

**Document of  
The World Bank**

Report No: ICR2224

**IMPLEMENTATION COMPLETION AND RESULTS REPORT  
(Loan No.3800 - HO)**

**ON A**

**CREDIT**

**IN THE AMOUNT OF SDR 7,200,000 EQUIVALENT**

**TO THE**

**REPUBLIC OF HONDURAS**

**FOR A**

**FINANCIAL SECTOR TECHNICAL ASSISTANCE CREDIT**

Finance and Private Sector Development  
Caribbean Country Management Unit  
Latin America & the Caribbean Region

**CURRENCY EQUIVALENTS**  
 (Exchange Rate Effective June, 2013)  
 Currency Unit = Lempiras (Lps.)  
 1 Lempira = US\$ 0.05  
 US\$1 = 20.29 Lps.

**FISCAL YEAR**  
 July 1 to June 30

**ABBREVIATIONS AND ACRONYMS**

ACH	Automated Clearing House
AML	Anti-Money Laundering
BAC	<i>Banco BAC</i>
BCH	Honduras Central Bank (Banco Central de Honduras)
BCP	Basel Core Principles
BCV	Central American Stock Exchange (Bolsa Centroamericana de Valores)
BGA	<i>Banco Grupo El Ahorro</i>
CAR	Capital Adequacy Ratio
CAS	Country Assistance Strategy
CD	Central Depository
CEPROBAN	Bank Processing Center (Centro de Procesamiento Bancario)
CFT	Combating Financing of Terrorism
CIC	Credit Information System (Central de Informacion Crediticia)
CNBS	National Banking and Insurance Commission (Comisión Nacional de Bancos y Seguros)
CPSS	Committee on Payment and Settlement Systems
CSD	Central Securities Depository
DO	Development Objective
DVP	Delivery-versus-Payment
FIU	Financial Intelligence Unit
FOGADE	Deposit Guarantee Fund (Fondo de Garantía de Depósitos)
FSDPC	Financial Sector Development Policy Credit
FOSEDE	Deposit Insurance Fund (Fondo de Seguro de Depósitos)
FSPC	Financial Sector Policy Committee
FSTAC	Financial Sector Technical Assistance Credit
FSAP	Financial Sector Assessment Program
GAFI	<i>Grupo Acción Financiera</i>
GDP	Gross Domestic Product
HIPC	Heavily Indebted Poor Countries
IADB	Inter-American Development Bank
ICR	Implementation Completion and Results Report
IDA	International Development Association
IMF	International Monetary Fund
IP	Implementation Plan

ISR	Implementation Status Report
JPHRD	Japan Policy and Human Resources Development Fund
LBTR	<i>Liquidación Bruta en Tiempo Real</i>
LISF	Financial System Institutions Law (Ley de Instituciones del Sistema Financiero)
LSF	Financial System Law (Ley del Sistema Financiero)
NPL	Non Performing Loans
OPD	Operations and Policy Department (WB)
OPDF	<i>Organizaciones Privadas de Desarrollo Financiero</i>
PAD	Project Appraisal Document
PCU	Project Coordination Unit
PDO	Project Development Objective
PIU	Project Implementation Unit
PRGF	Poverty Reduction and Growth Facility
ROA	Return on Assets
ROE	Return on Equity
RTGS	Real Time Gross Settlement
SDR	Special Drawing Rights
SENDI	Electronic Foreign Exchange Trading System (Sistema Electronico de Negociacion de Divisas)
SIGEF	Economic and Financial Management and Information System (Sistema de Información y Gestión Económica y Financiera)
SGPS	Supervision Management System (Sistema para Gestión del Proceso de Supervisión)
SML	Securities Market Law
SRA	Supervisory Risk Assessment
TA	Technical Assistance
TAL	Technical Assistance Loan
TTL	Task Team Leader

Vice President:	Hasan Tuluy
Country Director:	Carlos Felipe Jaramillo
Sector Manager:	P.S. Srinivas
Task Team Leader:	Juan Buchenau
ICR Team Leader:	Juan Buchenau
ICR Author:	Fernando Montes-Negret <sup>1</sup>

<sup>1</sup> The author would like to express his gratitude to the staff of the BCH, CNBS and the PCU, as well as to private sector financial institutions and associations, for their cooperation and assistance during his visit to Tegucigalpa. The author also wants to thank Nicolas Montes-Betancourt for his valuable comments.



# REPUBLIC OF HONDURAS

## FINANCIAL SECTOR TECHNICAL ASSISTANCE LOAN

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## Data Sheet

<b>A. Basic Information</b>			
Country:	Honduras	Project Name:	Financial Sector Technical Assistance Credit
Project ID:	P040177	L/C/TF Number(s):	IDA-38000
ICR Date:	08/28/2013	ICR Type:	Core ICR
Lending Instrument:	TAL	Borrower:	REPUBLIC OF HONDURAS
Original Total Commitment:	XDR 7.20M	Disbursed Amount:	XDR 7.12M
Revised Amount:	XDR 7.12M		
<b>Environmental Category: C</b>			
<b>Implementing Agencies:</b> Comision Nacional de Bancos y Seguros Banco Central de Honduras			
<b>Cofinanciers and Other External Partners:</b>			

<b>B. Key Dates</b>				
Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	04/21/2003	Effectiveness:	03/15/2004	03/15/2004
Appraisal:	05/19/2003	Restructuring(s):		04/27/2007 04/07/2009 11/29/2010
Approval:	06/24/2003	Mid-term Review:		
		Closing:	09/30/2007	02/28/2013

<b>C. Ratings Summary</b>	
<b>C.1 Performance Rating by ICR</b>	
Outcomes:	Moderately Satisfactory
Risk to Development Outcome:	Moderate
Bank Performance:	Moderately Satisfactory
Borrower Performance:	Moderately Unsatisfactory

<b>C.2 Detailed Ratings of Bank and Borrower Performance (by ICR)</b>			
<b>Bank</b>	<b>Ratings</b>	<b>Borrower</b>	<b>Ratings</b>
Quality at Entry:	Moderately Satisfactory	Government:	Moderately Unsatisfactory
Quality of Supervision:	Moderately Satisfactory	Implementing Agency/Agencies:	Moderately Satisfactory
<b>Overall Bank Performance:</b>	Moderately Satisfactory	<b>Overall Borrower Performance:</b>	Moderately Unsatisfactory

<b>C.3 Quality at Entry and Implementation Performance Indicators</b>			
<b>Implementation Performance</b>	<b>Indicators</b>	<b>QAG Assessments (if any)</b>	<b>Rating</b>
Potential Problem Project at any time (Yes/No):	Yes	Quality at Entry (QEA):	None
Problem Project at any time (Yes/No):	Yes	Quality of Supervision (QSA):	None
DO rating before Closing/Inactive status:	Satisfactory		

<b>D. Sector and Theme Codes</b>		
	<b>Original</b>	<b>Actual</b>
<b>Sector Code (as % of total Bank financing)</b>		
Banking	70	33
Law and justice	5	7
Payments, settlements, and remittance systems	25	60
<b>Theme Code (as % of total Bank financing)</b>		
International financial architecture	11	5
International financial standards and systems	22	15
Legal institutions for a market economy	22	60
Regulation and competition policy	23	20
State-owned enterprise restructuring and privatization	22	



<b>E. Bank Staff</b>		
<b>Positions</b>	<b>At ICR</b>	<b>At Approval</b>
Vice President:	Hasan A. Tuluy	David de Ferranti
Country Director:	Carlos Felipe Jaramillo	Jane Armitage
Sector Manager:	Subrahmanya Pulle Srinivas	Fernando Montes-Negret
Project Team Leader:	Juan Buchenau Hoth	Modibo Khane Camara
ICR Team Leader:	Juan Buchenau Hoth	
ICR Primary Author:	Fernando Montes-Negret	

## **F. Results Framework Analysis**

### **Project Development Objectives (from Project Appraisal Document)**

The objective of the Project is to assist the Borrower to develop the institutional capacity it requires to be able to address the systemic vulnerabilities of its financial system, through: (a) the design and implementation of a banking sector consolidation program; (b) the reform of the Borrower's payment system; and (c) the improvement of selected aspects of the Borrower's financial system infrastructure.

### **Revised Project Development Objectives (as approved by original approving authority)**

#### **(a) PDO Indicator(s)**

<b>Indicator</b>	<b>Baseline Value</b>	<b>Original Target Values (from approval documents)</b>	<b>Formally Revised Target Values</b>	<b>Actual Value Achieved at Completion or Target Years</b>
<b>Indicator 1 :</b>	<b>Compliance of all systemically important banks with CNBS's prudential regulations, including capital adequacy norms that are aligned with international standards.</b>			
Value quantitative or Qualitative)	All banks comply with CNBS's prudential regulations, however these regulations are not always consistent with international standards.	All banks comply with CNBS's prudential regulations, which are consistent with international standards.		According to CNBS, all banks comply with its prudential regulations, which are consistent with international standards.
Date achieved	12/31/2004	02/28/2013		06/30/2012
Comments (incl. % achievement)	Achieved. Compliance with international standards to be assessed in next FSAP Update.			
<b>Indicator 2 :</b>	<b>Improved risk management by the banking sector and increased cost efficiency.</b>			
Value quantitative or Qualitative)	NPL ratio = 8.7% Admin Expenses / Assets = 6.4	NPL ratio N/A Admin Expenses / Assets = 5.0		NPL ratio = 2.3% Admin expenses/ Assets= 8.49%

Date achieved	12/31/2005	02/28/2013		12/31/2012
Comments (incl. % achievement)	Largely achieved. Risk management practices in banking sector significantly improved. NPL ratio at only 2.2% in December 2012. The near systemic banking crisis at project inception satisfactorily resolved. Banks today are well capitalized and supervised.			
<b>Indicator 3 :</b>	<b>Reduced legal uncertainty in payment systems and improved risk management.</b>			
Value quantitative or Qualitative)	No clear regulatory framework for payment systems, no functioning lender of last resort.	High value payments system fully operational for all participants in systemically important transactions. The legal framework has been strengthened and the BCH has explicit powers to oversee the payments system.		The technical implementation of a modern payments system finalized and operating satisfactorily; connections with all individual financial institutions are being established. Legal framework strengthened, BCH has explicit powers to oversee the payments s
Date achieved	12/31/2004	02/28/2013		06/30/2013
Comments (incl. % achievement)	Largely achieved: 12 banks already submitting transactions electronically to new payments system (71% of the number and 94% of volume); remaining smaller institutions in final certification stages. Payments System Law drafted and submitted to Parliament.			
<b>Indicator 4 :</b>	<b>Effective special unit against money laundering within the CNBS leading to increased volume and quality of on-site examinations.</b>			
Value quantitative or Qualitative)	Financial intelligence Unit established but not yet operating effectively.	Improved effectiveness of special unit against money laundering at the CNBS.		Financial Intelligence Unit working effectively. FIU has sent 2,000 cases of potential money laundering cases to the Prosecutor's office.
Date achieved	12/31/2004	02/28/2013		06/30/2012
Comments (incl. % achievement)	Achieved. Financial Intelligence Unit established at CNBS and working effectively. Problems remain with other agencies lagging behind, particularly in following up with investigations (Prosecutor's Office) and enforcement (judicial system and police).			
<b>Indicator 5 :</b>	<b>Increased quality, transparency and timeliness of the information available to CNBS and BCH on bank soundness and major corporate clients.</b>			
Value quantitative or Qualitative)	Significant delays in the provision of data by banks.	All banks are reporting requested data to the CNBS and SIC on time, complying with established timelines.		All banks continue to report requested data to the CNBS and the SIC on time, complying with established timelines.
Date achieved	03/30/2005	02/28/2013		06/30/2012
Comments (incl. % achievement)	Achieved. Information on bank soundness readily available to CNBS, allowing to take preventive measures. Information on corporate clients available to authorities and all			

achievement)	regulated financial institutions through the Credit Information System (SIC).			
<b>Indicator 6 :</b>	<b>Reduced levels of non-performing loans from the top 50 Honduran corporate borrowers.</b>			
Value quantitative or Qualitative)	High level of nonperforming loans from top 50 Honduran corporate borrowers.	Reduced levels of nonperforming loans from top 50 Honduran corporate borrowers.		Cannot be verified, likely achieved as overall level of non-performing loans decreased significantly.
Date achieved	12/31/2004	02/28/2013		06/30/2012
Comments (incl. % achievement)	Cannot be verified. Information on performance of loans granted to the top 50 corporate borrowers is available in the credit registry to the authorities and regulated financial institutions, but not accessible to the public.			
<b>Indicator 7 :</b>	<b>Increased efficiency of corporate restructuring and orderly liquidations, both judicial and extra-judicial.</b>			
Value quantitative or Qualitative)	Inadequate framework and practices related to corporate dissolution, liquidation, bankruptcy and suspension of payments.	Increased efficiency of judicial and extra-judicial corporate restructuring.		Reflecting the increased relevance granted by the Honduran authorities to this subject, draft legislation on corporate insolvency was presented to Parliament (which has not been approved yet).
Date achieved	12/31/2004	02/28/2013		06/30/2012
Comments (incl. % achievement)	Not achieved.			

