

Public Disclosure Authorized

No. E 157

FILE COPY

67082

RETURN TO
REPORTS DESK
WITHIN
ONE WEEK

This report is not to be published nor may
it be quoted as representing the Bank's views.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

Public Disclosure Authorized

REPORT ON THE MISSION TO HONDURAS

May 15, 1951

Economic Department
Prepared by: Vittorio Marrama

TABLE OF CONTENTS

	<u>Page</u>
I. THE HONDURAN ECONOMY	1
II. WORK OF THE IBRD MISSION	2
III. ESTABLISHMENT OF THE BNF	3
1. The Law of the Banco Nacional de Fomento (BNF)	3
2. Credit Policies	4
3. Development Activities	4
4. Financing of the BNF	5
IV. OPERATIONS OF THE BNF	5
1. Internal Economy of Honduras	5
(a) Finances	5
(b) Occupational Distribution	6
(c) National Income	6
2. Credit Requirements of the Small Farmer	6
3. Distribution of BNF Funds	7
4. Rates of Interest	9
5. Credit Brigades	10
V. ECONOMIC DEVELOPMENT AND THE BNF	11
1. BNF Economic Development Policy for 1951	11
2. Long-Range Development Plans of the BNF	14
(a) Roads	15
(b) Immigration	16
(c) Power Facilities	16
(d) Cooperatives	17
(e) Fiscal Reform	17
VI. RESULTS OF THE MISSION	18

HONDURAS

Essential Statistics

Population (1950)	1.5 million
National Income (1950)	200 million lempiras
Index of Agricultural Production 1947-48 (1936-37 = 100)	(estimate)
Excluding bananas	210
Including bananas	145
Index Value of Sales of Principal Industries 1947-48 (1943-44 = 100)	204
Exports (1948-49)	85.9 million lempiras ^{1/}
Bananas (1948-49)	58.6 " "
Silver	6.6 " "
Lumber	5.2 " "
Coffee	2.8 " "
Abaca	2.5 " "
Gold	1.4 " "
Imports (1948-49)	67.9 " "
International Reserves (December 1950)	36.6 " "
Money Supply (December 1950)	46.4 " "
Budget Receipts (1949-50)	32.4 " "
Budget Expenditures (1949-50)	32.1 " "
Outstanding Foreign Debt (issue 1950)	1.12 " "
Index Wholesale Prices December 1950 (1938-39 = 100)	355.9 " "

Currency Equivalents:

U.S. \$1	=	Lempira 2
Lempira 1	=	U.S. \$0.50
Lempira 1 million	=	U.S. \$500,000

^{1/} Including valuation adjustment for banana exports.

REPORT ON THE MISSION TO HONDURAS

I. The Honduran Economy

Honduras is a country with an area of 150,000 square kilometers and a population of 1.5 million. The terrain is mountainous, except on the North Coast, where the banana plantations of United Fruit and Standard Fruit are located. The population in the interior lives in numerous separated valleys, which are interconnected, if at all, by very poor highways. The Honduran people are mostly "mestizo" (90% of the total); the majority - 63% according to a recent estimate - is illiterate.

About 85% of the Honduran working population is occupied in agricultural pursuits. Corn is the basic food of the population, but kaffir corn (maicillo), beans, rice, yuccas, bananas, plantains and other vegetable products are also important. All these products are locally grown and traded; lack of good roads makes it difficult to sell them to outside markets. The principal export crops are bananas (entirely in the hands of the fruit companies), coffee, coconut, tobacco and abaca. The livestock population is comparatively large, with a predominance of cattle and hogs. A substantial number of cattle are exported.

The national income of Honduras has been roughly estimated at 200 million lempiras equivalent to about 135 lempiras per capita, an amount which is very low even if compared with other underdeveloped countries.

From the point of view of economic geography, Honduras can be divided into three zones: the North Coast with its banana plantations, the interior with an economy largely based on subsistence crops, and the territory contiguous to El Salvador which grows both subsistence and commercial crops (coffee). This division into zones is important in the Honduran economy since the three zones are, to a considerable extent, economically independent from one another. The North Coast is centered on a banana economy and is relatively the most prosperous of the three zones. The interior lives at a near subsistence level, almost completely detached from the other zones for lack of adequate roads. The zone contiguous to El Salvador is in many respects integrated in the Salvadorean economy, El Salvador being the most convenient outlet for Honduran products both as a consumption market and as a channel to international markets.

The economic disunity of Honduras is the result of a complete lack of coordinated economic development in the past. Tegucigalpa, as the capital of the Republic and the residence of the Government, has never performed the function of coordinating and promoting economic development so that a focal point for a proper integration of the national economy has never existed. While the interior remained at an economic standstill, in the other two zones dynamic forces were at work. The operations of the fruit companies and the growth of the neighboring Salvadorean economy materially helped the development of the two zones located north and southwest. However, part of the economic benefits accrue to the fruit companies and the Salvadorean economy rather than directly to Honduras. All in all, the

three zones of Honduras are poor, although they are poor in a different degree.

Only a strong and coordinated movement towards economic development can unite the country economically; there is no doubt that such a movement must be undertaken by the Central Government in Tegucigalpa. Honduras has recently taken three important steps in this direction. They are:

- (a) the creation of a Central Bank;
- (b) the establishment of a National Development Bank; and
- (c) the introduction of an income tax.

The Honduran Government requested IBRD to send a technical mission to help in the organization and determination of the policy of the new Development Bank (Banco Nacional de Fomento), soon after its establishment was approved by the National Congress (February 17, 1950). The writer was assigned to the Honduran Government to "serve as an advisor to the newly-established Banco Nacional de Fomento to assist in formulating development policies and programs."

The work in Honduras started on April 25, 1950, and ended on December 31, 1950. The most important phases of this work, together with the underlying issues, will be described in the following pages.

