	163	161	158	153	149	146	143	140	137
Debt Service-to-Revenue Ratio											
Baseline	30	19	26	30	30	33	33	38	32	32	30
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2020-2030 2/	30	19	27	32	35	39	42	49	44	46	46
B. Bound Tests											
B1. Real GDP growth	30	19	28	32	34	38	39	45	40	40	40
B2. Primary balance	30	19	29	36	37	40	40	45	38	38	36
B3. Exports	30	19	27	32	32	35	35	40	36	35	34
B4. Other flows 3/	30	19	27	31	32	34	34	40	35	34	33
B5. Depreciation	30	19	28	30	30	33	32	38	31	29	27
B6. Combination of B1-B5	30	18	27	33	33	35	35	40	33	32	31
C. Tailored Tests											
C1. Combined contingent liabilities	30	19	35	39	40	43	44	46	40	39	38
C2. Natural disaster	30	19	33	38	39	42	43	46	41	40	39
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	30	19	26	30	31	33	34	39	36	31	30

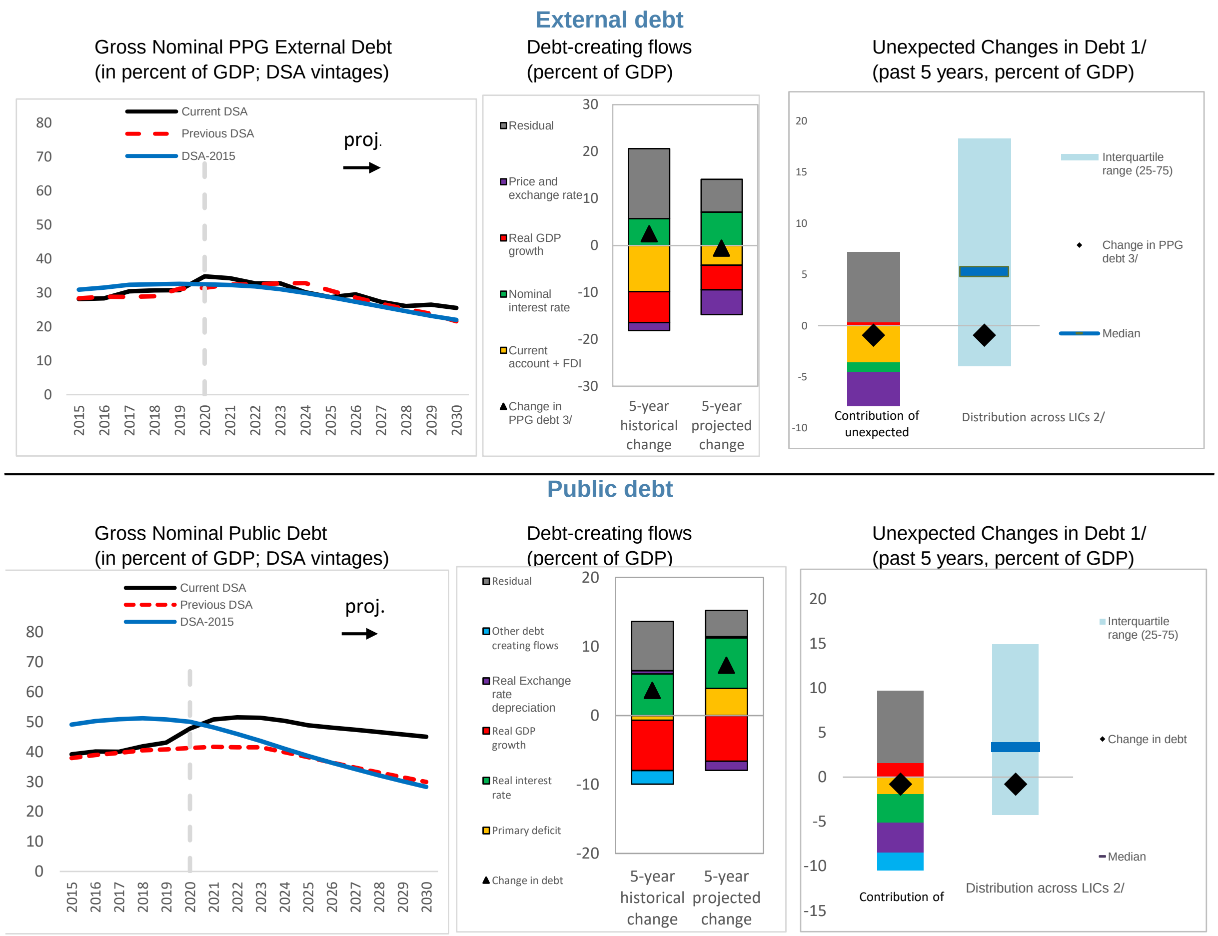
Sources: Country authorities; and staff estimates and projections.

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 3. Honduras: Drivers of Debt Dynamics – Baseline Scenario



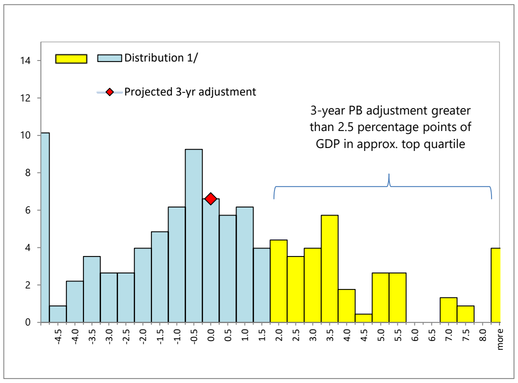
1/ Difference between anticipated and actual contributions on debt ratios.

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.