**(b) Intermediate Outcome Indicator(s)**

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
<b>Indicator 1 :</b>	<b>Banking resolution framework and capitalization fund capabilities.</b>			
Value (quantitative or Qualitative)	Inadequate banking resolution framework not based on minimum costs principles.	The operational procedures for the resolution process have been finalized and the fund established. The operational procedures have been proved and all the failed banks in the system have been resolved or merged with another sound financial		The operational procedures for a bank resolution process have been successfully tested (Banco del Pais , La Constancia, Banco de los Trabajadores). The resolution of the State-owned agriculture bank BANADESA however remains pending.

		institution.	
Date achieved	03/15/2004	02/28/2013	06/30/2012
Comments  (incl. % achievement)	Achieved		

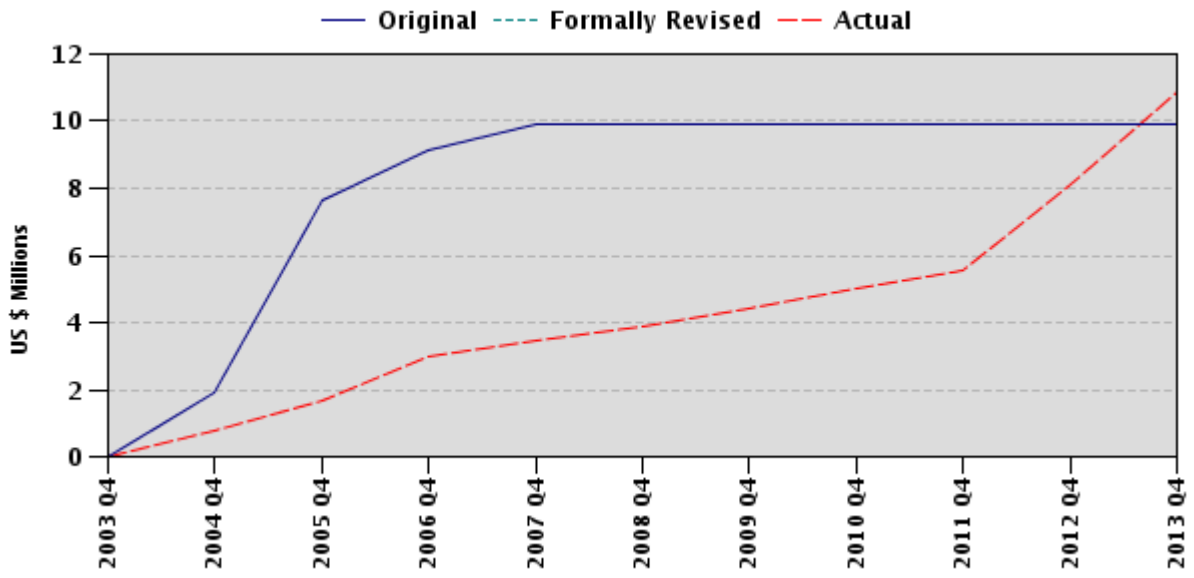
### G. Ratings of Project Performance in ISRs

No.	Date ISR Archived	DO	IP	Actual Disbursements (USD millions)
01	10/23/2003	Satisfactory	Satisfactory	0.00
02	6/10/2004	Satisfactory	Satisfactory	0.75
03	6/24/2004	Satisfactory	Satisfactory	0.75
04	11/30/2004	Satisfactory	Satisfactory	1.02
05	4/22/2005	Satisfactory	Satisfactory	1.29
06	9/20/2005	Satisfactory	Satisfactory	1.86
07	6/1/2006	Moderately Satisfactory	Moderately Satisfactory	2.98
08	11/28/2006	Moderately Satisfactory	Moderately Satisfactory	3.26
09	06/11/2007	Moderately Satisfactory	Moderately Satisfactory	3.38
10	12/19/2007	Moderately Satisfactory	Unsatisfactory	3.64
11	05/23/2008	Satisfactory	Moderately Unsatisfactory	3.78
12	10/30/2008	Satisfactory	Satisfactory	3.94
13	05/18/2009	Satisfactory	Satisfactory	4.39
14	12/23/2009	Moderately Satisfactory	Moderately Satisfactory	5.17
15	06/30/2010	Moderately Unsatisfactory	Moderately Satisfactory	4.98
16	12/17/2010	Moderately Satisfactory	Moderately Satisfactory	5.26
17	07/11/2011	Moderately Satisfactory	Satisfactory	5.54
18	01/26/2012	Satisfactory	Satisfactory	7.27
19	09/02/2012	Satisfactory	Satisfactory	8.20
20	03/12/2013	Moderately Satisfactory	Moderately Satisfactory	10.44

### H. Restructuring (if any)

Restructuring Date(s)	Board Approved PDO Change	ISR Ratings at Restructuring		Amount Disbursed at Restructuring in USD millions	Reason for Restructuring & Key Changes Made
		DO	IP		
04/27/2007		MS	MS	3.38	1.Extension of the closing date 2.First amendment to the Development Credit Agreement
04/07/2009		S	S	4.28	1.Extension of the closing date 2.Reallocation of the proceeds
11/29/2010		MU	MS	5.26	Extension of the closing date

## I. Disbursement Profile





## 1. Project Context, Development Objectives and Design

### 1.1 Context at Appraisal<sup>2</sup>

1. **Honduras has experienced several decades of low economic growth.** During the 1990s when growth had recovered in the rest of Central America, in Honduras, it barely kept pace with population growth, making it the slowest growth rate in the region. Natural disasters (hurricanes and earthquakes) and a deterioration of the terms of trade, exacerbated by erratic policies and institutional weaknesses, compounded the situation and weakened the banking system.

2. **By 2003, the stability of the Honduran banking system was uncertain, given the significant vulnerabilities of the country's financial sector.** The Honduran financial sector suffered a severe shock in October 1998, when Hurricane Mitch hit the country with devastating effects in terms of human lives and disruption of economic activity. In its immediate aftermath, the financial sector was faced with an upsurge in the volume of bad debts and substantial financial losses. A mid-sized bank had to be liquidated by the National Banking and Insurance Commission (*Comision Nacional de Bancos y Seguros*, CNBS) and most financial institutions were forced to request new injections of capital from their shareholders to restore their solvency. The 2003 Financial Sector Assessment Program Update (FSAP) highlighted significant vulnerabilities in the sector, including weak compliance with the Basel Core Principles (BCP) for effective banking supervision, insufficient provision of loans adversely affected by exogenous shocks, low capital asset ratios and high numbers of non-performing loans (NPL).

3. **In response, the Government embarked on an economic reform program focused on ensuring macroeconomic stability and strengthening growth prospects, and made significant progress in addressing financial sector vulnerabilities.** Consistent with the recommendations of the FSAP, a series of laws and regulations were approved in 2004 that: (i) strengthened prudential norms (including capital adequacy, loan classification, and provisioning), (ii) enabled consolidated supervision (including offshores, affiliates and subsidiaries), (iii) increased the powers of the supervisory agency, the CNBS, (iv) broadened the circumstances that require corrective actions by banks, and (v) improved the bank resolution framework. Within this context, the International Development Association (IDA) support sought to contribute to the strengthening of the financial sector, considered critical for the achievement of accelerating equitable and sustainable economic growth to levels consistent with the poverty reduction targets, as outlined in IDA's Country Assistance Strategy (CAS) approved by IDA's Board simultaneously with this Credit on June 24, 2003.

### 1.2 Original Project Development Objectives (PDO) and Key Indicators (*as approved*)

4. **The Project Development Objective was to assist the Borrower to develop the institutional capacity it required to be able to address the systemic vulnerabilities of its financial system, through:** (a) the design and implementation of a banking sector consolidation program, (b) the reform of the Borrower's payments system, and (c) the improvement of selected

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<sup>2</sup> See Annex 5 for more details.

aspects of the Borrower's financial system infrastructure. The Project defined seven key performance indicators covering (i) compliance with prudential banking regulations, (ii) improved banks' risk management systems and increased cost efficiency, (iii) reduced legal uncertainty and payment system risks, (iv) the creation of a Financial Intelligence Unit (FIU) within the CNBS, (v) better information for the CNBS on banks and corporates, (vi) reduced number of NPLs for the largest 50 corporate borrowers, and (vii) an enhanced corporate restructuring and insolvency system (see Datasheet, section F).

### **1.3 Revised PDO and Key Indicators, and reasons/ justification**

5. **The original PDO and key indicators were not revised throughout the life of the Project and commitment to the original Components was maintained.** This was originally a four-year Project, which was extended three times for a total of six additional years, in response to institutional changes and external events. However, the Project objectives were formulated in broad terms and remained largely relevant throughout the life of the Project. The only variation that could have warranted a reformulation of the PDO is related to the objective of designing and implementing a banking sector consolidation program, as only some aspects of the program were implemented, as detailed below.

### **1.4 Main Beneficiaries**

6. **The CNBS and the Central Bank (BCH) were the main direct beneficiaries of this Project.** Other beneficiaries were the financial institutions whose performance and safety were expected to improve based on a strengthened regulatory framework and increased access to a modern financial system payments infrastructure. Finally, the Project benefited all users of financial services in Honduras, including depositors, creditors, investors, firms and households, whose savings in the form of bank deposits or other types of investments were expected to be less vulnerable to losses and would benefit from more security and lower funds transfer and investment fees.

### **1.5 Original Project Components**

7. **The Project was primarily designed to help reduce the risks of systemic instability in the Honduran financial system and address many of the key policy weaknesses identified in the 2003 FSAP Update.** Support was provided through four Components (for a detailed description see Annex 6)<sup>3</sup>:

**Component 1:** A banking sector consolidation designed to establish a sound and stable foundation for the recapitalization and recovery of the Honduran financial sector (US\$4.50 million).

**Component 2:** A major reform of the payments system to improve the efficiency of the financial system and facilitate business transactions, introducing a Real Time Gross

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<sup>3</sup> The PAD foresaw a fifth component (unallocated reserve), which is not reflected in the Financing Agreement and which was not implemented.



Settlement (RTGS) System and moving away from manual processing of checks and large-value money transfers (US\$2.25 million).

**Component 3:** Technical assistance to improve selected aspects of the financial sector infrastructure, including addressing weaknesses in the Anti-Money Laundering/Combating Financing of Terrorism (AML/CFT) framework, enhancing oversight of the corporate sector and improving Honduras's insolvency regime, facilitating access to finance by small agricultural producers, as well as enabling the early recognition and more efficient handling of future problems in the financial sector (US\$2.03 million).

**Component 4:** Project Administration Component to provide support for the Project Coordination Unit (PCU) in the CNBS in order to assure effective project management and coordination, and strengthen the capacity of this unit to implement and supervise the Project (US\$1.11 million).

## 1.6 Revised Components

8. **The Project components did not change through the life of the Project.** In spite of this, the allocation of funds and resources dedicated to each area was significantly revised to reflect the changes in the needs and priorities of the CNBS and the BCH as will be described below.

## 1.7 Other significant changes

9. **The Project's closing date was extended three times to allow more time for completion of Project activities.** These extensions were motivated mainly by the delays in the implementation of components assigned to the BCH. The approval of the first extension was based on the expectation that project implementation would improve. The second extension was conditional on the signing of the contract between the CNBS and the implementing firm of the Project's payment system Component, and its subsequent approval by the Honduran Congress. The last extension was given on the condition that the bid evaluation for the payment system at the BCH be presented to IDA no later than mid-June 2011.

10. **The three extensions resulted in a major reallocation of Project funds.** Credit proceeds were reallocated among components to reflect changing priorities as the reduction of resources allocated to Component 1 allowed for the inclusion of new sub-projects (see below), which were necessary, but not included in the original plan. The first and second extensions brought a substantial reallocation of funds, leading to a significant decrease in the funds allocated to Consultants' Services, a major increase in the financing of Goods, and a decrease in Training, with minor adjustments in the remaining items (see Annex 1). This reflected the BCH's need to finance the acquisition of two new modules: the Economic and Financial Management and Information System (*Sistema de Información y Gestión Económica y Financiera*, SIGEF) and the Electronic Foreign Exchange Trading System (*Sistema Electronico de Negociacion de Divisas*, SENDI). The Project financed the software, hardware, and consulting services required to improve the BCH's internal systems.

## 2. Key Factors Affecting Implementation and Outcomes

### 2.1 Project Preparation, Design and Quality at Entry

11. **The Project correctly diagnosed the institutional weaknesses of the Honduran financial system.** Its diagnostic coincided with the FSAP in identifying low bank capitalization and a weak institutional framework for financial sector transactions, regulation and supervision as the main weaknesses of the financial system. In 2003, the banks had high non-performing loans and high operating costs which resulted in low profitability. Moreover, the banks had weak bank risk-management practices. These risks were magnified by the weak legal and regulatory framework and by the poor macroeconomic context and outlook. These factors made the likelihood of a systemic banking crisis a real possibility.

12. **The diagnostic correctly pointed to critical issues, such as weak institutional capacity at the CNBS, with major weaknesses in AML/CFT legislation and enforcement,<sup>4</sup> and a restrictive bank resolution framework with limited preventive and intervention tools.<sup>5</sup>** Weaknesses in regulatory elements (such as an adequate credit classification and provisioning system, supervision manuals, the training of financial sector supervisors, the use of compliance-based supervision, instead of a risk-based approach and the absence of consolidated supervision) facilitated regulatory arbitrage while hiding aggregate risks. In addition to weak supervision, banks had low and poor quality bank capital, raising concerns about solvency risks in some banking institutions, leading to the establishment of the Bank Capitalization Fund under the Project. An ineffective and seldom used corporate bankruptcy law, focused on the preventive attachment of assets by creditors, raising banks' losses given default.<sup>6</sup> Another major concern at the project's inception was the modernization of the payment systems, which had a number of structural shortcomings resulting in high exposure to credit, liquidity, legal, operational and settlement risks both for fund transfers and securities transactions.

13. **The PDOs were consistent with the Borrower's priorities at the time of Board approval and with the CAS.** The CAS (submitted to the Board with this credit) identified the weaknesses of the Honduran financial system as a potential constraint to achieving its first objective of accelerating equitable and sustainable economic growth to levels consistent with the poverty reduction targets. While formulated in broad terms, the PDO and Project components addressed the sectoral weaknesses and were relevant throughout the life of the Project, with the exception of Component 1, as discussed below.

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<sup>4</sup> Law 45-2002 was perceived as a significant step forward in the control of money laundering. However, much work remained to be done for its effective implementation. A major legislative gap was that the crime of financing of terrorism (CFT) was neither criminalized as a separate offense, nor as an AML offence.

<sup>5</sup> It contemplated only two possible resolution mechanisms: (i) the authorities could close a failing bank after transferring its deposits to another institution (the "restitution" mechanism) or, (ii) alternatively, they could capitalize and temporarily manage the impaired institution through FOSEDE, the Deposit Insurance Fund (the "extraordinary" mechanism). The latter had been abused beyond systemic crisis situations.

<sup>6</sup> This led to widespread early use of judicial enforcement mechanisms, explaining the significant amount of foreclosed assets owned by the banks.

14. **The PAD correctly assessed the overall high risk rating of the Project, however it underestimated the country related risks.** The risks of the weakening of the authorities' commitment to the financial reform program and the potential loss of confidence of depositors in the bank recapitalization program were rightly identified during Project design. The PAD underestimated the intrinsic project risks, which ended up delaying significantly its implementation. It was not possible to foresee the political instability that brought additional complications for project implementation.

15. **The design of project activities for the implementation of the payments system had some weaknesses and did not build on a comprehensive diagnostic of the capacity of BCH.** A more comprehensive diagnostic of the BCH's weaknesses would have pointed at the need to modernize the general ledger of the BCH as a condition for the successful operation of an automated payments system. It would also have addressed the lack of an automated foreign exchange auction system. As these weaknesses became evident, they forced a major redirection of the Project during implementation. The Project's design also underestimated the time required and the capacity of the key participating agencies (CNBS and BCH) to implement and coordinate the activities.