II. Work of the IBRD Mission

The first two months of the mission in Honduras were spent primarily in establishing contacts with public officials, bankers, merchants, engineers, etc., in collecting material and statistical information on the Honduran economy and in the practical organization of the new Development Bank, which was expected to begin operating on July 1st. Visits to different regions of Honduras were also made. Both visits and talks proved to be useful in getting a firsthand knowledge of the economic conditions of the country as well as an insight into its development problems.

The mission's main concern was with the practical organization of the new Banco Nacional de Fomento (BNF). In carrying out this objective, the Bank representative cooperated with a member of the Pan American Union and two Salvadorean experts. The work consisted primarily in writing the by-laws of the BNF and in setting up the various sections of the Bank, such as the section for the analysis of loan applications, the accounting and legal sections, etc.

During the first period of the work in Honduras, other problems arose and had to be dealt with, including some technical aspects of the foreign debt of Honduras and the distribution of the capital of the new

Bank between the Credit and the Development Departments.

The preliminary phase of the work in Honduras terminated with the inauguration of the BNF on July 1. After that, the problem of determining the policy of the new Bank was largely in the hands of the Technical Division, a semi-independent branch of the BNF established to study and advise the management of the Bank on matters of general policy.

This problem was approached along three lines: first the problem of credit policy was studied; then the Division worked on the general policy of economic development to be carried out by the Government with the technical assistance of the BNF; and finally the development policy of the Bank itself was taken up. This third step was given the lowest priority since the Bank's development operations were not scheduled to begin until January 1, 1951.

The Government was brought into these discussions as early as possible because the Technical Division constantly attempted to emphasize that the Government was responsible for economic development, and that the creation of two new State Banks (the Central Bank was also inaugurated on July 1) did not by itself solve the problem of development. It was realized that there were certain developmental activities (public utilities, highways, education, health, etc.) which neither the Central Bank nor the Development Bank could perform, because financially and functionally they fell within the realm of government activities.

III. Establishment of the BNF

1. The Law of the Banco Nacional de Fomento (BNF)

According to the Law, the BNF is divided into two departments, the Department of Credit and Operations and the Department of Development. These are actually two different types of institutions: a credit service designed to provide banking facilities to those parts of the country which either never had such facilities before or required more of them, and a development office to perform various types of non-banking development activities, such as the establishment and promotion of research and experimental services, the importation, exportation, purchase, sale, warehousing, etc. of capital goods and finished products, etc. The distinction between the two departments is clear-cut both functionally and financially.

The experiences during the first six months of operation of the BNF, and comparative studies made of similar institutions operating in Central America, have proved that this differentiation between banking and development activities is a useful one. It is also intended to facilitate, after a certain time, the creation of the Department of Development as an entirely independent agency.

In view of the fact that the Technical Division was supposed to occupy a key advisory position in the new Bank and that the law is not

clear enough about the relationships between this Division and the Bank's Credit Department, the principle was established in the by-laws that all matters of policy, both of credit and of development, should pass through the Technical Division, which is directly responsible to the President, and that the Division should assist the Board of Directors and the other internal Committees on all policy matters. This procedure has been rigidly adhered to.

This apparently formal point was emphasized because it was felt that a bank dealing with economic development needed a unit which would constantly coordinate operational policies. Only in this way did it appear possible to avoid a gradual departure from the main objectives of the institution, particularly since it was - and continues to be - subject to pressures from the outside. During this period the IBRD representative took charge of the Technical Division.

2. Credit Policies

The Department of Credit and Operations was established to carry out short, medium and long-term credit operations. The law defines the different kind of loans which can be made as follows: (a) "avio" (crop) loans which are granted for a period not exceeding 18 months and are normally guaranteed by the products to be obtained with the investment of the loan; (b) "refaccionario" (medium-term improvements) loans which are granted for a period not exceeding 4 years (or 7 years in exceptional cases) and are guaranteed usually by chattel or land mortgages; (c) long-term loans, which are granted at terms ranging from 5 to 25 years and must be guaranteed exclusively by mortgages. Two sections have been organized within the Department of Credit and Operations: the Short-Term Section which grants the loans mentioned under (a), and the Medium-and-Long-Term Section which grants the loans mentioned under (b) and (c).

3. Development Activities

The functions of the Department of Development are:

- (a) to provide all or part of the capital for private, public or mixed enterprises, and to buy and guarantee the obligations which such enterprises issue;
- (b) to market stocks and bonds of such enterprises under (a);
- (c) to organize and to participate in the organization and operations of enterprises and institutions related to the purposes of the Bank;
- (d) to establish, sponsor, and direct research institutes and experimental stations, to undertake studies, and grant scholarships;

- (e) to direct projects and development activities for the Government or for third parties;
- (f) to import, export, buy, sell, lease, store and transport machinery, tools, working equipment, seeds, fertilizers and other products;
- (g) to serve as coordinator of the Government's policy of economic development; and
- (h) to act as financial agent of the Government in contracting foreign loans for use in economic development.

4. Financing of the BNF

Upon inauguration of the BNF the government contributed to the capital of the Bank 1.4 million lempiras, which represented the yield of an exchange tax collected over a number of years. Furthermore, the State will allocate to the Bank 15% of the proceeds of the newly established income tax and the receipts from a 10% customs surcharge. In 1950, when income tax was paid only by the United Fruit Company, the proceeds amounted to 487,000 lempiras. In 1951, they are expected to amount to 750,000 to 800,000 lempiras. The proceeds of the custom surcharge are estimated at 58,000 lempiras per month: up to December 31, they had reached a total of approximately 350,000 lempiras.

