# Debt Management Performance Assessment (DeMPA)

## HONDURAS

## June 2021

The DeMPA is a methodology for assessing public debt management performance through a comprehensive set of indicators spanning the full range of government debt management functions. The DeMPA tool presents the 14 debt performance indicators along with a scoring methodology. The DeMPA tool is complemented by a guide that provides supplemental information for the use of the indicators.

For additional information on the World Bank's Debt Management Technical Assistance Program, including more on the DeMPA Tool, please visit our website at: http://www.worldbank.org/debt

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## Glossary

| | |
|---|---|
| BC | Business Continuity |
| BCH | Central Bank of Honduras (*Banco Central de Honduras)* |
| CABEI | Central American Bank for Economic Integration |
| CCP | Public Credit Commission *(Comisión de Crédito Público*) |
| CG | Central Government (*Gobierno Central*) |
| CL | Contingent Liabilities |
| CMNV | Securities Negotiation Contract *(Contrato Marco de Negociación de Valores)* |
| CPI | Consumer Price Index |
| CSD | Central Securities Depository |
| DCC | Quality Control Department (within the Back Office) *(Departamento de Control de Calidad)* |
| DGDR | Debt and Risk Management Department *(Departamento de Gestión de Deuda y Riesgo)* |
| DeMPA | Debt Management Performance Assessment |
| DFE | External Financing Department *(Departamento de Financiamiento Externo)* |
| DGCP | General Directorate of Public Credit (*Dirección General de Crédito Publico)* |
| DGIP | General Directorate of Public Investment (*Dirección General de Inversión Pública)* |
| DGPMF | General Directorate of Macro-Fiscal Policy (*Dirección General de Política Macro-Fiscal)* |
| DGV | Securities Management Department *(Departamento de Gestión de Valores)* |
| DM | Debt Management |
| DNFE | Department for Negotiation of External Financing *(Departamento de Negociación de Financiamiento Externo)* |
| DO | Operations Department *(Departamento de Operaciones)* |
| DSA | Debt Sustainability Analysis |
| EDMP | Medium Term Debt Strategy (*Estrategia de Deuda de Mediano Plazo)* |
| ENEE | National Electric Energy Company *(Empresa Nacional de Energía Eléctrica)* |
| FRS | Fiscal Risk Statement |
| GG | General Government (*Gobierno General)* |
| HR | Human Resources |
| IDB | Inter-American Development Bank |
| IFAD | International Fund for Agricultural Development |
| IMF | International Monetary Fund |
| JICA | Japan International Cooperation Agency |
| KfW | Kreditanstalt für Wiederaufbau |
| LOP | Organic Budget Law (*Ley Orgánica de Presupuesto)* |
| LRF | Fiscal Responsibility Law *(Ley de Responsabilidad Fiscal)* |
| MMFMP | Medium Term Macro Fiscal Framework (Marco Macro Fiscal de Mediano Plazo) |
| MMFMP | Medium-Term Macro Fiscal Framework (*Marco Macro Fiscal de Mediano Plazo)* |
| NFPS | Non-Financial Public Sector |

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|---|---|
| NTCP | Technical Notes of the Public Credit Subsystem (*Notas Técnicas del Subsistema de Crédito Publico)* |
| PCC | Public Credit Commission |
| PEP | Public Borrowing Policy *(Política de Endeudamiento Público)* |
| PF | Financing Plan (*Plan de Financiamiento)* |
| PIP | Public Investment Program (*Programa de Inversion Publica)* |
| PPP | Public Private Partnership |
| RDV | Rules of the Securities Depositary (*Reglamento de Depositaria de Valores)* |
| RELOP | Rules of Procedure for Execution of the Organic Budget Law *(Reglamento de Ejecución de la Ley Orgánica de Presupuesto)* |
| RNVG | Rules of Procedure for Public Securities' *Negotiation (Reglamento de Negociación de Valores Gubernamentales)* |
| SEFIN | Secretary of State in Finance (*Secretaria de Estado en el Despacho de Finanzas*) |
| SFN | National Financial System (*Sistema Financiero Nacional)* |
| SIAFI | Integrated Financial Management System *(Sistema de Administración Financiera Integrada)* |
| SIGADE | Debt Management and Financial Analysis System *(Sistema de Gestión y Análisis de Deuda)* |
| SOE | State Owned Enterprise |
| STA | Single Treasury Account |
| T-Bills | Treasury Bills |
| TGR | General Treasury of the Republic (*Tesorería General de la Republica)* |
| TSA | Treasury Single Account |
| TSC | Supreme Court of Accounting (*Tribunal Superior de Cuentas)* |
| UCF | Fiscal Contingencies Unit (*Unidad de Contingencias Fiscales)* |
| UPEG | Planning and Management Evaluation Unit *(Unidad de Planeamiento y Evaluación de la Gestión)* |
| WB | World Bank |