16. **This technical assistance project was followed by an adjustment operation (the "Financial Sector Development Policy Credit," FSDPC), which was unusual.** Usually the reverse sequence would have taken place. The justification for this unusual sequencing was based on the Government's need to organize its institutional framework for banking sector consolidation. The Government was also discussing a Stand-by Arrangement with the IMF, thereby making it impossible to move forward first with an adjustment credit (see Annex 6). The expectation was that by moving forward with the technical assistance credit even in the absence of an adjustment operation, the Government would be able to address some of the financial sector issues before committing more resources.<sup>7</sup>

## 2.2 Implementation

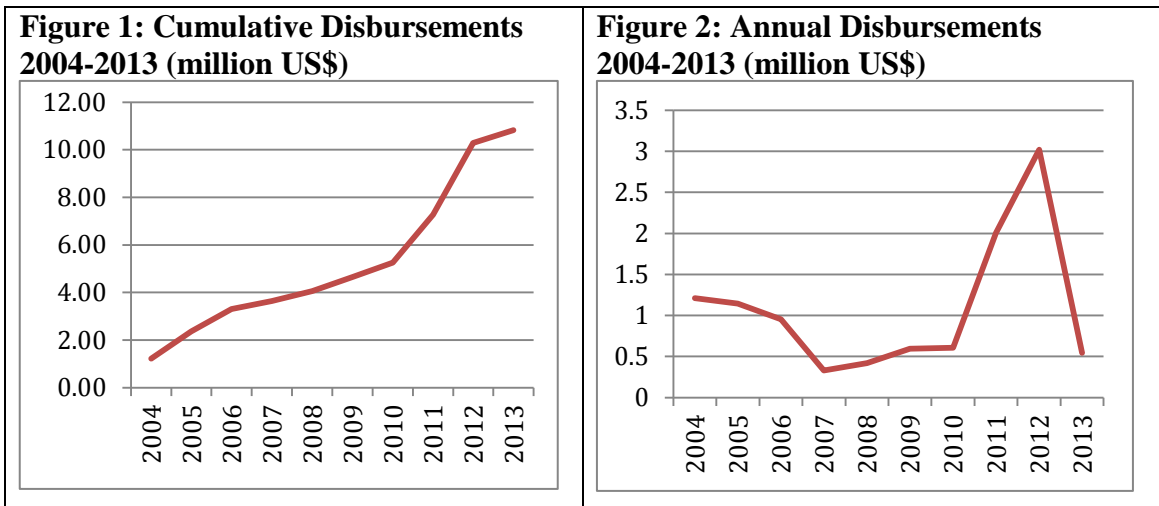
17. **Government Commitment to the Project fluctuated as a result of changes in leadership.** Initially, the Government and the two key participating agencies (CNBS and BCH) demonstrated a very strong commitment to the Project throughout preparation. After the change of administration and the changes in leadership of the CNBS and the BCH, the commitment became lukewarm and recovered in the last phase of the Project, during the tenure of the current administration of President Lobo.

18. **The Project made use of almost 99 percent of the Credit's resources.** Figures 1 and 2 show disbursements over time, with three rather distinct phases: (i) 2004-2007 with low and declining annual disbursements; (ii) relative paralysis between 2007 and 2010; and (iii) rapid execution of the Project since 2010. The first closing date extension did not accomplish the expected results and, towards the end of that period, external factors to the Project interfered with implementation (change in Government in June 2009). The second extension yielded results

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<sup>7</sup> PAD, page 15.

in its last year (2011), providing some justification for the third and final one. Notably towards the end of the project, the implementing agencies performed better than in the earlier years and provided significant support to complete successfully the project and make use of the available resources.



19. **Project implementation suffered numerous delays due to external and internal factors.** The external factors included: (i) delays in credit effectiveness because of delays in the Congressional approval process (one year), (ii) four changes in Government, one of which led to the suspension of high-level contacts between the Government and the Bank for a period of nine months (June 2009-April 2010) after the removal of President Zelaya; and (iii) multiple changes in the leadership of CNBS and BCH, resulting in an uneven commitment to the Project and a sometimes difficult relationship between the two institutions. The internal factors included: (i) the technical complexity of the tasks which generated difficulties in defining technical specifications and preparing bidding documents, (ii) the difficulties experienced in the procurement of goods and services, and (iii) the limited implementing capacity. In addition, the decision to allow both the CNBS and BCH to implement concurrently and have decision-making authority was also a factor impacting effective coordination and Project implementation. This made it more difficult to supervise the procurement of the appropriate modules required by the SIGEF and RTGS system.

20. **The Project’s focus shifted from the initial concentration on bank restructuring to the implementation of the payments and other IT systems at BCH while maintaining the activities to strengthen the regulations and supervisory capacity of the authorities.** There were multiple adjustments to the various components to accommodate new needs and changing priorities, particularly of the BCH. In particular, the objective of increasing the capacity of the authorities to promote and lead bank restructurings lost relevance in view of the capacity demonstrated by the private banks to restructure themselves with little CNBS intervention. Consequently the Bank Recapitalization Fund and attached technical assistance under Component 1 was not activated, resulting in a significant shift of resources from Component 1 to Component 2.

21. **The focus of activities in Component 1 shifted over time.** As the Project's activities related to the rehabilitation of failing banks lost importance, the activities under this Component concentrated on improving the legal and regulatory framework for banking (including the Financial Institutions Law, the Law for Deposit Insurance, the Laws for CNBS and BCH, key prudential regulations, inspections manuals, and risk and governance standards) as well as on developing CNBS's capacity to oversee the financial system and to deal with high risk institutions by developing an early warning system, training staff, and acquiring software and hardware to improve bank supervision. The activities financed in regards to the rehabilitation of some banks included only some legal and diagnostic work and the preparation of business plans, which were carried out during the early phases of project execution.

22. **The size of Component 2 greatly increased over the life of the Project.** Under Component 2, the Project's aim was to "carry-out an upgrade of the current system, including the launching of a special purpose large value payments system and the establishment of a government securities depository. Around 21.3 percent of IDA proceeds were original allocated to this Component; however, it ended up absorbing about 60 percent of the funding and financed the additional activities of SIGEF and SENDI.

23. **Activities under Component 3 were reduced as some sub-components were only partially implemented.** Component 3 focused on three aspects of Honduras's financial infrastructure: (i) the institutional framework for the AML/CFT, (ii) the oversight of the corporate sector and the insolvency and creditors' rights regime, and (iii) the instruments to facilitate access to finance by small agricultural producers. The latter two sub-components were only partially implemented, with the amendment of some regulations.

24. **The task force to implement the consolidation program for the financial sector foreseen under Component 4 was eliminated as it was not necessary anymore.** Initially, a task force of six members (four from the CNBS and two from the BCH) and an administrative assistant was to be established to implement the bank consolidation program. Given the demonstrated capacity of banks to restructure themselves, the task force was eliminated in 2007 as part of the amendments at the time of the extension of the closing date of the project to 2009.

25. **Despite challenges, key Project outputs by Component were largely achieved with the strengthening of CNBS and the establishment of the new payments system (see section 3.2).** A summary of the principal outputs is shown in Annex 2 (Outputs by Components). The annex breaks down the existing contracts that were entered into by the CNBS and the BCH and illustrates in detail how the Project Components were implemented. It shows the amounts disbursed by Component and summarizes the objectives that each contract was expected to meet.

### **2.3 Monitoring and Evaluation (M&E) Design, Implementation and Utilization**

26. **Measurement of achievements could have benefited from a stronger M&E framework.** While IDA did not put as much emphasis on the M&E framework when the Project

was designed, it would have been desirable to develop a more robust framework with measurable quantitative indicators during implementation as a tool to improve Project management and results.

27. **Overall, the results indicators were mainly qualitative in nature**, such as assessing whether the risk-based supervision carried out by a regulatory agency was consistent with international best practice. The PAD M&E framework did not originally include quantitative indicators, although certain indicators tracking the impact of Component outputs on PDO were later included in the Implementation Status Reports (ISR), including those related to the allocation of funds in 2009 and those associated with the reduction of risk and increase in efficiency of the financial system. Some of the Key Performance Indicators were not causally related to the Components, but depended on macroeconomic framework (for example, increased cost efficiency in the banking system and reduced NPLs for the largest 50 Honduran corporate borrowers) and other factors beyond the scope of the Project. The lack of a causal link of the indicators of the Project impeded management from integrating the M&E framework more closely with Project implementation, since the achievement, or lack thereof, of some of the outcome indicators was largely beyond the scope of the Project. In addition, the indicators related to the monitoring of corporate borrowers could only be tracked indirectly.<sup>8</sup>

28. **The PCU was moderately effective in terms of maintaining timely information.** While information about the execution of all activities was easily available, it did not keep up-to-date detailed records on a consolidated basis in terms of the purpose of each sub-project, costs, disbursements, and output.

## 2.4 Safeguard and Fiduciary Compliance

29. **There were no safeguard issues and fiduciary performance was adequate.** The Project did not trigger any social or environmental safeguards policies. The final audit found that the Project complied with all fiduciary requirements. Other audits during the period of execution marked only minor discrepancies in accounting (due to exchange rate fluctuations), as well as problems verifying compliance with some aspects of the loan agreement, which were resolved once issues surrounding the confidentiality of information were addressed.

30. **However, the Project faced significant challenges related to procurement, in particular of the payments system component, as well as of other IT components for the BCH.** In the case of the payments system, procurement activities had to deal with implementing a system in an environment of a rapidly evolving technology.<sup>9</sup> The procurement process leading

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<sup>8</sup> The indicators pertaining to corporate restructuring and to the performance of loans granted to the 50 largest corporate borrowers were not tracked in the ISRs, as the corresponding information is confidential and only available to the authorities and regulated lending institutions. The performance of corporate loans was tracked indirectly by looking at the overall behavior of the non-performance loans. In this light, a revision of the indicators related to the corporate sector would have been advisable.

<sup>9</sup> While the implementation of a payments system required, at the inception of the Project, the development of a customized IT solution, in the course of time, the industry evolved towards more standardized licensed packages,

to the selection of the winning firms (mainly for the RTGS) was slow, complex and disputed.<sup>10</sup> On IDA's side, there were delays in obtaining non-objections. A significant turnover of procurement officers, both at the IDA and in the PCU, was also a complicating factor. While technical and market factors contributed to the delays experienced in the implementation of the payments system, IDA and the Honduran authorities could have taken a more proactive approach to carry out the corresponding procurement processes, as a significant cause for the problems and delays in preparing the bidding documents was due to errors in following adequate procurement processes.

## **2.5 Post-Completion Operation/Next Phase**

**31. The authorities have indicated to IDA their interest in further technical assistance for both implementing agencies (BCH and CNBS).** The BCH would require support to further improve its systems in order to achieve further gains in security and efficiency, with a preliminary cost estimate of about US\$7.8 million. The CNBS would require support to better regulate and oversee financial cooperatives, the agricultural finance system, and the insurance sector as well as to further strengthen its capacity in the area of AML/CFT, among others, with preliminary cost estimates of about US\$2.6 million. The combined estimated external financing needs of the two institutions amount to about US\$10.5 million (see Annex 8). The lessons derived from the implementation of this technical assistance Project could be valuable in designing any new assistance.

## **3. Assessment of Outcomes**

### **3.1 Relevance of Objectives, Design and Implementation (Moderately Satisfactory)**

**32. The institutional strengthening objectives for the CNBS and the modernization of the BCH's general ledger and payments infrastructure were pertinent at design and remained highly relevant during the long implementation period.** The structure of the operation was appropriate to address the challenges faced by the financial sector and its oversight throughout the life of the project. The main shortcoming in the design was a consequence of the weak diagnostic for the payments systems activity, as described above. Based on this, the relevance of objectives, design and implementation are rated moderately satisfactory.

### **3.2 Achievement of the Project's Development Objective (Moderately Satisfactory)**

**33. The PDOs were largely achieved as measured by the seven Key Performance Indicators.** The overall assessment of the achievement of the PDOs is judged Moderately Satisfactory since the Project fully achieved three, largely achieved two, and did not achieve one

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which then had to be customized to meet the requirements of each institution. Overall, expertise on payments systems was very scarce in the market at the time of Project design.

<sup>10</sup> The difficulties faced by the payment system's contractor that won the bidding process of 2009 with the Central Bank ended in a contractual dispute, forcing the cancellation of the contract, payment of the guarantee and re-launching of the whole bidding process. In addition, the bankruptcy of the firm charged with implementing the precursor of the SIGEF system made it necessary to carry out a second procurement process for this activity.

of the seven PDO indicators. The only intermediate indicator was also achieved. One indicator - the level of non-performing loans of the top 50 corporations - cannot be verified, as the corresponding information is not publicly available, although the overall bank NPLs (which include those of the corporate sector) fell significantly over the period and it can be reasonably deduced, that the NPLs of the top 50 corporations have fallen as well.

34. **Supervision of the banking sector improved significantly**, due to the implementation of an ambitious plan to strengthen the CNBS's supervisory capacity with the help of this Project and additional assistance from the Inter-American Development Bank (IADB). Progress in modernizing and increasing the efficiency of supervision by the CNBS was very significant with the adoption of modern tools (Team Mate, electronic management of documents, and the introduction of a modern credit registry, among other tasks). Although the bank consolidation program and capitalization scheme to facilitate mergers between viable institutions was not activated, the initial diagnostics and business plans funded by the Project were very useful for the authorities to better understand and address the weaknesses of the system. Overall, the improved oversight contributed significantly to restore confidence in the financial system and through this to the growth of the economy through a higher savings rate and greater availability of financing. It's recommended that these advances be confirmed through an FSAP Update as soon as feasible, covering the assessment of compliance with the various international standards, particularly the BCPs.

35. **The Project achieved the modernization of the general ledger of BCH and development of the key financial infrastructure for the operation of the country's large-value payment and government securities systems (RTGS/SD)**, in addition to the foreign exchange auction system and the operation of the interbank market and efficient implementation of monetary policy. The new general ledger and connected systems (including the foreign exchange auction module) became operational in 2012. The RTGS/CD began operation on March 4, 2013, replacing numerous fragmented and cumbersome, vulnerable, and error-prone manual systems. These developments will enhance the efficiency and safety of financial transactions in Honduras and will have a significant longer-term development impact (see Annex 7). The adoption of a modern RTGS and the SENDI resulted in an increase in the efficiency and security of the country's large payments, enhancing the operational efficiency of monetary and exchange rate policies, as well as improving the safety of participants in the interbank market.