At the end of 1950, the capital of the Bank was 2.2 million lempiras (see Balance Sheet in Table I). This sum represents slightly more than 1% of the estimated national income and 7% of fiscal expenditures. Besides the previously mentioned allocations by the Government, the BNF can raise funds through collection of deposits (sight, saving and term deposits), rediscount operations with the Central Bank, and bond issues. However, since a private capital market is practically non-existent and is not likely to be created in the near future, it is expected that the BNF will operate, at least for some time, with its own capital and by rediscounting its short-term portfolio with the Central Bank. To date, the Bank has been operating exclusively with its own capital.

IV. Operations of the BNF

1. Internal Economy of Honduras

(a) Finances

The structure of the Honduran credit market at the time of the inauguration of the BNF was as follows: 45% of the portfolio of 21.7 million lempiras held by the private banks operating in Honduras consisted of loans for real estate, construction and purchase; 35% went to loans for commercial activities; and another 10% consisted of personal loans. Only

10% of the portfolio of the private banks consisted of loans for agricultural and industrial activities. Loans were usually guaranteed with mortgage on rural and, preferably, urban properties.

(b) Occupational Distribution

Tentative estimates of the occupational distribution of the Honduras working population indicate that roughly 84% are engaged in agricultural and livestock pursuits, 6% in mining, manufacturing, and handicraft, about 3% in building construction and 7% in services (transportation, banking, government, etc.). Although no statistics are available on the system of land tenure, it is known that the land is fairly well divided into small holdings which very often are part of a larger plot of land legally belonging to the whole local community (ejidos). These ejidos originally were established with the idea of avoiding concentration of land in large properties; apparently they have fulfilled their purpose. There are large landholdings in Honduras as in other Latin American countries, but on the whole small landholdings characterize Honduran agriculture. When one deducts from the total agricultural population the number of workers employed by the fruit companies (probably 10% of the total) and the big and medium-size landowners (roughly another 10%), it appears that approximately 70% of the total working population of Honduras is made up of small farmers.

(c) National Income

No accurate national income estimates are available in Honduras. Preliminary figures are expected to be ready by the middle of this year. For the time being, therefore, it is impossible to evaluate what portion of the total income is produced by small farmers. Sufficient evidence exists, however, to indicate that this portion is very modest indeed, providing bare subsistence levels.

2. Credit Requirements of the Small Farmer

The small farmer has enjoyed practically no credit facilities. The result has been, throughout the years, a severe exploitation of the small producer by the local big landowner or merchant, and not infrequently by large commercial houses. Annual rates of interest of 24% and 36% or even higher have been common with the result that small properties were often lost to the local lender who enjoyed a monopoly position.

Because of his low real income, the small farmer has always been in need of funds to cover his living expenses and his costs of production. Usually he is compelled either to sell his crop in advance or at the harvesting time to the advantage of the local big landowner-merchant who profits by the seasonal decline in prices when he buys the crop at the moment of the harvest. A statistical survey carried out in an important and

representative producing zone of Honduras - the Valley of Comayagua - indicates that the cereal producers who sell their crops at harvest time get 50% of the retail price, and those who sell in advance get only 34%. The local lender gets shares of 22% and 38% respectively, the balance going to transport and retail mark-ups.

In order to help the small farmer, it appears necessary to provide him with an alternative source of funds before and after the harvest. The two most important means to accomplish this seem to be:

- (1) short-term crop loans; and
- (2) storage facilities for the purpose of
 - (a) storing the products,
 - (b) giving credit on these products, or
 - (c) buying the products at established minimum prices.

These devices are complementary. Short-term crop loans without storage facilities would leave the farmer unassisted at the moment of the seasonal decline in prices, storage facilities without short-term crop loans would not benefit those farmers who for the lack of subsistence funds have to sell their crop in advance.

Besides short-term credit and storage facilities, the small farmer needs medium-term improvement loans to increase his long run productivity. Since Honduran agriculture is primitive, high returns per unit of investment are to be expected. Other non-banking development activities, such as extension services, ought to accompany improvement loans but it is important to note that these other means of increasing productivity do not occupy the same order of priority as short-term crop loans and storage facilities.

3. Distribution of BNF Funds

According to the Law, part of the capital of the Bank is allocated automatically to the Credit Department, and another part must be distributed by the Board of Directors between the Credit Department and the Development Department. The part subject to distribution is the 15% coming from income tax proceeds (see p. 5). At the suggestion of the Technical Division, this part has been allocated almost entirely to the Development Department. At the end of December, total available capital was distributed as follows: 1.8 million lempiras to the Credit Department and 0.4 million lempiras to the Development Department.

The Technical Division was confronted with the following problems in connection with the distribution of the funds available for credit

operations: (1) how to distribute them among short, medium and long-term loans; (2) how to distribute them among agricultural, livestock and industrial activities - and in each of these fields, among different sectors. In view of the limited amount of available funds, careful distribution was essential.

The first question was solved by suggesting a greater concentration of funds on short-term operations in order to meet the most urgent needs of the Honduran small producers who require primarily crop and small improvement loans. The Board of Directors of the Bank was advised to distribute the funds as follows: 60% on short-term crop loans and short-term improvement loans, 25% on medium-term improvement loans and 15% on long-term mortgage loans. The suggestion was also based on the necessity of keeping the portfolio of the bank as liquid as possible until some experience has been acquired, and on the advisability of limiting the volume of long-term operations until a larger volume of voluntary savings becomes available.

The second problem, that of the distribution of the funds among different economic activities, was solved by suggesting a larger concentration on agricultural and livestock activities, with 60% going to agriculture and 20% to livestock pursuits. Only 10% was assigned to industrial and other undertakings, leaving another 10% for credit operations such as refinancing of old debts. Among the different activities, a heavier concentration was suggested on those which yield products (coffee, wheat, sugar cane, cotton, cattle and dairy products) which either can be exported or can replace imports. They are also the activities most likely to give higher returns per unit of investment. Promotion of agricultural activities which are exchange-earning or exchange-saving was considered advisable because of the necessity of leaving more room in the foreign exchange budget for greater imports of capital goods for development purposes, and on the advisability of restricting the new Bank in its initial period as a banking institution to those operations which are, on the whole, less risky than those connected with subsistence crops. A maximum limit of 20,000 lempiras for each credit operation was suggested by the Technical Division and accepted by the Board of Directors.