# I. Executive Summary

A World Bank mission undertook an assessment of the government's debt management capacity and institutions in Honduras during May 10-18, 2021. The mission comprised Andre Proite (TTL), Leandro Secunho- both Senior Debt Specialists (MTI/EMFMD), and Elizabeth Currie, Leonardo Somarriba – both WB consultants. The mission was supported by Elena Bondarenko – Country Economist (MTI/ELCMU) and Belkis Diaz – Team Assistant (LCCHN). The objective of the mission was to assess the debt management strengths and areas in need of reform through the application of the Debt Management Performance Assessment (DeMPA) methodology.

The DeMPA mission delivered technical assistance in evaluating the legal, institutional and regulatory framework in government debt management. The primary counterpart was SEFIN (*Secretaria de Finanzas*) and the DGCP (*Dirección General de Crédito Público*) which is the main debt management office.

Two cross-cutting indicators are highlighted: Staff and DM Information Systems, as they help to explain DM's performance. DGCP staff are specialized and can perform all core debt management functions (see DPI 2.3). The recruitment process followed is acceptable and turnover ratio is low. At the beginning of the year training plans are discussed with the personnel who performs according to job descriptions. All staff must sign a code of conduct, a confidentiality agreement and there has been no evidence of misconduct. The staff uses the system (SIGADE) to record all debt related transactions and payments are generated by the system (see DPI 15.1).

| Strengths | Areas for Improvement |
|---|---|
| 1. Governance and Strategy Development | |
| • Managerial structure<br>• The content of Debt Law (LOP) is fairly complete according to the DeMPA requirements<br>• Debt Reporting<br>  o Complete debt cost-risk indicators for the CG Debt portfolio<br>  o Debt coverage for Subnational and SOEs<br>• Debt Strategy<br>  o Medium-Term Debt Strategy and Financing Plans are updated yearly | • Legal Framework<br>  o Adhere to existing regulations for all beneficiaries of guarantees/on-lending<br>• Debt Reporting<br>  o Include fiscal arrears in the stock of overall CG debt<br>  o Provide more details on the guarantees and on-lent portfolio |
| 2. Coordination with Fiscal and Monetary Policies | |
| • Detailed debt flows and estimates are shared between the DMO and the Macro-Fiscal Area<br>• Debt-Related Fiscal Risks are monitored<br>• DSAs are conducted at least annually | • Observe the overdraft limit<br>  o Repayment of BCH advances has been refinanced with securities without clearing the original flow<br>• Publish financial ratios for government related entities |