36. **Although the technical assistance credit was small, it produced relevant and tangible results that enhanced the Honduran financial sector.** The Project achieved a number of significant results. The main achievements of the Project were:

- i. Systemically important banks are meeting CNBS prudential regulations and required CARs.<sup>11</sup>
- ii. Banks have enhanced their risk management systems, purchasing specialized

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<sup>11</sup> The Honduran banking system remains solid with an average capital adequacy ratio of 14.5 percent in December 2012, up from 13.5 percent in November 2008, with all the banks in the system presenting capital adequacy ratios above the regulatory minimum of 10 percent.



software and consulting services.

- iii. The BCH's new automated general ledger, the large payment system and securities depository and the automated foreign exchange auction system are all operational and working efficiently, achieving one of the most important Project objectives.
- iv. The Financial Intelligence Unit at the CNBS is operating effectively, reporting suspicious transactions to the investigative and enforcement organs of the State, achieving, as far as the CNBS is concerned, the Project objectives.<sup>12</sup>
- v. The timeliness, quality and granularity of the credit and financial information used for prudential purposes by the CNBS and the BCH have greatly improved with access to a comprehensive and timely database.
- vi. The level of non-performing loans in the banking system has declined significantly, although this cannot be attributed directly to the Project.
- vii. The corporate and insolvency creditor rights have made some progress, but further work needs to be done to make the system operate effectively, particularly the interventions by the judicial system.
- viii. The operational procedures for a bank resolution process were finalized and have been successfully tested.

### **3.3 Efficiency (Moderately Unsatisfactory)**

37. **The longer-than-programmed duration of the Project adversely affected the efficiency of the outcomes.** Costs were higher for purchases of goods and services and Project management costs rose. The weakness in the procurement office during the early phases of the Project may have materially increased Project costs, and the less than satisfactory financial control reduced the efficiency of implementation. Overall, slow implementation significantly reduced the efficiency of the Project (see figure in the Datasheet Section I showing the gap between originally expected and actual disbursements). The project did not have an economic analysis.<sup>13</sup> While the Project's efficiency significantly improved in the final phase and all major activities were implemented, the Project experienced a long implementation period due to (i) poor management of the procurement process, and (ii) significant problems with service providers involved with the acquisition of the RTGS/CD that took place during the initial phase. The efficiency is rated as Moderately Unsatisfactory in consequence hereof.

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<sup>12</sup> These improvements contributed significantly to improve the rating of Honduras in respect to its efforts in the area of ASML/CFT, as acknowledged by the Financial Action Task Force, an international body that oversees the countries' efforts in regards to AML/CFT activities in its report from May, 2013

<sup>13</sup> The PAD stated in the section of economic analysis: "Given the character of this operation, a quantitative economic and financial analysis would not be the appropriate tool to assess the significance of this project. The pace and depth of the reforms envisioned in this operation will determine the ultimate economic benefits of this credit."

### 3.4 Justification of Overall Outcome Rating

38. **The Project has substantially contributed to strengthening the Honduran financial sector and the two main government authorities which have oversight function.** While the project took a long time to develop, it contributed substantially to:

- i. Strengthening the capacity of CNBS to supervise the financial institutions, detect in a timely manner the risks that could potentially affect them and, lastly, to have the mechanisms in place to act fast and deal with any negative developments, thus limiting considerably the potential negative consequences that the failure of a financial institution could have on the economy.
- ii. Establishing a functioning payments system that reduces the overall costs and uncertainty of financial transactions.
- iii. Improving significantly the monitoring of suspicious financial transactions that could be related to money laundering or the financing of terrorist activities.

39. **The PDOs maintained their relevance throughout the period and the most important institutional objectives were largely met.** Nonetheless, significant shortcomings in terms of efficiency and extended delays resulted in increased opportunity cost for the country and higher operational costs. Considering the above, the Development Outcome of this technical assistance credit is rated Moderately Satisfactory.

### 3.5 Overarching Themes, Other Outcomes and Impacts

40. **Although the project contributed to the improvement of the conditions for economic development, it did not have any direct attributable impact on poverty or social development.** The focus of the PDOs was on strengthening the institutional framework and of BCH and CNBS and did not address any gender issues. No unintended outcomes or impacts have been reported.

### 3.6 Summary of Findings of Beneficiary Survey and/or Stakeholder Workshops

41. **There was no formal survey of beneficiaries,** but the Bankers' Association and the Bank Processing Center (*Centro de Procesamiento Bancario*, CEPROBAN) were very supportive of Project activities, indicating to the ICR mission that its implementation has resulted in a very noticeable improvement in the safety and efficiency of operations for financial intermediaries. CEPROBAN opposed the BCH's imposition of a rather low cap for RTGS operations, as this reduces the volume of payments channeled by banks through its Automated Clearing House (ACH). The Bankers' Association mentioned the importance of FSAPs to assess the authorities' performance in complying with the various international standards assessed, including the BCPs.

## 4. Assessment of Risk to Development Outcome

Rating: Moderate

42. **A Moderate risk rating is assigned to the development outcome**, reflecting the perceived likelihood that changes that are detrimental to the sustainability of the Project objectives could take place. This rating is justified because:

- i. the risks to the continuity of the payments system reforms can be judged to be small. The RTGS system is operating satisfactorily with 12 of the 17 banks of the financial system (responsible for 71% of the transactions), and the remaining entities in process of joining it. The technology of the system has been proven in other countries and it the payments system can be expected to continue operating in a stable manner.
- ii. some moderate risks remain to the continuity of the achievements in the area of prudential regulations and supervision of the financial system. In spite of the considerable strengthening of the supervisory capacity of the authorities and the improvements to their framework, the risk of external interference into their operations remains. And,
- iii. a higher risk is attached to the effectiveness of the AML/CFT efforts beyond the scope of responsibilities of the CNBS. While the FIU at CNBS is operating adequately, the Prosecutor's Office and judicial system are not yet following up on the suspicious transactions reported to them by the FIU.

## **5. Assessment of IDA and Borrower Performance**

43. Project performance highly depends on six inter-linked critical factors: (i) initial Project design, (ii) flexibility to accommodate changing priorities, (iii) ownership, (iv) implementation capacity and skills, (v) sequencing and prioritization of the reforms; and (vi) absorptive capacity and resources.

### **5.1 IDA Performance**

#### **(a) Bank Performance in Ensuring Quality at Entry**

Rating: Moderately Satisfactory

44. **The PDO, Components and activities included in the PAD properly addressed the concerns of a likely systemic banking crisis in Honduras**, in view of the deterioration of the quality of bank assets, the weaknesses in prudential supervision and AML/CT systems, and the structural weaknesses in the payment systems of the country diagnosed in the 2003 FSAP. The likelihood of a systemic crisis scenario was even more plausible in view of the existing macroeconomic imbalances addressed by the IMF Stand-by Arrangement being negotiated with the Borrower. The Project correctly focused on the most critical and strategic weaknesses in the financial system.

45. **While the diagnostic of the CNBS weaknesses was appropriate, the diagnostic of BCH requirements was weak and the quality of the assessment of the implementing agencies was uneven.** Especially the initial, rather incomplete, diagnostic of the BCH's needs made it difficult to foresee and sequence the necessary activities that culminated in the implementation of the payment system Component, the RTGS system. A broader and more

thorough initial assessment of the BCH's weaknesses would have facilitated Project execution, focusing first on modernizing the general ledger and systems and financing the necessary technical assistance and IT systems for the critical SIGEF. The significant time, effort, and funding required to develop this system delayed the completion of the RTGS. For the above reasons IDA's performance in ensuring quality at entry is rated Moderately Satisfactory.

#### **(b) Quality of Supervision**

Rating: Moderately Satisfactory

46. **IDA proactively identified and resolved threats to the achievement of the development objectives, thus dealing with the consequences of significant political instability that resulted in uneven levels of commitment and high turnover of the senior staff at the implementing agencies.** In this context, IDA compensated for weaknesses in implementation capacity by extending the Project implementation period, intensifying supervision and financing additional consulting services. Focusing on the high developmental impact of the tasks financed by the Project, staff maintained in this form an intense supervision (20 ISRs) and added additional consulting services to foster the successful completion of the RTGS. Frequent missions provided support to the Honduran counterparts to better manage the Project activities and to discuss how to address the identified financial system weaknesses.

47. **The ratings assigned in the twenty ISRs might have been too sanguine when the Project was experiencing significant delays, possibly not bringing to management's attention the difficulties encountered: only one of the early ISRs gave an unsatisfactory rating.** Similarly, staff recommended the approval of the three extensions, but there was no evidence that the mid-term review flagged implementation problems, or recommended a possible restructuring or even the cancellation of the Project.<sup>14</sup> The Project should probably have been restructured to modify at a minimum the Key Performance Indicators or even the PDO.

48. **Based on the ICR guidelines, the quality of supervision was overall instrumental in achieving the objectives of the Project.** These factors, combined with the weaknesses in the Project's M&E, leads the rating for supervision to be Moderately Satisfactory.

#### **(c) Overall IDA Performance**

Rating: Moderately Satisfactory

49. **The PDOs remained valid and did not change throughout the nearly 10-year implementation period.** However the accumulation of delays, for reasons that were internal and external to the Project, led the authorities to request three extensions of the closing date. Over time, the priority and scope of the objectives changed, with greater emphasis given to the BCH Component, particularly the RTGS system. IDA's flexibility, staff stamina and patience to carry on with the implementation of the RTGS system until its successful completion allowed the Project to largely achieve its development objectives. However at the same time the prolonged

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<sup>14</sup> A mid-term review, carried out in early 2007, resulted in an adjustment to the project budget and extension. However, no mid-term review document was issued.

implementation period led to increased opportunity costs for Honduras and direct supervision costs for IDA.

50. **The combined rating for IDA's performance considering the above two factors is Moderately Satisfactory.** It should be noted that there were significant internal pressures to close the Project, which the authorities effectively resisted in view of the national importance of achieving the key objectives. A second order restructuring of the Project would have been adequate, especially to adjust the Key Performance Indicators and in this way to better reflect the changes in circumstances since inception.

## 5.2 Borrower Performance

### (a) Government Performance

Rating: Moderately Unsatisfactory

51. **The level of commitment and ownership at the highest levels of Government suffered during the long implementation period from the country's political and institutional instability.** Bank experience has shown that government ownership and commitment to achievement of the PDOs are the most critical factors for success. Both factors were in short supply during part of the implementation period, particularly between 2007 and 2010. The political instability, the changes in administrations, and the significant turnover in leadership of the implementing agencies contributed to the delays in implementing the Project (see Annex 4). In addition, the lack of supportive macroeconomic and institutional policies to expedite the approval of critical legislation and reforms<sup>15</sup> contributed to these delays. Finally, the appointment of inadequate staff to the PCU was a factor under the discretion of the government but was not always satisfactorily and promptly resolved. The rating of Moderately Unsatisfactory reflects these issues.

52. **Only towards the end of the Project, with the changes at the most senior levels of BCH and CNBS, a renewed and strong commitment was there and the present administration should be congratulated for this and for the achievement of the Project's objectives.**

### (b) Implementing Agencies Performance

Rating: Moderately Satisfactory

53. **The implementing agencies contributed decisively to the achievement of the PDO and the disbursement of the available funds despite periods of uneven performance.** Overall, CNBS and BCH valued IDA's assistance and recognized the importance of the development objectives supported by the credit: they actively engaged in implementing the Project's activities and achieving its goals. Although ownership of the Project at the highest levels, especially of BCH was at some points uneven, reflecting the fluctuating ownership of the

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<sup>15</sup> E.g. the Payments System Law or the Law on Corporate Insolvency

Project by the Government, the continuing efforts of the operational units made it possible for the activities related to the payments system to continue during the period of relative paralysis between 2007 and 2010. The active collaboration of the PCU, and of the units in charge of the modernization of the payments' and other systems at BCH, were decisive to the achievement of the PDOs. Although the difficulties in the procurement processes for the large IT systems (RTGS, SIGEF and, to a lesser, extent the SENDI) reflected the lack of experience of BCH staff, their technical capacity improved in time, allowing the Project to substantially contribute to a more efficient and secure operation of BCH in those areas. Considering the above, the performance of the implementing agencies is rated as Moderately Satisfactory.

### (c) Overall Borrower Performance

Rating: Moderately Unsatisfactory

54. **The rating reflects the average performance over all the phases of the Project.** Although the project's development objectives were largely achieved, the very significant delays in Project execution over time, which were caused largely by the uneven Project ownership by the authorities described above, had a major opportunity cost for the country and led to significant and high additional costs for IDA. As evidenced by the annual and accumulated disbursement charts, only from 2010 onwards did Project funds disburse rapidly, as the most expensive components (related to the SIGEF and the RTGS) were procured. The slight "disconnect" between the ratings assigned in the last ISR and the ratings in this ICR is because the ICR rates the overall performance of the borrower throughout the whole period of Project execution, while the ISR rates just the period preceding it. Given this overall performance, the rating for the borrower is Moderately Unsatisfactory.

## 6. Lessons Learned

55. The principal lessons learned for Project design and implementation are as follows:

- **In an environment of limited implementation capacity, Project design should be as simple as possible.** While there are limits to the simplification of specific components<sup>16</sup>, the overall design of the Project was overly complex for an environment of limited implementation capacity, uneven leadership, and episodic institutional conflicts between the two main implementing agencies (CNBS and BCH). A simpler structure and a better separation and costing of tasks would have been more appropriate.
- **The largest Project Component in terms of financing—the modernization of the payment system—suffered from an incomplete and superficial diagnostic at inception and an overly complex design.** The diagnostic included only a very limited scope of activities to be reformed and financed, making it necessary to incorporate other systems that were sub optimally sequenced and coordinated, which in turn caused additional costs and delays. The diagnostic of BCH's shortcomings should have gone further to include its

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<sup>16</sup> The modernization of the payments system, for example, requires a reform of applicable regulations, an update of procedures as well as the management of change by the participating financial institutions, which all have to be implemented together with adjustments to the technological infrastructure.

general ledger and its technical capacity before undertaking the modernization of the payment system. The Project should have identified the need for further technical assistance to the implementing agencies and, also, for the need to take a broader approach in modernizing BCH's systems and processes, sequencing the replacement of the general ledger and the addition of the SENDI as a prior reform to implanting a modern RTGS. In addition, the initial technical proposal to modernize the payment system prepared by BCH included too many modules, adding complexity to the bidding process and contributing to the failure of the first contractor<sup>17</sup>. The lesson for IDA was that breaking down the required actions into a phased approach could have simplified the process. This would have allowed for more attention to implementing the individual modules that support the overall structure of the RTGS and the securities depository Components, which should have been implemented in a second phase rather than simultaneously with the supporting modules. In this regard, the IDA team could have been more proactive in assisting and advising the BCH, both in terms of technical specifications and the complex procurement process.