From July 1 to December 31, loans were approved totalling 599,855 lempiras, with an average of 3,100 lempiras for each operation (Table III). Loans actually disbursed amounted to 389,858.52 (Table I). The extensive work done by the Bank in appraising loan applications, the number of which far exceeded the number of loans granted, can be observed in Table III.

This table and others pertaining to loan operations give a somewhat distorted picture because the data include a six months loan of 100,000 lempiras granted to the Compania Azucarera Hondurena for financing its sugar crop. Table VI is especially affected by this loan. If this loan is excluded, the table would show that 40% of the total amount loaned was for small loans of 5,000 lempiras or less. This must be considered quite an achievement considering the short period of operation of the Bank.

A condensed view of the credit operations of the BNF from July 1 to December 31, 1950, is presented in the following table (in thousands of lempiras):

<u>Type of Loans</u>	<u>Approved</u>	<u>Disbursed</u>	<u>Major destination of disbursed loans</u>
Crop loans	262	200	97% Agricultural Livestock
Improvement loans	189	85	93% Agricultural Livestock
Mortgage loans	<u>149</u>	<u>110</u>	<u>82%</u> Refinancing
Total	600	395	75% Agricultural Livestock

In actual operation it developed that the market was pressing particularly for long-term loans for the refinancing of old debts, but the Technical Division soon controlled this pressure by establishing a ceiling and other limitations on such operations. Eventually, the refinancing operations diminished until they disappeared, nevertheless in December the actual distribution of the portfolio was still somewhat distorted compared with the planned one, as a result of the refinancing operation carried on in the first few months (see Table V). There are sound indications that in the following months the actual distribution will gradually approach the planned one.

From the time that the question of refinancing loans arose, the Technical Division endeavored to impress upon the Board of Directors of the BNF that even if a "passive" credit policy was admissible in the initial period of operation, it would not be justified later on. It was argued that an "active" credit policy which would endeavor to channel credit into previously selected fields instead of following the demand of the market, was a necessary condition for the success of a development bank. By now this concept of the "active" credit policy has been accepted by the Directors of the BNF.

4. Rates of Interest

Another important problem in the field of credit policy has been rates of interest. According to the law, the new Central Bank is authorized to establish maximum rates of interest and commissions which the banks may pay or charge for their lending or borrowing operations. Such ceilings were established by a Central Bank resolution of June 29. For the so-called direct credit operations of the BNF in Tegucigalpa the ceilings were 8% interest rate plus 1% commission on long-term mortgage loans, and 6% preferential interest rate for short-term crop loans and medium-term improvement loans. It was made clear at the time of the Central Bank resolution that the BNF would propose a different system of rates of interest to be applied to the credit operations of the local rural agencies of the Bank. This new system of rates for rural or indirect credits was outlined by a

Delegation of the Banco Nacional of Costa Rica in the following weeks. The proposed rates were higher than those for direct credits established by the Central Bank resolution of June 29, the justification being that the administration expenses for rural credit are much higher than those for direct credit.

The Technical Division consistently opposed this system of interest rates, arguing that there was no reason to force down the rates of interest in a market where the operations to be financed primarily by the BNF had usually paid rates of at least 2½% annually. The Division further argued that ceilings established for direct credits were too low considering the current situation of the Honduran credit market, where an average rate of 8% had been the rule for bank loans much less expensive and risky than those of the BNF. It was further pointed out that the low ceilings were bound to cause difficulties in raising additional funds in the money and capital markets. Finally the Division declared that the discrimination between direct and rural credits, if justified for purely administrative reasons, was not justified at all on social and economic grounds. The Technical Division maintained in this connection that one of the fundamental objectives of the BNF was to improve income distribution and that a unified system of interest rates was one of the means to this end. A number of memoranda were prepared by the Technical division on this subject.

The Central Bank, however, decided not to change the ceilings for direct credits and on September 29 maximum rates for rural credits were established as follows: 8% interest rate plus 1% commission on long-term mortgage loans, and 6% interest rate plus 2% commission on short-term crop loans and medium-term improvement loans. A ceiling of 2,000 lempiras was fixed for each rural credit operation.

The Technical Division thereupon suggested to the Board of Directors that the Bank operate at the ceilings, but although this suggestion was accepted, there is no doubt that even at these rates the new Bank will have bigger losses than expected in its initial period of operation in view of the high administrative expenses. The loss for the first six months of operation amounted to 106,000 lempiras (see Table II). Because the BNF is a State Bank, the Technical Division has not been too concerned about these losses, which were in effect a further subsidy to agricultural and livestock undertakings. It is expected that as the volume of operations increases the losses will diminish.

5. Credit Brigades

One of the most interesting aspects of the BNF's work in the credit field has been its efforts to reach the small producers. Since the establishment of a satisfactory network of rural credit agencies would take considerable time, "Credit Brigades" were organized, staffed by Bank personnel, to travel to economically important regions of the country for the purpose of making loans to the small farmers.

During the first four months of operations ending in December, a substantial number of small credits were granted, particularly crop loans. The political impact of these loans was probably even greater than their economic effect. The plan is gradually to convert the Brigades into permanent Local Credit Commissions or Rural Credit Agencies.

The Technical Division has periodically reviewed the credit operations and the composition of the portfolio in order to see whether or not they comply with the recommendations and if not, to urge the Board of Directors to make appropriate changes. In a number of cases the Technical Division was asked to express its opinion upon particular loans which, either because of their nature or their amount, represented a departure from the established rules.