| | |
|---|---|
| • Clear separation between Monetary Policy and Debt Management | |
| **3. Borrowing and related financing activities** | |
| • Market based instruments are used domestically<br>• External Borrowing is processed and monitored in details<br>• Credit / financial risk analysis is undertaken for most beneficiaries for Guarantees/ On-lending | • Issuance calendar has not always been observed<br>• Short-term bonds could be used to coordinate the yield structure with BCH's repo<br>• Guarantees / On-lending<br>    o Avoid waiving the formal guidance to provide guarantees/on-lending<br>    o Guarantees/on-lending are deemed to be inadequate policy instruments to support ENEE under the current legal and operational framework. |
| **4. Cash flow forecasting and cash balance management** | |
| • Daily cashflow estimates for the whole year<br>• Good CG coverage<br>• Performance assessment of the estimates vs actuals | • Government balances on BCH are not remunerated<br>• Absence of ST instruments to cover temporary cash shortages |
| **5. Debt Recording and Operational risk management** | |
| • Recording and Payment processes are well defined<br>    o Separation of duties<br>• The IT infrastructure supports DM operations<br>    o Backups are frequent and safely stored<br>• Complete database for Central Gov't debt | • Business Continuity plans are not in place<br>• Auditing trail is not possible from the Debt System |
| **6. Cross Cutting Indicators** | |
| • Staff<br>    o The personal is capable of performing core DM functions<br>    o The turnover is low<br>    o The size of the staff is appropriate for the current portfolio<br>• DMIS – Debt Management Information Systems<br>    o Staff prepares cash flows, payments and reports based on their own records. The staff is able to undertake substantial work around the system to perform core debt functions | • Staff<br>    o Code of conduct does provide guidance for debt-related transactions<br>    o Staff development plans should be developed<br>• DMIS – Debt Management Information Systems<br>    o Higher automation of system functionalities could improve the efficiency of the existing processes within the DMO |

# II. Background and Government Debt

## II.1. Economic Background

**Relative macroeconomic stability favored the rollout of a robust reform agenda in recent years.** The real GDP growth averaged 3.1 percent over the past decade, aided by remittance-fueled private consumption. Prudent macroeconomic management anchored in the Fiscal Responsibility Law (LRF) implemented in 2016 supported prudent fiscal policies, a crawling peg exchange rate with ample foreign reserves, and a solid financial sector supported macroeconomic stability in the run-up to the COVID-19 crisis. The government advanced reforms to strengthen the macroeconomic framework, business environment, and monitoring and mitigation of fiscal risks, including those related to the state electricity company (ENEE) – the key source of fiscal vulnerability. However, country's exposure to external shocks, natural hazards, combined with high crime rates and a weak institutional and business environment, undermined its competitiveness and ability to boost growth and incomes. in 2019, almost half the population (4.8 million people) lived on less than US$5.50 per day, making Honduras one of the poorest countries in the Latin America and Caribbean region.

**The global pandemic and the impacts of tropical cyclones Eta and Iota have strongly impacted Honduras in 2020 and exacerbated existing economic and social challenges.** The real GDP contracted by a record 9 percent in 2020 (y/y) due to a sharp fall in trade, investment and consumption amid the global recession, extended lockdown, and damages caused by the hurricanes. Both hurricanes affected around 4.7 million people (48 percent of the population), generating social and economic costs that are estimated at around USD 1.8 billion (7.5 percent of 2020 GDP) due to damages to key infrastructure, land and crops. As unemployment spiked in the United States, growth in remittances to Honduras decelerated from an average of 10 percent, (y/y) to 3.8 (y/y) in 2020, suppressing private domestic demand and domestic investment, and contributing to rising levels of poverty. Weaker domestic demand, lower commodity prices, freezes in prices and a relatively stable exchange rate reduced consumer price inflation, despite higher food prices in the aftermath of hurricanes. Annual inflation decelerated to 3.5 percent (y/y) in 2020 – near the lower limit of the Central Bank's (BCH) target band (4% ± 1 %). As a result, the BCH cut the key policy rate by 250 basis points to 3 percent in 2020. While the policy response to the pandemic was well designed, emergency programs had a relatively small mitigating impact as COVID-19 related lockdowns impacted employment and incomes, and access to education, while new COVID—19 daily cases continue rising amid slow vaccination rates in the country.