- **In low-income countries with limited implementation capacity, it is critical to plan for and expect longer-term IDA engagements since these Projects often encounter adverse circumstances and delays.** Although this Project had clear implementation arrangements, the initial execution period proved to be too optimistic and three extensions of the closing date were required for successful implementation. An important lesson is that IDA must maintain the flexibility, staff stamina, and patience to carry on with the implementation of such Projects, even under duress, considering that the authorities would not have had the capacity to carry on and modernize a vital Component of the country's infrastructure.
- **IDA should agree up-front with Government on the size and composition of the PCU as well as the minimum experience and qualifications for each position.** Relative high turnover of staff at the PCU, both at the level of the Director and Procurement Officers, affected the dynamism and normal functioning of the Unit. The Government's selection of an inadequately qualified Director, who remained in the job for an extended period, ultimately contributed to additional delays in the execution of the credit. The high Senior staff turnover at the CNBS and the BCH and the uneven level of commitment towards the Project also resulted in significant delays in the implementation of the tasks under Components 1 (banking system consolidation) and 2 (financial sector supervision), but these changes were beyond the Project's control. It would have been useful for the Government and IDA to agree up-front on the minimum requirements and qualifications for PCU personnel as well as criteria to evaluate performance.

## **7. Comments on Issues Raised by Borrower/Implementing Agencies/Partners**

The borrower, i.e. CNBS and BCH, agreed in with the contents of this ICR and had some comments on specific details, which have been incorporated into this document.

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<sup>17</sup> Between the first and second bidding processes for the payment system the number of components were scaled down in order to increase efficiency and facilitate the procurement process. The implementation of the various modules was successfully accomplished by the second contractor, which won the second bid. It implemented a system that was less complex than the one originally offered by the first contractor, but more responsive to the central bank needs.

## ANNEXES

### Annex 1: Project Costs and Financing

**(a) Project Cost by Component (in USD Million equivalent)**

Components	Credit Amount (USD thousands)	Amount Paid (USD thousands)	Percentage of Total Cost
Technical Assistance for Banking Sector Consolidation Program (BCP)	3,114.90	2,714.80	28%
Reform of Payment System	5,874.10	4,985.90	52%
Improvement of Financial System Infrastructure	661.80	661.80	6%
Project Administration	1,293.00	1,254.30	12%
Exchange Rate Differential 01/02/13	173.70	0	2%
Rotating Fund	0	787	0%
<b>Total Project Cost</b>	<b>11,117.50</b>	<b>10,403.80</b>	

Note: Total amount as of March 2013

**(b) Financing**

Source of Funds Reform of Payment System	Amount Paid Estimate (USD millions)	Percentage of Cost of Reform of Payment System
International Development Agency (IDA)	5,874,118.81	85%
Central Bank of Honduras	1,047,751.78	15%
<b>Total</b>	<b>6,921,870.59</b>	<b>100%</b>



**(c) : Re-allocation of Funds 2007-2013 (SDR Equivalent)**

	<b>Credit Development Agreement</b>	<b>First Amendment</b>	<b>Second Amendment</b>	<b>Third Amendment</b>	<b>Disbursed*</b>	<b>Undisbursed</b>
Closing	September 30, 2007	June 30, 2009	June 30, 2011	February 28, 2013	July 23, 2013	July 23, 2013
Consultant Services	3,830,000.00	4,440,000	3,220,000	3,220,000	2,782,503	437,497
Goods	1,560,000	930,000	3,166,000	3,166,000	3,689,276	-523,276
Training	570,000	780,000	456,000	456,000	391,721	64,279
Audits	70,000	50,000	40,000	40,000	43,882	-3,883
Operational Costs	450,000	280,000	270,000	270,000	199,983	70,017
Unallocated	720,000	720,000	48,000	48,000	0	48,000
Designated Account A					8,125	-8,125
Total	7,200,000	7,200,000	7,200,000	7,200,000	7,115,491	84,509

\* The Disbursed column includes amounts as of July 23, 2013 (see draft closing letter to Minister of Finance) for each category. The amount for Designated Account A represents the exchange rate fluctuations between the SDR and the cost currency used to purchase the US Dollars for disbursement purposes.

**Annex 2: Outputs by Components**  
**Summary of Existing Projects**

<b>Existing Contracts CNBS</b>	<b>Amount</b>	<b>Objectives met</b>
<p>Acquisition of SGPS software (Sistema para Gestion del Proceso de Supervision). Installation, license rights.</p> <p>Objective: Provide CNBS auditors with modern audit software Team Mate.</p>	\$333,136.08	System has been installed on CNBS servers. Tests have been run on six (6) supervised entities. 100% of staff has been trained in use of software.
<p>Acquisition of SGDE (Sistema de Gestion de Documentos Electronicos). Installation, license rights.</p> <p>Objective: Document management software for CNBS.</p>	\$549,195.00	Software has been installed on CNBS servers. Usage manuals have been completed and training programs for technology, DPUF, legal and admin personnel have been concluded.
<p>Consulting Agreement: provide support to risk supervision and prepare plan of supervision.</p> <p>Objective: Provide training sessions to BNPS, SBFAAP on supervision manual based on risks faced by banks and financial institutions. Instill best practices.</p>	\$47,660.00	60 CNBS employees have undergone training.  A supervision strategy is being prepared for 2013 SBFAAP
<p>External Audit of project held Jan. 1 through December 31 2012 and at project closing.</p> <p>Objective: Allow external auditor to provide opinion with regard to financial status of project 3800-HO.</p> <p>Provide report and opinion on internal controls and compliance with Credit Agreement and applicable laws and regulations.</p>	\$16,750.00	Have the benefit of an external auditor independent from the project
<b>Existing Contracts BCH</b>		
<p>Acquisition, installation and implementation of LBTR (liquidación bruta en tiempo real).</p> <p>Acquisition, installation and implementation of CDV (sistema central de valores).</p> <p>Objective: To rely on a real time settlement payment system by which participating institutions can settle high value transactions in national and foreign currency through accounts held in Central Bank.</p> <p>Centralized automated registry of securities.</p>	\$1,068,271.40	<p>LBTR: Central Bank is running trial runs with SWIFT participant (Nov. 27, 2012).</p> <p>BCH has completed 80% of its trial runs. Participants have completed 10% of their trial runs.</p> <p>CDV: BCH started trial runs with participants Nov. 28, 2012.</p>

		CBH completed 95% of trial runs. Participants have completed 30% of trial runs.
<p>Consulting Agreement: payment system and securities settlement system specialist for the Central Bank.</p> <p>Objective: Provide advice to BCH in the evaluation of offers and contract negotiations for the acquisition of LBTR and CDV systems.</p>	\$92,600.00	Received advice and guidance from an international expert with regard to the design of the system, and the acceptance of the system.
<p>Consulting Agreement: Payment system and securities settlement system surveillance to BCH.</p> <p>Objective: Provide advice to BCH/CNBS with the acquisition process, negotiation and analysis of products with respect to surveillance for payment system and securities settlement system.</p>	\$51,600.00	Receive the benefit of a conceptual framework with respect to the function of surveillance and to benefit from a model of surveillance functions.
<p>Provision of hardware and software to strengthen client capabilities related to payment system of BCH.</p> <p>Objective: Provide equipment to be used in connection with software and computer solutions for payment system.</p>	\$359,178.71	Provide BCH with a modern technological infrastructure
<p>Consulting Agreement: National legal expert to develop legal framework for savings and credit cooperatives and corresponding regulations</p> <p>Objective: Prepare a draft of the legal framework and expand on a regulatory framework to be shared with international consultants.</p>	\$22,000.00	Have the benefit of a pre program study explaining the existing legal framework and regulations.
<b>Executed Contracts BCH</b>	<b>Amount</b>	<b>Objectives met</b>
<p>Acquisition of SIGEF (sistema de informacion para la gestion economica y financiera) for BCH.</p> <p>Objective: Obtain SAP ECC software modules: for accounting, budget preparation, inventory management, accounts receivable and bills payable etc...</p> <p>Software will be provided by Systech, S.A</p>	\$3,184,978.75	<p>The following capabilities were acquired:</p> <ol style="list-style-type: none"> <li>1. Accounting module implemented;</li> <li>2. Budget preparation module implemented;</li> <li>3. Several different types of Inventory management modules were implemented;</li> </ol>

		<p>4. Fixed asset module implemented;</p> <p>5. Acquisition module implemented;</p> <p>6. Accounts payable module implemented;</p> <p>7. Unusual operation detection module implemented.</p>
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### Annex 3. Bank Lending and Implementation Support/Supervision Process

#### (a) Task Team members

Names	Title	Unit	Responsibility/ Specialty
Modibo Camara	Senior Financial Sector Specialist	LCSPF	TTL at preparation and Project launch 2003-2004
Juan Carlos Mendoza	Manager, Portfolio and Operations	EACNF	TTL 2004-2005
Aquiles A. Almansi	Lead Financial Sector Specialist	FCSAB	TTL 2005-2008
Juan Buchenau Hoth	Senior Financial Sector Specialist	LCSPF	TTL 2009-2013
Alvaro Larrea	Senior Procurement Specialist	LCSPT	Procurement
Andres Mac Gaul	Senior Procurement Specialist	LCSPT	Procurement
Andrew McEwen Mason	Consultant	ECSF3	Payments Systems
Antonio Leonardo Blasco	Senior Financial Management Specialist	LCSFM	Financial Management
Beate Gisela Mueller	Consultant	LCSPF	Procurement
Carlo Corazza	Senior Payment Systems Specialist	FFIFI	Payments Systems
Corina Arteche	Consultant	FFIFI	Financial Systems
Diomedes Berroa	Senior Operations Officer	LCSPT	Procurement
Etel Patricia Bereslawski Aberboj	Senior Procurement Specialist	LCSPT	Procurement
Eva M. Gutierrez	Lead Financial Sector Specialist	LCSPF	Financial System
Fernando De Mergelina	Consultant	LCSPF	Financial System
Gisela Durand	Consultant	AFTFE	Operations
Henry Forero Ramirez	Senior Information Officer	TWICT	IT Systems
Ilka Funke	Consultant	LCSHS	Financial Inclusion
Joaquin G. Gutierrez	Lead Financial Sector Specialist	FFSAB	Financial system
Keisgner De Jesus Alfaro	Senior Procurement Specialist	LCSPT	Procurement
Luis Tineo	Senior Operations Officer	EACNF	Operations
Mary Lou M. Veizaga	Procurement	LCSPT	Procurement
Miriam Milquelis Pujols-Tizol	Program Assistant	LCSSD	Operations
Monica Patricia Rivero Riveros	Program Assistant	LCSPF	Operations

#### (b) Staff Time and Cost

Stage of Project Cycle	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
<b>Lending</b>		
FY03	28.62	214.00
FY04	18.28	106.50
<b>Supervision/ICR</b>		
FY05	18.02	82.00
FY06	13.05	98.00

FY07	19.62	155.00
FY08	12.81	117.55
FY09	16.28	141.00
FY10	16.92	171.00
FY11	9.25	139.53
FY12	10.71	109.00
FY13	8.28	117.00
<b>Total:</b>	<b>171.84</b>	<b>1,450.58</b>

#### Annex 4: PCU Staff Members and Counterparts

<b>PCU Coordinators</b>		
Gustavo Bonilla	February 2004	March 2006
Vidal Flores	April 2006	January 2008
Fernando Neda	February 2008	August 2009
Juan Carlos Fiallos	September 2009	December 2010
Fernando Neda	January 2011	June 2013

<b>Procurement Officers</b>	<b>Starting date</b>	<b>Ending Date</b>
Helka Rodriguez	February 2004	January 2006
Karina Portillo	February 2006	March 2006
Mercy Hernández	May 2006	June 2006
Evelin Galeano	July 2006	December 2006
Karla Barahona	July 2007	June 2013

<b>Financial Specialists</b>		
Mario Ramirez	February 2004	May 2006
Nahun Flores	June 2004	June 2013

#### Institutional Leadership during Loan Period

<b>Term</b>	<b>National Banking and Insurance Commission</b>	<b>Term</b>	<b>Honduras Central Bank</b>
2002 – 2005	Ana Cristina Mejia de Pereira	2002 – 2005	Maria Elena Mondragon
2006 - Feb 2009	Gustavo Alfaro	2006-2008	Gabriela Nuñez
Feb – Jul 2009	Milton Jimenez Puerto	2008-2009	Edwin Araque
Jul – Aug 2009	Daniel Figueroa (Interim)	2009-2010	Sandra Midence
Sep 2009-Feb 2010	Jose Luis Moncada	2010-2014	Maria Elena Mondragon
Feb 2010-2014	Vilma Cecilia Morales		

## Annex 5: Context at appraisal and in 2012

### Context at Appraisal<sup>18</sup>

1. **Between 1960 and 2000, Honduras had many years of low economic growth performance.** Output growth ranked among the lowest in the region. During the 1990s when growth recovered in the rest of Central America, in Honduras it only kept pace with population growth. Natural disasters (hurricanes and earthquakes) and a deterioration of the terms of trade, exacerbated by erratic policies and institutional weaknesses, adversely affected growth. Slow growth and weak governance contributed to widespread social unrest. In response, the authorities embarked on an economic reform program focused on ensuring macroeconomic stability, strengthening growth prospects through the development of human capital and basic infrastructure, improving the environment for private sector development, and using international trade agreements to boost growth.
2. The government's program—supported by an International Monetary Fund (IMF) Poverty Reduction and Growth Facility (PRGF) arrangement—improved overall economic performance. The PRGF arrangement, approved in February 2004, contributed to a modest recovery and a significantly improved external position. A two percent annual growth rate in real per capita GDP was finally attained in 2004, after an extended period of zero or even negative rates. The fiscal strategy embedded in the PRGF was based on the gradual reduction of the fiscal deficit, while at the same time orienting spending toward priorities (growth-enhancing investment and poverty spending). Key reforms supporting this strategy included broadening the tax base, strengthening tax administration, upgrading the Integrated Public Financial Administration System, introducing the single treasury account, and the gradual restructuring of the public sector. Nevertheless, the risks to the fiscal strategy were rated as significant.
3. Key policy achievements included fiscal adjustments, in particular, by improving governance, catalyzing the reform of the financial system recommended by the 2003 Financial Sector Assessment Program (FSAP), and containing the increase in the teachers' wage bill. Successful program implementation was deemed crucial for sustained economic recovery, continued external support, and reaping the benefits of the Heavily Indebted Poor Countries (HIPC) initiative. However, public sector unions resisted the implementation of a prudent wage policy. Combined with rising oil and basic foodstuff prices, this resistance led to broad-based demands to relax fiscal policy.
4. The 2003 FSAP confirmed the significant financial sector vulnerabilities which had led to the establishment of this Project. These were, in particular:
  - *Weak compliance with the Basel Core Principles (BCP).* Honduras largely complied with three principles, materially non-complied with 20 principles, and did not comply with another two.
  - *Adversely affected loans not fully provisioned.* Banks had still not fully provisioned loans

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<sup>18</sup> IMF, Honduras, "Staff Report for the 2005 Article IV Consultation, Second Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility", March 5, 2005; and World Bank- IMF "Joint Staff Advisory Note on the Poverty Reduction Strategy Paper Second Annual Progress Report", March 8, 2005.



adversely affected by exogenous shocks, including Hurricane Mitch (1998) and the coffee crises (1999 and 2001).