V. Economic Development and the BNF

1. BNF Economic Development Policy for 1951

According to the law, the BNF was scheduled to start its development operations on January 1, 1951. Extensive preparatory work was required from the Technical Division, including obtaining assurances that technical assistance would be forthcoming in the field of agricultural development. Following is a summary of the activities initiated by the Division:

- (1) expediting of negotiations between the Government of Honduras and the Institute of Inter-American Affairs for the establishment of a STICA 1/ service in Honduras;
- (2) arranging with the FAO for a mission of agricultural experts to assist the Bank in its program of agricultural development. The mission was expected to include experts in the following subjects: (a) credit supervision; (b) grain storage facilities; (c) planning for agricultural development; and (d) forestry; and
- (3) preparing a plan of investment for the BNF's Development Fund for 1951.

At the end of December, the Government of Honduras had already entered into final negotiations with the Institute of Inter-American Affairs and the STICA service was expected to be established early in 1951. A contract had been signed with FAO for the services of the necessary agricultural experts.

With regard to the plan of investment of the Development Fund, the Technical Division suggested two exploratory missions by the BNF to neighboring countries to study the organization and policy of more advanced

1/ Servicio Tecnica Internacional Cooperativa Agricola.

development institutions. The two missions, one to Guatemala (INFOP) and the other to Costa Rica (Banco Nacional and Consejo Nacional de la Produccion) took place in the first half of August and November, respectively.

On the basis of the observations made during those missions and of the studies carried out meanwhile (the result of which has been largely summarized in the section of this report dealing with credit policy and operations), the Technical Division produced a memorandum containing detailed suggestions on how to distribute in 1951 the funds available for development activities. A slightly revised edition of that memorandum was approved by the Board of Directors in November.

The plan prepared by the Technical Division is based on two fundamental principles:

- (a) that the development work of the new Bank should center upon the agricultural and livestock activities of the country, with particular emphasis on fostering subsistence crops; and
- (b) that during 1951 the Bank should permit a certain amount of experimentation in its development projects, reserving until later, possibly in 1952, concentration on those fields which experience will indicate are the most profitable for speeding up the process of economic development.

The funds to be distributed in 1951 among different development activities amount to 650,000 lempiras, which include a balance of 425,000 lempiras brought forward from 1950 and an estimated 225,000 lempiras to be added during 1951. Following the suggestions of the Technical Division, the funds have been allocated as follows:

(1) Administrative expenses of the Development Department and additions to permanent assets	150,520
(2) Studies for the general plan of economic development and for the plan of agricultural development	41,600
(3) Investments in "indirect" development	338,000
(4) Scholarships and studies for investment of direct development	25,000
(5) Investments of "direct" development	<u>94,880</u>
Total	650,000

The expenditures under (1) include administrative expenses and expenses for office equipment, for technical instruments and for a library. The expenditures under (2) include those which will arise in connection

with the foreign experts requested from FAO and from the U.S. Government, as part of the Point IV program.

Of particular importance are the expenditures under (3) which in the opinion of the Technical Division will be basic to the Bank's future activities in the field of economic development. The investments in this sector have been distributed as follows:

(a) Pilot-project for different experimental activities (primarily subsistence crops and livestock)	90,000
(b) Grain storage for corn and beans in the valley of Comayagua (80 km. Northwest of Tegucigalpa)	60,000
(c) Two warehouses in coffee producing zones (Marcala and El Paraiso)	100,000
(d) General warehouse in Tegucigalpa	50,000
(e) Establishment of coffee nurseries	20,000
(f) Veterinary service	15,000
(g) Publications and other means of instruction	<u>3,000</u>
Total	338,000

It will be noticed that 62% of the available funds in this section have been allocated to the establishment and equipment of storage facilities.

The expenditures under (4) include the costs of scholarships for training of Hondurans abroad in agriculture and stockbreeding, and the cost of studies to be made by experts on temporary assignment on activities in which the Bank may directly participate, such as textile production, cement, etc.

The expenditures under (5) cover direct investments of the Bank in industrial activities which are expected to promote the economic progress of the country. The Technical Division has pointed out, however, that the sum allocated to these expenditures must be considered as flexible, in the sense that it could be transferred, if necessary, to supplement other expenditures included elsewhere in the program. In the opinion of the Technical Division, it would be premature for the Bank to start investment programs of this nature which would require substantial funds not yet available to the Bank.

The purpose of the plan of investments prepared by the Technical Division is to test the feasibility of attaining two main objectives of development: (1) a direct increase in the productivity of the farmer and stockbreeder; (2) elimination of the local "marketing and credit monopolies" which profit by the lack of storage facilities and rural credit.

As part of this investment plan, the Technical Division suggested that economic and statistical investigations be carried out in those zones in which the Bank will concentrate activities during 1951 and in subsequent years. A model of such investigations has been set up in a study prepared by the Technical Division (in cooperation with statistical experts) on the conditions of production and marketing of cereals in the valley of Comayagua, where a grain storage, together with a rural credit agency, is to be established according to the current investment plan. This model will be followed by other investigations of similar character, such as those to be undertaken in the two coffee producing zones where the plan of investment will probably include the construction of warehouses with facilities for processing coffee beans.

It is not possible at the moment to predict how the development activities for which the BNF is directly responsible will evolve, but the Technical Division at least has attempted to lay the groundwork - through its planning operations - for the successful undertaking of these activities.

Another noteworthy action taken by the Technical Division was in connection with the use of reserves in excess of foreseeable commercial requirements. The Technical Division suggested assigning a part of the available sum for purchases of agricultural machinery and implements. By the end of December, the BNF had ready a list of agricultural machinery and implements to import from abroad for early approval by the Board of Directors of the Bank and by the Central Bank. The planned expenditure amounts to 1.5 million lempiras.