**In response to the shocks, the government has enacted targeted policies to cushion the impacts on economic activity and welfare, authorizing new borrowing of up to US$2.5 billion (10% of GDP) for 2020–21** and reallocating nonpriority spending**.** The government's Containment and Response Plan prioritizes healthcare and humanitarian services, as well as targeted support to the secondary sectors (manufacturing, energy and construction) and small businesses. The country's relatively low public debt and deficit levels coupled with good access to concessional financing allowed for the countercyclical response amid activations of the FRL's escape clause. As a result, the NFPS deficit increased to 5.5 percent of GDP in 2020 (up from 0.9 percent in 2019), bringing public non-financial debt to 53.7 percent of GDP in 2020 (compared to 43.1 percent in 2019). The government continues to implement targeted policies to cushion the impacts of the multiple shocks on economic activity and livelihoods, and the country is expected to continue receiving external financial support while gradually consolidating its fiscal position. The government is committed to fiscal prudence and aims to return to the 1 percent NFPS deficit ceiling in 2023 while protecting priority spending. The required consolidation is challenging and is expected to be supported by the unwinding of pandemic support, budget reallocations, strict spending controls, and gradual revenue growth aided by the economic recovery and revenue mobilization measures.

**After the sharp contraction in 2020, economic growth has been steadily recovering in the first half of 2021 led by remittance-fueled private consumption and post-hurricane reconstruction.** Real GDP grew 1.3 percent y/y in the first quarter of 2021, while the index of economic activity registered a 12.4 per-cent y/y expansion in the first half of 2021. This expansion was broad-based (except for labor-intensive agriculture) driven by private consumption and post-hurricane reconstruction spending. Growth in remittances, representing 23.4 percent of GDP in 2020 and 29 percent of household income for the poorest remittance-receiving households, accelerated by 29.6 percent y/y in the first quarter of 2021, further supporting the total house-hold incomes. Employment gains associated with this recovery are expected to help restore household income. Real GDP is expected to reach its pre-pandemic level by 2023, supported by a favorable external environment and strengthening domestic activities amid vaccination rollout. Manufacturing and services are expected to pick up in the short term, while the recovery in the agriculture sector could be subdued amid severe damages to crops and land.

**The external position remains relatively strong, supported by remittances and higher external financing, mainly from multilateral organizations, received in response to the pandemic.**. Foreign reserves stood at US$8.9 bn (37 percent of 2020 GDP) at the end-August 2021, supporting exchange rate stability. After registering a historical surplus of 2.9 percent of GDP in 2020, the current account is expected to reverse to a deficit in 2021 on the back of recovering imports. A wider current account deficit associated with higher import values is expected to be financed primarily by FDI inflows in the medium term. As the economy begins to gain momentum, an increase in FDI is expected, especially in critical economic sectors such as maquila. As the authorities advance with the much-needed reform agenda for the electricity sector, greater investments in generation and transmission are also expected.

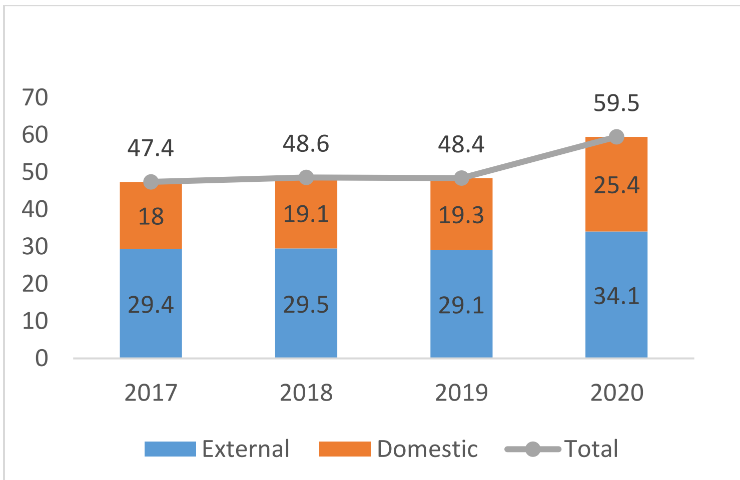
**The Government aims to achieve medium term public debt sustainability through due compliance with the FRL**. This process confirms the commitment to continue with the path of macroeconomic stability, which contributes to the recovery and acceleration of economic activity, improve the position of the balance of payments, reduce vulnerabilities, create fiscal spaces for both structural reforms and the execution of programs, projects for reactivation and reconstruction, reduce sovereign risk and increase the attraction of Foreign Direct Investment (FDI).