5. **Since then, the authorities have made significant progress in addressing financial sector vulnerabilities.** Consistent with the recommendations of the FSAP, a series of laws and regulations were approved in 2004 that: (i) strengthened prudential norms (including capital adequacy, loan classification, and provisioning), (ii) enabled consolidated supervision (including offshores, affiliates and subsidiaries), (iii) increased the powers of the supervisory agency, the CNBS, (iv) broadened the circumstances that require corrective actions by banks, and (v) improved the bank resolution framework. The CNBS approved a schedule that gradually implemented the new provisioning requirements over three years.

#### The Honduran Economy in 2012<sup>19</sup>

6. **After reaching 3.75 percent in 2011, economic growth slowed in 2012.** Estimated at 3.25 percent, this decline in real GDP growth in 2012 partly reflected a contraction of the “maquila” sector (the light manufacturing sector operating in free zones). Headline inflation reached its lowest level at 4 percent in July 2012, but rose to 5.4 percent by the end of the year. This uptick reflected a reversal of favorable commodity price developments. Core inflation however, remained broadly stable at about 6 percent throughout the year.
7. **Fiscal policy became expansionary in 2012.** Government real expenditure grew slightly faster than in 2011 and tax revenue growth declined sharply. The latter reflected continuing tax exemptions, weak revenue administration, the expiration of tax measures adopted in 2010, and a Supreme Court ruling against changes to the income tax from 2011.
8. **The central government deficit is estimated to have grown to 6 percent of GDP in 2012, from 4.5 percent in 2011.** While the performance of state-owned enterprises also weakened, ongoing surpluses by public pensions contained the combined public sector deficit to 4.25 percent of GDP in 2012. Reduced domestic demand for new government paper and limited access to official external financing led to the accumulation of domestic arrears (whose stock is estimated to have reached about 4 percent of GDP at the end of 2012) and to the BCH credit to finance the deficit.
9. **Honduras’s external position continued to weaken during 2012.** The external current account deficit is projected to have risen to almost 10 percent of GDP in 2012, driven mainly by robust domestic demand, exchange-rate overvaluation, and less favorable terms of trade. Net international reserve losses for 2012 reached about US\$370 million, with gross reserve coverage falling to three months of imports (from 3.5 months at the end of 2011). Private capital outflows picked up in the second half of 2012, reflecting partly declining confidence.
10. **Monetary policy efforts have not been enough to prevent the deterioration of the external position.** Low policy interest rates and a tightly managed exchange rate have supported the expansion of domestic demand since 2010. Bank credit growth rose significantly in 2012, particularly foreign currency loans and consumer credit. Reflecting partly crowding out by the public sector, loan and deposit interest rates in lempiras rose

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<sup>19</sup> International Monetary Fund, Article IV Consultation with Honduras 2012.

substantially since mid-2012, but did not contain credit growth. The heavily managed exchange rate has not helped reduce the excess demand for foreign exchange or contain the real appreciation of the lempira.

11. **Today, Honduras continues to face significant social and institutional challenges.** It is one of the poorest countries in Central America and social conditions remain depressed, with about two-thirds of the population living in poverty. Policymaking has been constrained by persistent structural problems, including short political cycles, powerful vested interests, and social unrest. The country also faces challenges in the areas of rule of law, corruption, and government effectiveness.

### The Honduran Banking System

12. The Honduran banking system underwent a severe test as a consequence of the world crises in 2008 and 2009 and of the political crisis of 2009. Although the financial system fared relatively well in terms of stability—or has at least not performed worse than the rest of Central America—the crises’ negative impacts on loan portfolio quality led to widespread loan restructuring and weakened some banks to an extent which may merit a closer review.
13. **Notwithstanding the earlier crises, the financial sector remains generally sound.** Non-performing loans (NPLs) are low (2.5 percent in November 2012) and have been declining; and capital levels and provisions against NPLs have increased. Recently introduced new regulations to strengthen risk management will be fully implemented during 2013 and 2014. However, the rapid growth of consumer lending poses risks and financial dollarization remains high at about 30 percent. In addition, significant currency mismatches, especially on the borrower’s side, pose risks. The Superintendency of Banks has been addressing this issue through higher capital requirements on un-hedged loans.
14. **Banks and financial institutions experienced a significant turnover between 2004 and 2012.** In this period, the number of total banks grew from 16 to 17 and the number of financial institutions grew from nine to 10. In addition, there was a significant turnover among participants. Five banks exited and six new banks entered the market; one financial institution exited and two entered the market. The banking system also experienced a gradual and modest consolidation, as some banks were sold (Trabajadores Bamer, and HSBC), merged (Cuscatlan and Uno) or exited the market (Futuro and BGA) and new banks entered (Procredit, Azteca, Lafise, Popular, Davivienda and Citibank). Banco Cuscatlan was absorbed by Banco UNO, which afterwards was bought by Citibank. Banco de los Trabajadores is, at present, under a recapitalization plan ordered by the CNBS. Banco Bamer was absorbed by BAC, which in turn was recently purchased by a Colombian group. BGA, owned by the Panamanian Banco del Istmo, was bought, jointly with the whole group, by HSBC, which recently sold all its operations in Honduras to Davivienda, another Colombian group. Banco Futuro was sold to Banco Lafise, while Banco La Constancia and Banco de las Fuerzas Armadas were closed.
15. The turnover of financial institutions did not result in a significant market consolidation and a moderate market concentration remains. The three largest banks in 2004 had a 44.3 percent market share, rising in 2012 to 47.6 percent. There is a much higher degree of concentration of non-bank financial institutions; the three largest institutions in 2004 had a market share of 79.9 percent, dropping in 2012 to 60 percent. With very few exceptions,

the majority of participating banks and financial institutions have a market share of less than 10 percent.

2004 (absolute values in billion Lempiras)			2012 (absolute values in billion Lempiras)		
BANKS	LOANS	MARKET SHARE	BANKS	LOANS	MARKET SHARE
BANCATLAN	7,727	15.50%	BANCATLAN	31,070	18.30%
HONDURAS	470	0.90%	HONDURAS	395	0.20%
BANCOCCI	5,443	10.90%	BANCOCCI	20,800	12.30%
BANCOTRAB	1,418	2.80%	BANCOTRAB	2,007	1.20%
BANCON	1,112	2.20%	BANCON	6,046	3.60%
FICENSA	1,552	3.10%	FICENSA	5,778	3.40%
BAMER	5,573	11.20%	---	---	---
BANHCAFE	705	1.40%	BANHCAFE	1,931	1.10%
BANPAIS	5,011	10.00%	BANPAIS	18,867	11.10%
FICOHSA	6,614	13.30%	FICOHSA	27,818	16.40%
BANCO UNO	1,523	3.00%	---	---	---
BAC HONDURAS	2,504	5.00%	BAC HONDURAS	21,961	12.90%
PROMERICA	942	1.90%	PROMERICA	4,455	2.60%
FUTURO	720	1.40%	---	---	---
BGA	7,694	15.50%	---	---	---
CUSCATLAN	662	1.30%	---	---	---
			LAFISE	7,757	4.60%
			DAVIVIENDA	11,516	6.80%
			PROCREDIT	1,377	0.80%
			AZTECA	1,838	1.10%
			POPULAR	993	0.60%
			CITIBANK	4,962	2.90%
TOTAL	49,670	100%	TOTAL	169,572	100%
FINANCIAL INSTITUTIONS	LOANS	MARKET SHARE	FINANCIAL INSTITUTIONS	LOANS	MARKET SHARE
COFISA	233	17.50%	COFISA	848	12.17%
CODIMERSA	39	2.90%	CODIMERSA	153	2.20%
CREDI Q	618	46.50%	CREDI Q	2,171	31.15%
ACRESA	40	3.00%	ACRESA	759	10.89%
COFINTER	50	3.80%	COFINTER	320	4.59%
FPC	80	5.90%	FPC	255	3.66%
FICASA	40	2.90%	---	---	---
FINSOL	212	15.90%	FINSOL	969	13.90%
FINISA	18	1.30%	FINISA	110	1.58%
			FINCA	172	2.47%
			ODEF	1,212	17.39%
TOTAL	1,329	100%	TOTAL	6,969	100.00%

Source: CNBS Economic studies

## **Annex 6: Original Project Components and Sequencing of IDA Interventions**

1. **The original project objectives** were broken down into four Components: (i) Technical Assistance for Banking Sector Consolidation, (ii) Reform of the Payments System, (iii) Improvement of Financial System Infrastructure, and (iv) Project Administration.

### 1. Technical Assistance for Banking Sector Consolidation – (US\$4.50 Million):

2. This Component was originally designed to focus on:
  - Improvement of the legal and regulatory framework for banking, including the review and reform of: (i) the Financial Institutions Law, (ii) the FOSEDE Law, (iii) CNBS and Central Bank Laws, (iv) drafting of key prudential regulations and the inspection manual, and (v) the adoption of governance and risk management standards. The procurement actions are in the form of individual consultancies.
  - Rehabilitation planning and in-depth diagnostics of selected banks, including the preparation and assessment of rehabilitation plans, special diagnostic of troubled banks and advisory assistance for the resolution of non-viable banks. The procurement actions are in the form of consultants' services, employing firms and individual, both nationally and internationally.
  - Enhancing management of systemic risks, including detailed contingency plans, ongoing diagnostic and intensive supervision of high-risk institutions. The procurement actions were for: (i) consultants' services employing firms and individual, both nationally and internationally, (ii) training, including workshops, seminars, study tours and on-the-job training at similar institutions abroad, and (iii) acquisition of equipment, such as desktops and lap-tops, a database interface, servers and examination and statistical software and licenses.
  - The design and implementation of incentive packages for self-rehabilitation of banks, including hiring specialized companies to assist eligible institutions.
  - The design of an effective framework for bank asset liquidations by hiring a firm to carry out this function.

### 2. Reform of the Payments System – (US\$2.25 Million):

3. This Component involved advisory assistance for the formulation of a reform strategy and its implementation, acquiring and implementing a RTGS and acquiring and implementing equipment for the reform of the securities depository. The procurement actions were for: (i) consultants' services employing individual consultants, (ii) training, including workshops, seminars, study tours and on-the job training at similar institutions abroad, and (iii) equipment purchases (for the RTGS and securities depository).

### 3. Improvement of Financial System Infrastructure (US\$2.03 Million):

4. This Component focused on:
  - Strengthening the legal and institutional framework for AML/CFT, including strengthening of the Financial Information Unit (FIU), awareness-raising and training. The procurement actions were in the form of: (i) consultants' services, employing firms

and individual consultants, both national and international, (ii) training including workshops, seminars, study tours and on-the-job training at similar institutions abroad, and (iii) acquisition of equipment, such as desktops and lap-tops, a database interface, servers and analytical tools.

- Strengthening the framework for corporate restructuring and the initiation of the public oversight function, including the creation of an Oversight Unit for corporate risks at BCH, the reform of Honduras' Bankruptcy Law and regulations, improving creditor rights, advisory assistance for the implementation of new framework for corporate restructuring mechanisms (both judicial and extra-judicial) and elaboration of a reform proposal for property registries. The procurement actions were for: (i) consultants' services employing firms and individual consultants, both national and international, (ii) training, including workshops, seminars, study tours and on-the-job training at similar institutions abroad, and (iii) equipment purchases, such as desktops, servers and licenses.
- Dissemination of best practices in rural finance. The procurement actions were for: (i) consultants' services employing firms and individual consultants, both national and international, and (ii) training including workshops, seminars, study tours and on-the-job training at similar institutions abroad.

#### 4. Project Administration (US\$1.11 Million):

5. This Component was designed to provide support for the Project Coordination Unit (PCU) in the CNBS in order to assure effective project management and coordination, and strengthen the capacity of this unit to implement and supervise the project. It included the hiring of a project coordinator, a procurement specialist, and a financial/accounting specialist. This was done in accordance with IDA's guidelines for selection of individual consultants.
6. **The sequencing of IDA interventions was unusual, since the TA operation preceded the adjustment operation.** Nonetheless, correctly, the decision was made to provide initially support to the authorities through the TA project and to follow later on with the development policy credit. This sequencing was rather unusual, reflecting the constraints at the time of the project's approval, but, in the end, the adjustment operation came to support the execution of the project and, under normal project implementation circumstances, the project would have saved time.
7. Prior to appraisal of the IDA adjustment operation, the government had negotiated with the IMF an economic program aimed at reversing Honduras's fiscal deterioration and at creating the basis for faster growth and reduced poverty. The authorities reached a new Poverty Reduction and Growth Facility (PRGF) arrangement with the IMF Board in February 2003.
8. The First Financial Sector Development Policy Credit (First FSDPC) was to be executed over a period of two years, and would support the institutional development of the financial sector through reforms in the following five areas: (i) strategy for management of systemic risks, (ii) strengthening of the legal and regulatory framework, (iii) strengthening of anti-money laundering and financing of terrorism prevention system, (iv) strengthening of

supervision and control of systemic risks, and (v) strengthening of the payments system.<sup>20</sup>

9. **As indicated in the ICR of the First FSDPC, the PDO Indicators were:** (i) resolution of the adverse events that have occurred in the financial system within the framework of the new Financial System Law (Ley del Sistema Financiero, LSF), (ii) commitment to maintain Honduras's status of cooperating country with the Financial Action Task Force (FATF) and improved compliance with the FATF 40+8 recommendations, and (iii) achievement of the goal of clearing of checks in less than 48 hours.
10. **Intermediate Outcome Indicators included the requirements for:** (i) all banks to have risk management systems according to CNBS norms, (ii) banks to be in compliance with portfolio ratings and provisioning norms, and (iii) CNBS to take steps to carry out consolidated supervision of the financial groups operating in the country. The almost complete overlap of the project and the first programmatic financial sector development policy credit is quite striking.
11. According to the Implementation, Completion, and Results Report for the FSDPC, the implementation of its reform program "was significantly assisted" by the on-going TA project. "The approval of a technical assistance credit before the approval of the adjustment operation was crucial in helping the authorities to implement the financial sector reforms that were later supported by the first FSDPC." The project "financed the drafting of laws and regulations and the strengthening of the capabilities of the BCH and CNBS to implement the reforms." In this sense the two operations were mutually reinforcing.