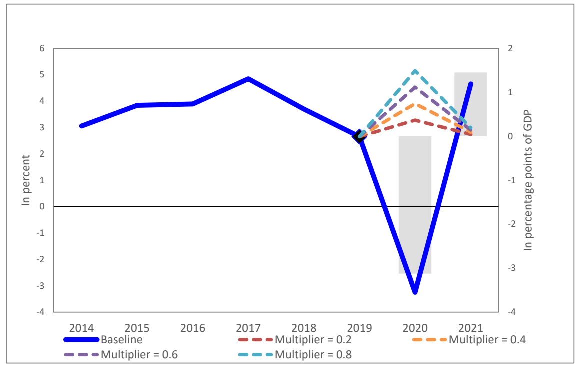
Figure 4. Honduras: Realism Tools

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



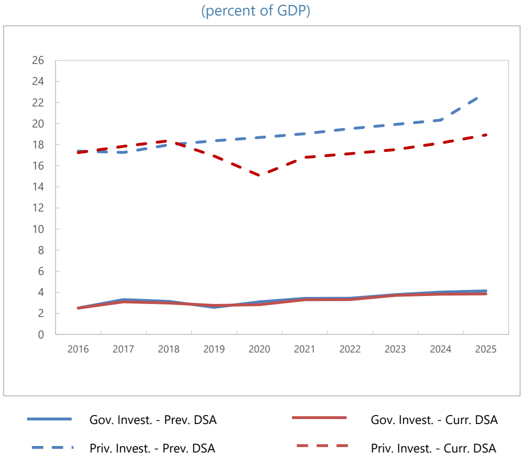
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

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)

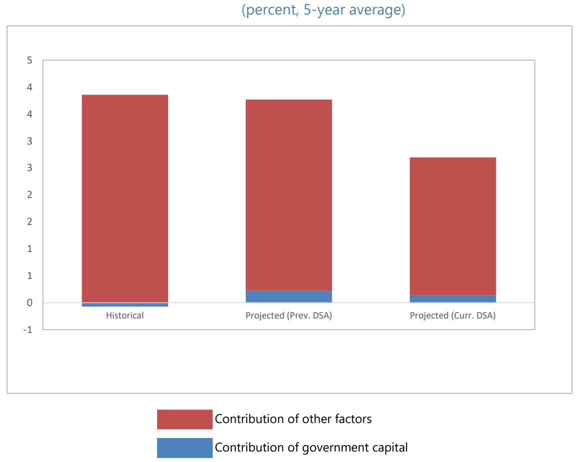
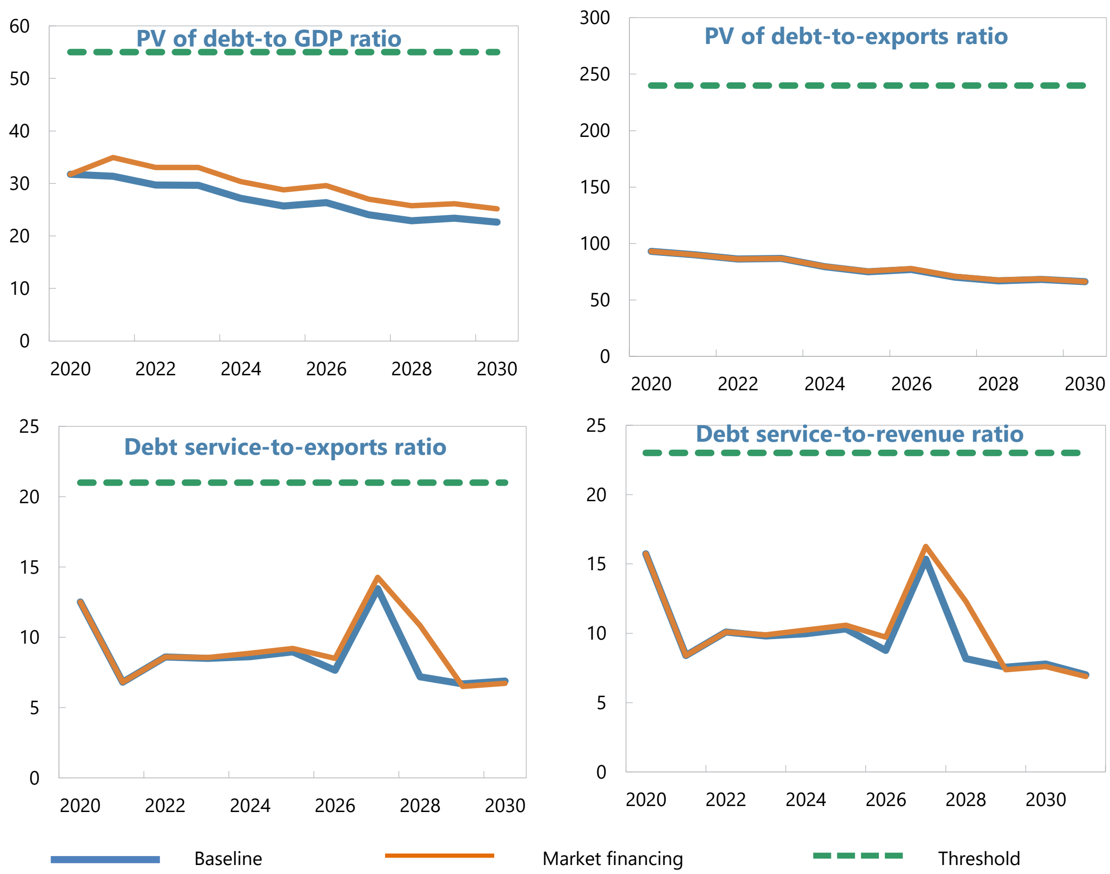


Figure 5. Honduras: Market-Financing Risk Indicators

	GFN	1/	EMBI	2/
Benchmarks	14		570	
Values	9		550	
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.