## II.2. Government Debt

**In December 2020, the preliminary balance of the total NFPS debt was USD 13,121.2 million (equivalent to 59.5 percent of GDP), increasing USD 1,987.2 million (17.8 percent) with respect to 2019.** The external debt was equivalent to 64.4 percent of the total and 35.1 percent of the GDP, and the internal debt represented 35.6 percent of the total and 19.4 percent of the GDP. Most of the internal debt was constituted by the Central Government's (CG) obligations at 81.6 percent of the total, with 10.6 percent corresponding to decentralized organizations and 7.8 percent to the municipalities.[1]

**The CG public debt increased from 48.4 percent of the GDP in 2019 to 59.4 percent in 2020, as a result of new debt mainly associated with the COVID-19 pandemic.** These resources were authorized by the National Legislature to attend the humanitarian and health emergency under the framework of a fiscal policy and in compliance with the International Monetary Fund (IMF) program.

**Figure 1** – Central Government Debt (% GDP)



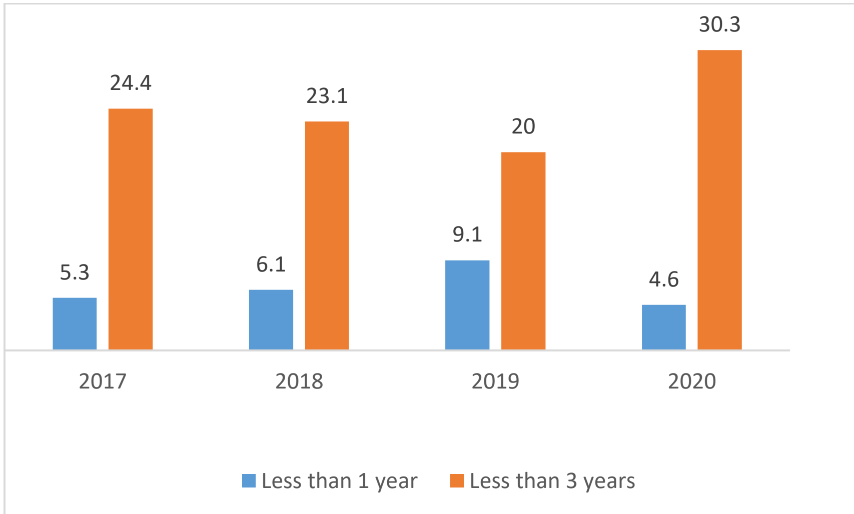

Source: SEFIN (PEP)

**An overview of total Central Government (CG) debt in December 2020 shows that external debt accounted for 57 percent of total debt or USD 8,206.3 million while the internal debt amounted to USD 6,102.9 million.** The total debt's average life rose slightly from 8.7 years in 2019 to 8.9 years in 2020, and the proportion of fixed rate debt also grew during that period from 69.8 percent to 72.1 percent, factors which contributed to reduce risk. However, currency risk was significant as only 42.6 percent of the CG debt was denominated in Lempiras (HNL) -or 25.4 percent of GDP. Also, while 4.6 percent of the total portfolio came due in less than one year (at Dec.2020), showing a reduction from the level of 8.7 percent in 2016, the proportion coming due for a period of less than 3 years was 30.3 percent, a higher concentration than in 2016 (PEP).

**The degree of concessionality is still significant which explains the long and fixed debt profile.** Debt having concessional terms decreased from 57 percent in 2016 to 47.1 percent and 46.7 percent in 2020 and March 2021, respectively. Even so, the average concessionality element of the external debt grew slightly in 2020, from 27.9 percent in 2019 to 29.9 percent in 2020, due to the greater concessional terms of new multilateral loans. The external debt has an average life of 11.8 years, and close to 63 percent of external debt has a fixed interest rate. Its most important currency is the US dollar (85 percent) followed by SDR (10.2%), and others.