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<sup>20</sup> ICR of the First FSDPC, page 4.

## **Annex 7: Improvements in Strengthening the Financial Sector’s Legal and Regulatory Framework and in the Operation of the Central Bank (BCH) under the Project**

1. The financial sector legal and regulatory framework has been significantly strengthened by the laws approved under the reform program including the enactment of the LSF law, the amendment of other financial sector laws, and the issuing by the CNBS of norms and regulations for the implementation of the LSF. The CNBS is effectively applying the new framework for prompt corrective action, which allows the authorities to detect and require remedial measures if the entities in the financial system suffer deterioration in their financial health due to the risks assumed. Several outcome indicators in this area have been met. Adverse events that have occurred in the financial system have been resolved within the framework of the new LSF. The dissolution in 2006/7 of a savings and loans association was carried out within the new legal framework and the assets and liabilities of the failed entity were sold to a large bank with contributions from FOSEDE. Since then, no adverse event has occurred in the financial sector that required the application of the bank resolution mechanism in the LSF law.
2. The outcome indicator concerning banks' compliance with the new norms has been met. Most of the banks in the system are in the process of adjusting their procedures to comply with the CNBS's norms on credit risk, including the establishment of risk management systems. This norm was fully implemented by December 2009. Foreign owned banks have their own risk management systems in place, as required by their headquarters. Also, according to CNBS reports, all banks are in compliance with portfolio ratings and provisioning norms. These norms have been modified several times.
3. Congress has not yet approved a new legal framework for the payment systems, (although a law has been presented) and the Law on Electronic Signatures (is being drafted).
4. Additional measures will be required to improve the effectiveness of the AML/CFT legislation, particularly since prosecution and the enforcement of sanctions fall under the orbit of the Public Prosecutor (“Ministerio Publico”) and the police, where major deficiencies remain in terms of resources, prosecutors’ integrity, judicial and police enforcement, and imposition of sanctions. While the UIF is functioning well within the CNBS, critical government agencies charged with investigation and enforcement are not performing their duties.
5. By contributing to a greater reliability and efficiency of BCH’s foreign exchange, monetary policy operations and payment processing, the project reduced prior vulnerabilities and costs, enhancing the efficiency and safety of the foreign exchange, money and inter-bank markets. The project will provide tangible benefits for the commercial banking system, particularly by improving the banks’ cash management and treasury operations. This will allow for a significant reduction of inter-bank risks as it will now be possible to conduct collateralized overnight operations in which BCH will block paper issued by itself or the government as collateral in its securities depository. This will eliminate the banks’ bi-lateral pledges via the exchange of letters or uncollateralized short-term loans. The following table provides an oversight over the main improvements in the

operation of BCH under the project.

<b>Before</b>	<b>After</b>
<p><b>Banks:</b></p> <p><b>(i) Account Management</b> Lack of on-line access to balances the BCH. Forced to request in paper form, by messenger, transfers or provide instructions via SWIFT through the International Department. Signatures must be verified, balances are checked manually and then operation is entered. Multiple staff and BCH Departments intervene during hours of operation (9:00 a.m.- 3:00 p.m.). BCH provides via e-mail messages debits/credits every hour to banks. Banks unable to have an efficient management of their Treasury operations (single account in three currencies: Lempiras, US Dollars and Euros). Banks are requesting an extension of the hours of operation.</p> <p><b>(ii) Government and BCH Securities/Bills</b> BCH auctions take place once a week on Mondays, but only until Wednesday the operation is finalized and the bank accounts are debited. Banks' offers are made through BCH web page and BCH Liquidity Committee decides auction amounts and prices.</p>	<p><b>Banks:</b></p> <p><b>(i) Account Management</b> Allows banks to improve significantly the security, efficiency and profitability of their Treasury operations, with on-line access to their BCH accounts. Banks will be able to manage efficiently their liquidity and invest excesses liquidity faster in the BCH and government paper. Queuing of payments will bring advantages in planning and prioritizing payments throughout the day. Banks' request for cash and coins will be channeled through the RTGS and BCH will instruct its branches to deliver. Efficiency gains in managing reserve requirements and forced investments.</p> <p><b>(ii) Government and BCH Securities/Bills</b> Opens the possibility of developing an efficient interbank market collateralized with BCH or government paper, improving systemic liquidity management and eliminating banks' credit risk, as safe collateral can be pledged overnight.</p>
<p><b>Automated Clearing House (ACH) Clearing and Settlement:</b> Banks electronically (image) present checks to the ACH managed by the Bank Processing Center (CEPROBAN) from 9:00 a.m. to 5:00 p.m. Checks are settled the same day, but they are physically exchanged next day. Banks' debit/credit customer accounts next day at noon. The ACH presents net balances (debits and credits) to the BCH to settle at the end of the day. There is no check truncation yet, due to legal restrictions.</p>	<p><b>ACH Clearing and Settlement:</b> ACH is able to clear check balances more often throughout the day, settling interbank debits or credits in the books of the BCH.</p>



<p><b>Foreign Exchange Operations:</b> Operations are manual and paper based, with banks sending, by messenger, envelopes the day before the auction, with FX allocated the following day in the morning, but accounts in dollars were credited two days later (no Delivery versus Payment).</p>	<p><b>FX Operations (SENDI):</b> The FX auction system, financed under the project, started operations in 2009. Banks can safely enter to buy FX (US dollars only) at BCH auctions between 1:00-4:00 p.m. defining amounts and exchange rate offered. Next day at 8:40 a.m. funds in Lempiras are blocked and at 11:30 a.m. banks' accounts are debited and US dollars credited in the correspondents' accounts. Banks are informed via SWIFT messages (Delivery versus Payment). SENDI is connected to the SIGEF.</p>
<p><b>RTGS/SD:</b> Large value payments going through the BCH are requested in paper form, via messenger, by the banks. Security is a major concern. De facto a lot of the large value payments are channeled through the ACH. Not possible to establish payment priorities.</p>	<p><b>RTGS/SD:</b> BCH was one of the last central bank in the region to introduce an RTGS/SD system (Belize being the last one). It will bring major improvement in security and efficiency, enhancing the operation of the FX, money and government/ BCH securities markets. Manual and multiple systems in operation (4 for securities) will be eliminated. BCH intends to limit ACH payments up to US\$10,000. The RTGS system completed parallel trials and started to operate March. As of mid-July, 2013 not all banks had been connected due to delays in complying with BCH's 4-step certification protocol. Small banks faced additional difficulties. Digital signatures lack legal basis until new law is approved and today operate under a CNBS regulation. The new Payments Law is in Parliament for approval.</p>
<p><b>Government Accounts:</b> The government has a unique centralized account at the BCH, but account management is paper-based and manual. Multiple accounts (about 2,000, in addition to accounts with SEEFIN) for state-owned enterprises (SOEs) managed by the BCH</p>	<p><b>Government Accounts:</b> National Treasury will enhance timeliness, security, and efficiency of liquidity management. Additional enhancements required to facilitate management of SOEs need to be developed.</p>

Note: DvP= Delivery versus Payment.

## **Annex 8: Post-Completion Operation/Possible Next Phase**

Moving forward, the BCH and CNBS have identified the following areas, in which they would require further assistance:

- I. The BCH has identified pressing needs going forward in the following areas:
  - a. Development of a government agencies' deposit and payment module linked to the RTGS.
  - b. Module of authorized electronic signatures of users of the Central Bank's RTGS system.
  - c. Purchase of middleware to allow the integration of Central Bank applications.
  - d. Addition of a human resource management and planning modules to the core SAP in use.
  - e. Module to automate the information of the Social Security Department.
  - f. Acquisition of digital document administration to replace current system of microfilming government and Central Bank securities.
  - g. Strengthening the computer centers' backup and recovery infrastructure.
  - h. Investing in IT systems to further protect the security of information.
  - i. Computer and telecommunication equipment for the new Central Bank building and the Parallel Computer Center in San Pedro Sula.
  - j. Central Bank "cloud" computer services.
- II. Despite significant strengthening of the CNBS's institutional capacity achieved in the last decade, going forward, there are significant needs in banking supervision. Thematically the following areas have been highlighted as priority areas for additional TA support:
  - a. Drafting of regulations to implement new laws, including the Social Security Law, the Law on Sureties and Guarantees.
  - b. Analysis, restructuring and development of new regulatory and supervisory frameworks for the cooperative sector, Fund Administration Companies and Mutual Guarantee Funds.
  - c. Development of financial inclusion plans linked to remittances channeled through cooperatives and OPDFs.
  - d. Improve the rural and agricultural finance systems and reform of BANADESA;
  - e. Review of the adequacy of the reinsurance regulations and training of specialists.
  - f. Regulation of micro-insurers and micro-pension companies.
  - g. Assistance to strengthen consolidated supervision.
  - h. Software and training to: (i) analyze the corporate data collected by the Credit

Risk Bureau for prudential purposes, (ii) development of stress-testing models, (iii) acquisition of statistical tools to estimate maximum expected losses.

- i. Assistance to conduct a self-assessment of GAFI's 40 recommendations for AML/CFT.
- III. Going forward, Honduras' CPS aims to define areas of engagement selectively. Selectivity can best be exercised by focusing on those sectors where the government has demonstrated strong demand and commitment, and where IDA is prepared to deliver. With this new focus, IDA should continue to pay attention to strengthening financial supervision, including regulation and supervision of non-bank financial institutions, while assisting the Central Bank to continue improving the country's payment system.

## Annex 9. Honduras: Selected Economic Indicators

	2008	2009	2010	2011	Projections 2012	2013
	(Annual percentage change, unless otherwise indicated)					
<b>National income and prices</b>						
GDP at constant prices	4.2	-2.4	3.7	3.7	3.3	3.3
GDP deflator	7.8	7.7	4.7	7.7	4.3	5.2
Consumer prices (end of period)	10.8	3.0	6.5	5.6	5.4	5.9
<b>Exchange rate (end of period, depreciation -)</b>						
Lempiras per U.S. dollar	19.0	19.0	19.0	19.1	...	...
Real effective rate	4.9	7.8	1.6	1.2	...	...
<b>Money and credit</b>						
Private sector credit	9.9	5.0	3.1	10.3	16.9	21.6
Broad money	5.3	1.1	9.4	12.4	9.7	15.7
Lending rate (end of period, in percent)	18.5	17.1	15.1	14.2	...	...
Deposit rate (end of period, in percent)	13.1	10.6	8.0	7.4	...	...
	(In percent of GDP, unless otherwise indicated)					
<b>Combined public sector</b>						
Noninterest revenue and grants	25.7	22.8	22.7	21.9	21.7	22.0
Noninterest expenditure	27.4	28.2	26.1	24.9	25.9	25.9
Primary balance	-1.7	-5.4	-3.4	-3.0	-4.2	-3.9
Net interest payments	-1.0	-0.9	-0.6	-0.2	0.9	1.0
Public saving	2.8	-0.8	0.6	1.1	0.7	-0.1
Capital expenditure	6.0	5.8	5.4	5.9	5.8	5.7
<b>Overall balance</b>	<b>-1.7</b>	<b>-4.5</b>	<b>-2.8</b>	<b>-2.8</b>	<b>-4.3</b>	<b>-4.6</b>
<b>Public sector debt 1/</b>	<b>22.9</b>	<b>24.6</b>	<b>29.7</b>	<b>32.1</b>	<b>34.7</b>	<b>36.2</b>
<i>Of which:</i> External debt	16.8	16.9	17.9	18.2	19.9	24.5
Public sector external debt service (in percent of non-maquila exports)	2.8	12.2	3.9	4.5	2.9	4.4
<b>Savings and investment</b>						
Gross fixed capital formation	33.6	22.0	21.6	25.2	23.7	24.5

Gross national savings	18.2	18.0	16.3	16.6	13.8	13.3
Gross international reserves (millions of dollars)	2,691	2,331	2,931	3,043	2,778	2,695
GIR (In months of imports) 2/	4.7	3.6	3.6	3.5	3.0	2.9
Change in net international reserves (increase -)	185	604	-589	50	367	50
External current account balance	-15.4	-4.0	-5.3	-8.5	-9.9	-11.2
Exports, f.o.b. (annual percentage change)	7.2	-22.1	26.6	27.6	2.4	1.4
Imports, f.o.b. (annual percentage change)	17.6	-29.4	20.7	23.4	2.5	6.7

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

1/ Debt series revised based on more comprehensive data series provided by the authorities in September 2012.

2/ Refers to the following year's imports of non-maquila goods and nonfactor services.