2. Long-Range Development Plans of the BNF

The Technical Division very early raised the problem of the general economic development of Honduras. Since nothing or almost nothing had been done previously in this field, the Technical Division pointed out that the creation of the two new State Banks (the BNF and the Central Bank) offered a good opportunity to start working systematically toward general economic development; that the establishment of the two Banks was to be considered as the first step toward an active economic development policy and not the final one; and that the work of the Banks could be successful only if complemented by a well coordinated and decisive effort of the Government toward the same objectives.

Since the law of the BNF states that the Bank may "serve as coordinator of the Government's policy of economic development," the Technical Division suggested the following steps:

- (1) to concentrate the function of studying and planning for economic development in the hands of the Development Department of the BNF;
- (2) to start, as soon as possible, statistical investigations in order to learn the relevant economic magnitudes such as

national income, capital formation, etc., which are indispensable in the preparation of estimates regarding the investment capacity of the country;

- (3) to establish the principle of a General Development Plan which should be prepared in the fiscal year 1951-52 on the basis of the statistical investigations mentioned under (2) and put into execution in the fiscal year 1952-53;
- (4) to initiate immediately planning studies on those matters which, in the opinion of the Technical Division, will occupy high priority in any future general development plan.

The Government accepted the suggestions under (1) and (2). Consequently, soon after the employment of a statistical expert from El Salvador, the statistical investigations were started (September) and a thorough functional and financial reorganization of the General Statistical Office was undertaken. At the end of December both the statistical investigations and the reorganization of the Statistical Office were well under way. It is expected that preliminary statistical investigations will be ready by the middle of 1951.

On points (3) and (4), the Technical Division suggested focusing efforts upon the following matters: highways, immigration for agricultural colonization and hydroelectric facilities. These fields of immediate action were selected on the basis of studies made by the International Monetary Fund Mission in 1949 and of independent investigations made by the Bank mission which revealed that the major bottlenecks in the economic development of Honduras are the lack of an adequate network of roads, the low population density in some regions and the lack of electric power both for consumption and industrial uses.

(a) Roads

Honduras has almost 1,300 kilometers of all types of roads which, compared to the area of the country, gives a coefficient of 0.008 kilometers per square kilometer. By comparison the density of roads in other Central American republics is 0.060 in El Salvador, 0.095 in Guatemala and 0.020 in Costa Rica. In Honduras no road is paved and probably more than 40% are in very bad condition. It is clear that economic development depends to a large extent upon the construction of an adequate network of highways over a reasonably short period of time.

Since the work of the BNF in the field of the general economic development was proceeding at a satisfactory pace, the Technical Division decided to accelerate the program, particularly in regard to the activities of the Highway Commission. In order to start the execution of the highway program in the fiscal year 1951-52 and in view of the preliminary results

of the investigations by the Commission the Technical Division suggested that action be taken (1) to obtain an allocation of about three million lempiras out of existing revenues, in addition to the 3.5 million already budgeted for highway construction; (2) to propose the early reform of two direct taxes (the tax on rural and urban properties and the inheritance tax) for raising additional funds for highway construction; (3) to shift the control of the funds from the Highway Treasury (a government agency) to the Development Department of the BNF under the supervision of the Highway Commission. A letter to the President of the Republic to this effect was drafted for the Highway Commission.

Towards the end of the year, it became clear that the Government was not contemplating any action on the proposal. Although the Technical Division strongly emphasized the urgency of the highway program, for various reasons the Directors of the Bank were not agreeable to taking a strong stand against the Government so that for the time being the proposal was put aside. Shortly afterwards the Technical Division suggested, in full agreement with the Central Bank, another line of action to expedite the highway program, namely, the utilization of part of the international monetary reserves of Honduras (which are far beyond those required if a deterioration of the balance of payments should take place) for purchasing highway machinery and implements. Honduran international liquid reserves amount to 36 million lempiras or \$18 million, which is 80% of the money supply. At the end of December the new proposal was still under consideration by the Government.

(b) Immigration

With regard to the suggested immigration scheme, one must take into account that the average density of population in Honduras is (according to the last census) 10 inhabitants per square kilometer compared with densities of 58.0 in El Salvador, 32.8 in Guatemala and 20.0 in Costa Rica. Moreover, a comparison of the census of 1945 with that of 1930 shows that substantial movements of population from the interior toward the North Coast and the region of the capital took place during that 15-year period, with the result that some regions of the interior, potentially rich in resources, are now underpopulated. It is believed that agricultural colonization of those areas by groups of foreign immigrants with their higher technical experience may result in a net benefit to the regions themselves and indirectly to the entire Honduran economy.

(c) Power Facilities

In a study on the Rio Lindo power project in Honduras, prepared by the IBRD in 1949, it was pointed out that in 1945 the total installed power capacity in Honduras amounted to 4,500 kw with a production of 15 million kwh. Of this capacity, about 70% belonged to the United Fruit Company. The situation has not changed appreciably since 1945 with the result that both the light and power rates are very high in Tegucigalpa and other

important towns. In such circumstances, the use of power for industry and private consumption is practically precluded to large sectors of the economy. At some stage of its economic development, Honduras has to face the problem of power supply if real progress is to be achieved.

The Technical Division proposed the creation of three Permanent Commissions, with the assistance of three foreign experts, to prepare studies and plans on the problems of highways, immigration and the hydroelectric resources of Honduras. Recommendations were accepted by the Board of Directors of the BNF and by the Government, and the Commissions started their work in September 1950. Technical aid was requested from the IBRD which decided, however, that the assistance required was of a character that would be better furnished under the Point Four program of the U.S. Government, to whom the request was transmitted. At the end of December, the work of the Honduran Commissions was well under way, but no definite negotiations had yet taken place in respect to the foreign experts.

(d) Cooperatives

Another important activity in the field of general development carried out by the Technical Division was the launching of a campaign for the establishment of cooperatives. Since there is no legislation in Honduras adequately dealing with cooperatives, the staff of the Technical Division prepared a bill for submission to the National Congress. A member of the staff participated in the Regional Seminar held by the Pan American Union last November in El Salvador in order to get the advice of experts on the subject of cooperatives. At the end of December, the bill prepared by the Technical Division was being reviewed by a Special Commission of the Board of Directors of the BNF, and it is expected that the bill will be presented in the current session of the National Congress.

(e) Fiscal Reform

Since a General Development Plan of the nature described would involve heavy additional public expenditures, the Technical Division soon raised the question of a fiscal reform. The Division recommended that this reform should take place during 1951, possibly with the technical assistance of an international organization. It was pointed out by the Technical Division that the reform should be comprehensive, taking into account all aspects of taxation inclusive of state taxes, municipal taxes, tariffs and tax exemptions, and that the tax system must be geared as far as possible to ability to pay. Until last year, fiscal revenues were derived almost entirely from indirect taxation thereby discriminating against the lowest income groups. With the introduction of the new income tax last year an important step was taken toward a more balanced fiscal structure, but the tax system still is largely regressive. In view of the necessity of raising additional funds, one has to envisage an increase in indirect taxes equitably distributed, as well as an early revision of the existing direct taxes such as the tax on urban and rural properties and commercial establishments and the tax on inheritances, which at present yield in the aggregate

less than one per cent of total revenues.

A major fiscal reform was recommended to shift the tax burden to middle and high income groups, although the Technical Division was aware of the potentially unfavorable effects which such a redistribution of the tax burden might have on the volume of savings. It was felt, however, that the potential repercussions on the level of savings could be disregarded. In Honduras' present state of economic development it seems more important to devote resources to the formation of social overhead capital such as roads, port facilities, schools, etc., than to the accumulation of capital in the hands of private entrepreneurs who, in accordance with local tradition, invest the major proportion of their savings in landed property or hold them idle in the form of foreign balances. The suggested fiscal reform was favorably received by the BNF, but was neither accepted nor rejected by the Government. It has become apparent that the Government is not yet ready to give the matter serious consideration.

VI. Results of the Mission

While in Honduras, the writer was also teaching at the National University. A new "Department of Economic Sciences" was established in May 1950 and the writer taught a course on "Principles of Economics" to a class which was attended by 108 students representing a cross-section of the Honduran population. Classes were held four times a week in the evening. The course was organized to emphasize the fundamental concepts of national income and its composition and to point towards problems of economic development.

The work at the University also included the preparation of a plan of studies for the new economic department. Although this plan was prepared independently, it closely resembled the plan suggested by the San Carlos University of Guatemala for the unification of economic studies in Central America.

There are reasons to believe that the results of the Bank mission in Honduras have been satisfactory to such an extent as to justify the consideration of missions of a similar character to our underdeveloped member countries, particularly the smaller ones.

It is of direct interest to the Bank that the Honduran Government, upon the suggestion of the BNF and the Central Bank, authorized the International Bank to utilize without any limitation the 18% of the Honduran quota. The Government also decided to invest \$1 million into IBRD bonds.

Possibly the most important achievement of the mission has been the creation in the BNF and outside the Bank (particularly in the University) of a group of persons who understand the problems of economic development of their country and know what measures are to be taken in dealing with them. This achievement can be credited to the fact that the IBRD mission remained in Honduras eight months, giving the writer ample opportunity to

familiarize himself with the country, its people and its problems.

The fact that the BNF was on a sound working basis by the end of December is also a result of the long and frequent discussions and planning sessions between the Bank representative and the directors of the BNF. It is doubtful whether similar results can be obtained in a shorter period of time.

TABLE I

HONDURAS

Balance Sheet of BNF as of December 31, 1950

ASSETS

Cash		L 1,676,743.81
Foreign Exchange		24,461.94
Loans and Discounts		389,858.52
Short-term crop with untransferred security and discounts	L 144,025.57	
Short-term crop with mortgage security	52,410.00	
Medium-term improvement with mortgage security	84,304.91	
Long-term mortgage	<u>109,118.04</u>	
Deferred Accounts		130,997.19
Bank Equipment	49,458.67	
Minus Reserve for Amortization	<u>5,521.18</u>	43,937.49
Other Assets		<u>2,715.85</u>
	Total Assets	<u>L 2,268,714.80</u>

LIABILITIES

Deposits		L 31,460.17
Sight	L 6,377.28	
Saving	1,158.50	
Restricted	<u>23,924.39</u>	
Deferred Accounts		18.45
Other Liabilities		3,130.95
Capital		<u>2,234,105.23</u>
	Total Liabilities	<u>L 2,268,714.80</u>

TABLE II

HONDURAS

Statement of Profit and Loss of BNF as of December 31, 1950

Expenditures

Salaries and wages		L 76,706.39
Board of Directors		5,690.30
General expenditures		
Rent	L 4,700.00	
Office equipment	3,830.93	
Communications	41.18	
Per diem	8,815.84	
Maintenance and repair of vehicles	1,159.80	
Maintenance and repair of real estate	27.50	
Maintenance and repair of office equipment	51.35	
Public relations and publications	345.00	
Social security for employees	192.00	
Representation expenses	554.00	
Depreciation	5,521.18	
Others	<u>2,987.22</u>	
Total general expenditures		28,226.50
Interests		<u>66.45</u>
<u>TOTAL</u>		<u>L 110,689.64</u>

Receipts

Interests	L 2,698.83	
Commissions	13.10	
Exchange Profits	419.61	
Other	<u>31.78</u>	
BALANCE	L 4,163.32	
	<u>106,526.32</u>	
<u>TOTAL</u>		<u>L 110,689.64</u>