## **Annex 10. Summary of Borrower's ICR and/or Comments on Draft ICR**

### **A) Borrower's ICR**

The borrower submitted an ICR which is filed in WB Docs. Annexes “B” (general conclusions) and “C” (lessons learned) of the Borrower's document are reproduced below:

### **ANEXO B**

#### **CONCLUSIONES GENERALES**

1. La asistencia técnica para el programa de consolidación de la banca, ha sido altamente favorable para mejorar las capacidades normativas de la CNBS, estableciendo un marco regulatorio adecuado para realizar una supervisión basada en riesgos, manejo de instituciones en problemas e implementar los mecanismos de resolución, que permitan fortalecer la solvencia y mantener la estabilidad del sistema financiero.
2. Se elaboró y aprobó el Marco Jurídico Adecuado que regula la Insolvencia Empresarial, reformando los títulos VI y VII del Código de Comercio y artículos del Código Penal,
3. Se aumentó los niveles de solvencia de las instituciones financieras debido al fortalecimiento de las Reservas y del Capital regulatorio.
4. Se obtuvo una reducción y control del riesgo de concentración de operaciones con partes relacionadas mediante la disminución del monto otorgado a los mismos.
5. La aprobación de la reglamentación de Gobierno Corporativo efficientiza la administración de las entidades financieras.
6. Se establecieron los procedimientos para agilizar los mecanismos de aprobación y concesión del prestamista de última instancia.
7. Hay evidencia de logro de mejoras de la supervisión de las instituciones financieras, a través de la prevención de riesgo sistémico y el manejo de contingencias.
8. Se logró un desarrollo de la capacidad y competencias del recurso humano de la CNBS mediante la incorporación de nuevas herramientas de supervisión basadas en riesgo.
9. Las reformas del Sistema de Pagos constituyen un elemento vital en la infraestructura financiera de la economía del país, ya que posibilita y facilita las transacciones económicas, brindando seguridad en el proceso de intercambio de bienes y le proporciona al Banco Central de Honduras, el mecanismo para efectuar las acciones de política monetaria y regular la liquidez de la economía.
10. La implementación del Modelo de Indicadores de Alerta temprana para actuar en forma preventiva y no reactiva ante una eventual crisis sistémica, es un factor muy importante para una sana supervisión prudencial.
11. El Análisis y Actualización de la Regulación y Supervisión de los diferentes tipos de riesgos asociados a las Instituciones Financieras que atienden al Sector de Microfinanzas, permitió obtener conocimiento sobre la importancia de la supervisión de la actividad microfinanciera; así como, sobre los riesgos y retos de dicho sector en la región.

12. La nueva Metodología de Supervisión implementada, permitió fortalecer los procesos de supervisión para las instituciones que atienden al sector de microfinanzas, principalmente en lo relacionado a la evaluación del riesgo de crédito.
13. La obtención de nuevos conocimientos respecto al marco conceptual sobre la administración integral de riesgos, permite que la CNBS prevenir a las instituciones supervisadas para que no sufran pérdidas económicas considerables por la exposición al riesgo excesivo y que asuman los riesgos con decisiones acertadas.
14. Las nuevas metodologías específicas para la evaluación de un plan estratégico y de negocios, permitió determinar si los mismos expresan la estrategia real de las instituciones supervisadas, que atienden el sector de microfinanzas. En la actualidad dicha evaluación forma parte de la guía del riesgo estratégico de los procesos de supervisión.
15. En términos generales podemos concluir que al haber estado en el marco de Solvencia I, los organismos supervisores a nivel internacional han tendido a buscar mecanismos de regulación y prácticas de supervisión que les permitan cuantificar y monitorear los riesgos a los que están expuestas las instituciones de seguros por la actividad que realizan, por lo que buscan otro nuevo enfoque que combine las exigencias tradicionales de solvencia (reservas técnicas y suficiencia de capital), con requerimientos de gobierno corporativo y transparencia de mercado, así como fortalecer el perfil financiero de las instituciones de seguros y su calidad crediticia, aplicando el enfoque de solvencia II.
16. La Inestabilidad política del país debido a los sucesos de junio 2009 afectó la ejecución normal de las actividades del Proyecto, lo que trajo como consecuencia postergación de inicio y de ejecución de algunas actividades, cambios en los perfiles y alcances de algunos proyectos importantes.
17. Los cambios de autoridades en la CNBS y el BCH, generaron durante los primeros cinco años de ejecución del proyecto una alta rotación del personal clave del proyecto (Coordinador y personal técnico de adquisiciones) y además esto provocó constantes cambios en la programación de actividades producto de los objetivos que perseguía las autoridades de cada Institución.
18. Para la ejecución del Proyecto fue muy importante el apoyo recibido de expertos del Banco Mundial en actividades estratégicas como es el Sistema de Pagos del BCH.
19. La Comisión Nacional de Bancos y Seguros avanzó significativamente en la modernización del marco regulatorio del sistema financiero, así como en el alcance de su propio fortalecimiento interno en materia de metodologías, sistemas y herramientas desarrolladas para realizar la supervisión basada en riesgos.
20. Con recursos del Proyecto se iniciaron las primeras actividades para la implementación de la supervisión integral basada en riesgos, actividad estratégica que fue concluida a con recursos de otra entidad financiera internacional para la completa implementación del nuevo Manual de Supervisión Integral Basada en Riesgos, basado en las mejores prácticas.
21. La herramienta informática para auditoría denominada Team Mate, adquirida con recursos del Proyecto para las tres Superintendencias, se ha constituido en una plataforma electrónica de alto valor para efectos de mejorar la planificación, ejecución y hacer más efectiva la supervisión in situ y extra situ.

22. Con recursos del Proyecto y como parte de las actividades fundamental del mismo, el Banco Central de Honduras ha implementado con todo éxito el Sistema de Liquidación Bruta en Tiempo Real (LBTR) y Central Depositaria de Valores (CDV).
23. El Sistema electrónico de negociación de divisas, es otro proyecto financiado el cual permite la negociación de divisas entre los agentes cambiarios autorizados y el BCH, el que se encuentra funcionado desde el mes de junio de 2009.
24. La Unidad Coordinadora de Proyectos (UCP), dependiente de la Comisión Nacional de Bancos y Seguros (CNBS), fue de gran apoyo tanto como enlace entre Banco Mundial y el BCH, como en el asesoramiento, planificación, control, seguimiento y ayuda en las diversas tareas que implicaron la implementación de estos sistemas.
25. La implementación de estos proyectos impulsó a la elaboración de la Ley de Sistema de Pagos y Liquidación de Valores, así como de varios reglamentos resoluciones y circulares para normar los sistemas de pagos, y de Liquidación de Valores.
26. El Sistema financiero hondureño se ha visto beneficiado por la modernización del Sistema de Pagos y actualmente realiza parte de sus operaciones por medio de la ACH-Pronto y de la Cámara Electrónica de Compensación de Cheques, además poco a poco están procesando sus transacciones de alto valor por medio de la BCH-TR, con lo cual han mejorado substancialmente la seguridad y rapidez de las transacciones que llevan a cabo.
27. El Gobierno Central que es uno de los principales entes que realiza pagos, se ve altamente beneficiado con los nuevos Sistemas de Pagos, tanto por medio de la ACH-Pronto, de la Cámara de Compensación de Cheques, así como próximamente por medio de las transacciones en la BCH-TR.
28. El Banco Central de Honduras, ha visto una mejora considerable tanto desde el punto de vista jurídico; mediante la aprobación de los Reglamentos y Resoluciones del Directorio del BCH, que han venido a normar las diversas transacciones que se dan en el Sistema de Pagos y de Liquidación de Valores, así como desde el punto de vista del aumento en la seguridad, velocidad de las transacciones, costo y ahorro de recursos tanto humanos como de bienes.
29. La economía hondureña en general se ha visto beneficiada por la mejora en el Sistema de Pagos, dada la mayor confiabilidad que tiene debido al uso de los nuevos mecanismos de pagos, de subasta de títulos valores y subasta de divisas.



## ANEXO C

### LECCIONES APRENDIDAS

1. La actualización y mejora del marco regulatorio permite enfocar en mejor forma las acciones y los recursos para efectuar un efectivo proceso de supervisión e intervención en instituciones con alto riesgo.
2. La atención a los riesgos sistémicos debe hacerse en coordinación con todas las entidades que conforman la Red de Seguridad Financiera y apoyarse en indicadores de alerta temprana, para actuar en forma preventiva y no reactiva ante una eventual crisis sistémica.
3. El conocer de las debilidades de la Ley y de las normativa vigente, fue un aprendizaje que permite actuar para buscar mecanismos alternos de orientación al sistema asegurador como de los funcionarios de la Superintendencia de Seguros y Pensiones, manteniendo el monitoreo continuo de la solvencia y de las reservas de las instituciones bajo los mecanismos actuales de regulación.
4. Con las normas prudenciales del Reglamento sobre Constitución de Reservas Técnicas, Reglamento del Margen de Solvencia y del Reglamento de Inversiones para la supervisión de las instituciones de seguros, consideramos que fue un aprendizaje continuo y compartido con las instituciones de seguros, al mantener mecanismos de regulación que le permitieran a la institución cuantificar sus riesgos y a la Superintendencia de Seguros y Pensiones a monitorear las operaciones realizadas por estas.
5. Los planes de adquisiciones al inicio del proyecto y durante un buen tiempo de ejecución del mismo, fueron muy ambiciosos en función de la inexperiencia que se tenía en la ejecución de los procesos; sin embargo, a partir de 2010 al 2012 por las lecciones aprendidas y la curva de aprendizaje más el apoyo decidido de las autoridades superiores, se replanteo un PAC realista de conformidad con los objetivos del convenio de crédito.
6. Es indispensable que para una buena ejecución de los proyectos, todo su personal, debe tener los conocimientos y experiencia en gestión de proyectos; con esto se evita retrasos en los procesos y por ende en la ejecución de los mismos.
7. Todo el personal de la UCP independientemente de su forma de contratación o financiamiento debe tener una supervisión y evaluación continua de desempeño, y sus recontrataciones deben ser al menos de 12 meses y no por periodos menores, pues con esto se evita crear incertidumbre e inestabilidad laboral.
8. El acompañamiento y empoderamiento de las contrapartes técnicas desde la etapa de inicio hasta la etapa de cierre de los contratos en cada uno de los procesos, es un aspecto fundamental para lograr los objetivos propuestos.
9. Los manuales operativos de los proyectos deben ser revisados y de ser necesario modificados al menos una vez al año, a efecto de irlos adaptando a la dinámica administrativa, financiera, operativa y contable, en base a las mejores práctica.
10. Durante la ejecución del Proyecto se tuvo cuatro (4) cambios de Presidente del país, seis (6) cambios de autoridades tanto en la CNBS como en el BCH, Cinco (5) Coordinadores de la UCP, cinco (5) oficiales de Adquisiciones de la UCP, por parte del BM, cuatro (4) Task Manager y Seis (6) Especialistas de Adquisiciones. Esta altísima rotación de

personal se constituyó en un fuerte obstáculo para el acelerado avance en la ejecución de los Planes de Adquisiciones, ya que cada cambio tenía una nueva visión del Proyecto y se hacían las modificaciones respectivas; no obstante a lo anterior, es evidente que una adecuada coordinación, seguimiento y apoyo institucional e interinstitucional, tal y como sucedió durante el período de gobierno 2010 al 2013, fue un factor preponderante para impulsar en forma definitiva las actividades del Proyecto y lograr una ejecución final del 99% de los recursos aprobados.

11. La pausa obligatoria que se originó por los acontecimientos del año 2009, más los tiempos de aprobación por parte del Banco Mundial en alguno de los procesos más importantes que se ejecutaron en el Proyecto, así como también la demora en la aprobación de las enmiendas al convenio de crédito, provocaron atrasos en los primeros cinco años de ejecución del proyecto.
12. Uno de los aprendizajes más importantes durante la ejecución del Proyecto fue la necesaria evaluación y planificación previa de los recursos humanos y tecnológicos con que cuenta una institución, a fin de determinar cuántos proyectos es capaz de ejecutar en forma simultánea, junto a las además tareas rutinarias que se desempeñan.
13. Considerando que la simultaneidad de los proyectos fue una de las principales causas de problemas en el proceso de implementación, se ha establecido en el BCH y en la CNBS, una metodología de priorización de proyectos, tomando en cuenta la disponibilidad de recursos monetarios y humanos, así como también por la importancia en el cumplimiento de los objetivos institucionales, entre otros.

## **B) Borrower comments to this ICR:**

The borrower sent the following general comments on the ICR:

From: Fernando Neda <FNeda@cnbs.gov.hn>  
To: "jbuchenau@worldbank.org" <jbuchenau@worldbank.org>  
Date: 08/27/2013 07:24 PM  
Subject: INFORME DE CIERRE PROYECTO 3800-HO

Estimado Juan:

Hago referencia a la videoconferencia sostenida con Ustedes esta mañana, en la que participaron representantes del BCH y de la CNBS, donde se nos presentó los principales hallazgos y conclusiones del informe de cierre del Proyecto 3800-HO elaborado por el Banco Mundial.

Tal y como fue manifestado en la videoconferencia, en términos generales los representantes de ambas instituciones han manifestado su conformidad con el contenido de dicho informe, sin perjuicio de unas pequeñas observaciones y comentarios que por aparte se las estamos remitiendo para su consideración.

Por otra parte, estamos esperando la autorización de las autoridades superiores, para remitirles nuestro informe de cierre que conjuntamente con el BCH hemos preparado.

Nuevamente queremos agradecerle por todas las gestiones que en su calidad de Gerente del Proyecto ha venido realizando en los últimos cuatro años, lo que indudablemente ha sido un importante elemento, para que se hayan logrado los resultados obtenidos durante dicho período.

Cordiales saludos

Fernando Neda Brito  
Coordinador Unidad Coordinadora de Proyectos / CNBS

In addition to the general agreement with the content of the ICR expressed above, the borrower provided more specific comments in a separate file, which were incorporated into this ICR. Such comments include:

- Currently, all large payment transactions are carried out through the RTGS. 71% of the number of transactions (covering 94% of the volume of transactions) are submitted electronically, while the remainder, namely of those banks which are not yet participating fully in the RTGS, are recorded manually in the system;
- The borrower asked to revise the wording under Section 4 “Assessment of Risk to Development Outcome” to reflect that the high risk for the outcome in the area of AML is due to the lack of follow-up on suspicious transactions by the Prosecutor’s Office and the judicial branch, and to make clear that the FIU is operating properly.
- Under the Section “Lessons Learned”, , the borrower requested to include that some of the project’s activities, such as the modernization of the payments system, require the simultaneous implementation of legal, technical and institutional reforms to be successful and that such reforms therefore cannot be simplified. The borrower stressed in this context the importance of capacity building to enable implementing agencies to address these issues properly.
- Some dates in the text, and data on the relative participation of the Finance Companies in Annex 5 were inaccurate and have been corrected.

## **Annex 11. List of Supporting Documents**

1. Project Appraisal Document
2. Project Information Document
3. Integrated Safeguards Data Sheet
4. Credit Agreement
5. ISRs from 2003 – 2013
6. Miscellaneous project documents (filed in WB Docs)