TABLE III

HONDURAS

Movement of Loan Applications to BNF from July 1 to
December 31, 1950

	<u>Number of Applications</u>	<u>Total L</u>
Loan Applications Approved	193	599,855.00
Loan Applications Rejected	67	625,815.00
Loan Applications Withdrawn	46	251,100.00
Loan Applications Pending Action	6	85,100.00
Loan Applications in Process	<u>110</u>	<u>445,090.00</u>
TOTAL	<u>422</u>	<u>2,006,960.00</u>

TABLE IV

HONDURAS

Approved Loans of BNF as of December 31, 1950,
Classified by Type

<u>Type of Loan</u>	<u>Number of Loans</u>	<u>Amount of Loans</u>	<u>% of Total</u>
Long-term mortgage loans	21	L 148,680.00	25.8
Medium-term improvement loans	56	189,550.00	31.6
Short-term crop loans	<u>116</u>	<u>261,625.00</u>	<u>43.6</u>
TOTAL	<u>193</u>	<u>L 599,855.00</u>	<u>100.0</u>

TABLE V

HONDURAS

Approved Loans of BNF as of December 31, 1950,
Classified by Purpose

<u>No.</u>	<u>Destination</u>	<u>Amount</u>	<u>% of Total</u>
1	Refinancing	L 124,360.00	20.73
2	Purchase of properties	20,500.00	3.42
3	Permanent improvement	53,405.00	8.90
4	Agricultural machinery and implements	54,615.00	9.11
5	Reconditioning of pasture grounds	3,900.00	0.65
6	Purchase of working animals	3,800.00	0.63
7	Purchase of dairy cattle	34,800.00	5.80
8	Purchase of beef cattle	52,850.00	8.81
9	Coffee crop	63,620.00	10.61
10	Sugar cane crop	137,270.00	22.88
11	Subsistence crops	22,935.00	3.82
12	Industry	<u>27,800.00</u>	<u>4.64</u>
	TOTAL	<u>L 599,855.00</u>	<u>100.00</u>

TABLE VI

HONDURAS

Approved Loans of BNF as of December 31, 1950,
Classified by Amount

<u>Amount of Loans</u>			<u>No. of Loans</u>	<u>Amount ^{1/} (lempiras)</u>	
From L	25.00	to L	100.00	25	1,562
	101.00		500.00	58	17,400
	501.00		1,000.00	18	13,500
	1,001.00		2,000.00	32	48,000
	2,001.00		5,000.00	32	112,000
	5,001.00		10,000.00	15	112,500
	10,001.00		15,000.00	7	87,500
	15,001.00		20,000.00	4	70,000
	20,000.00	or more		<u>2</u>	<u>137,392</u>
				<u>193</u>	<u>599,855</u>

^{1/} This column has been statistically calculated. The error has been corrected in the last figure, that is the one which refers to loans of 20,000 lempiras or more.

TABLE VII

HONDURAS

Disbursed Crop Loans of BNF as of December 31, 1950,
Classified by Purpose

	<u>With untransferred security</u>	<u>With mortgage security</u>	<u>Sub-Total</u>	<u>Total</u>	<u>% of Total</u>
<u>AGRICULTURE</u>					
Coffee	21,735.00	7,950.00	29,685.00		
Sugar	114,845.00	4,160.00	119,005.00		
Corn	685.00	6,300.00	6,985.00		
Beans		3,500.00	3,500.00		
Sub-Total	137,265.00	21,910.00	159,175.00	159,175.00	79.68
<u>LIVESTOCK</u>					
Beef cattle	2,000.00	30,000.00	32,000.00		
Dairy cattle	3,100.00	200.00	3,300.00		
Sub-Total	5,100.00	30,200.00	35,300.00	35,300.00	17.67
<u>INDUSTRIAL</u>					
Wood boxes	2,000.00		2,000.00		
Turpentine		1,800.00	1,800.00		
Tanning		1,500.00	1,500.00		
Sub-Total	2,000.00	3,300.00	5,300.00	5,300.00	2.65
TOTAL	<u>144,365.00</u>	<u>55,410.00</u>	<u>199,775.00</u>	<u>199,775.00</u>	<u>100.0</u>

TABLE VIII

HONDURAS

Disbursed Improvement Loans of BNF as of December 31, 1950,
Classified by Purpose

	<u>Lempiras</u>	<u>% of Total</u>
<u>AGRICULTURE</u>		
Coffee	8,240.00	
Sugar cane	2,125.00	
Corn	1,000.00	
Potatoes	500.00	
Drainage and irrigation	200.00	
Installations	4,100.00	
Purchase of working animals	2,230.00	
Machinery and implements	33,105.00	
Fences	1,950.00	
Refinancing	<u>2,700.00</u>	
Sub-Total	56,150.00	65.71
<u>LIVESTOCK</u>		
Dairy cattle	9,400.00	
Machinery and implements	2,200.00	
Installations	5,500.00	
Pasture	3,280.00	
Fences	<u>2,520.00</u>	
Sub-Total	22,900.00	26.80
<u>OTHER</u>		
Refinancing	2,000.00	
Fences n.e.s.	3,400.00	
Constructive	<u>1,000.00</u>	
Sub-Total	<u>6,400.00</u>	<u>7.49</u>
TOTAL	<u>85,450.00</u>	<u>100.0</u>

TABLE IX

HONDURAS

Disbursed Mortgage Loans of BNF as of December 31, 1950,
Classified by Purpose

	<u>Lempiras</u>	<u>% of Total</u>
Refinancing	90,300.00	82.24
Construction of rural houses	4,500.00	4.10
Purchase of rural properties	<u>15,000.00</u>	<u>13.66</u>
TOTAL	<u>109,800.00</u>	<u>100.0</u>