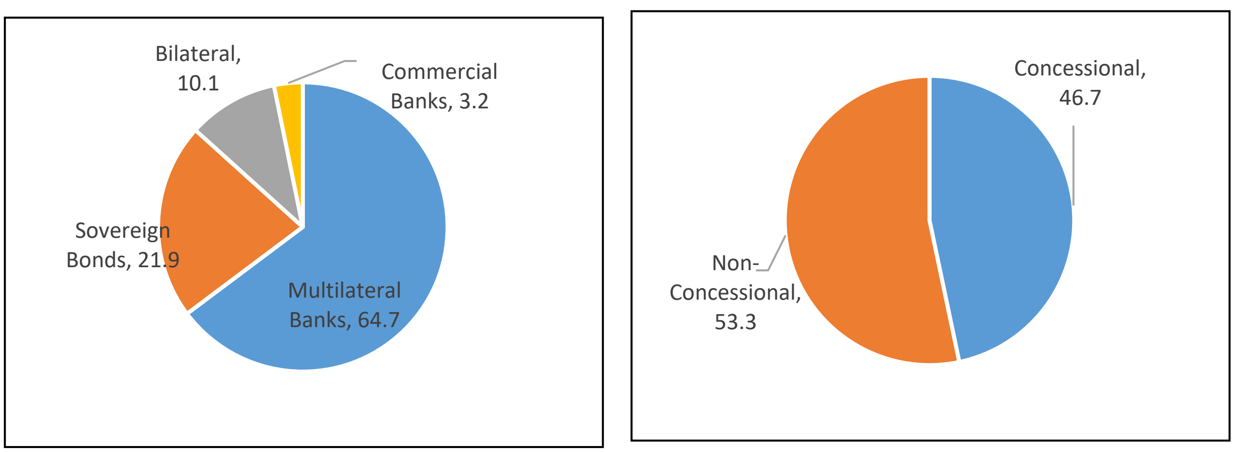
[1] Source: PEP

**Figure 2- Central Government Debt Structure (%)**




Source: SEFIN (PEP)

**Figure 3 - Central Government External Debt Composition- 2020 (%)**

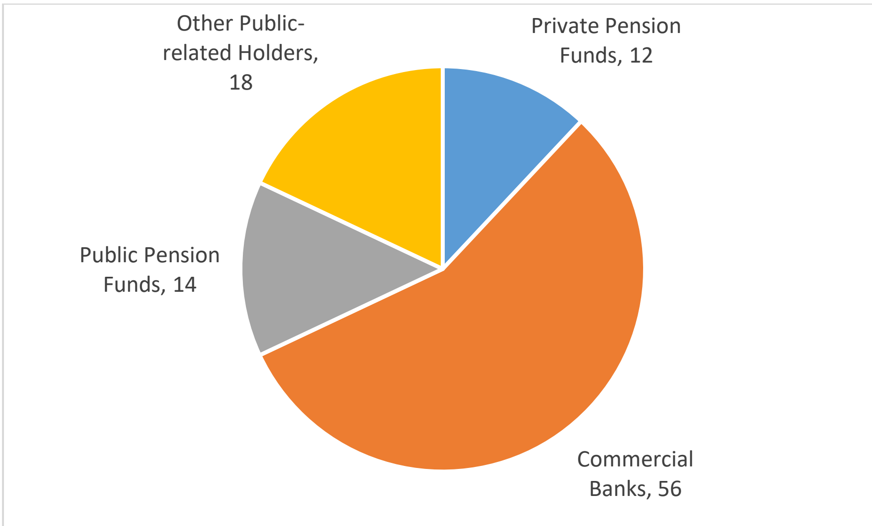



Source: SEFIN (PEP)

**Eurobond issuances have increased recently.** Two international bonds were issued in 2013: each for USD 500 million, one a 11-year (soft-bullet) and the other with a 7-year maturity (due on December 2020). A 10-year bond was issued in 2017 for USD 700 million, another 10-year bond was issued in 2020 for USD 600 million and there is authorized another bond in 2021 for a maximum of USD 600 million.

**During the past five years, the domestic debt has maintained its share of CG debt at between 38 and 40 percent, although in 2020 it increased to 42.7 percent and in March 2021 to 44.3 percent.** The domestic debt is mainly held by national commercial banks (56 percent), followed by public and private pension funds (26 percent). The share of commercial banks increased due to high market liquidity as a result of an expansive monetary policy following the pandemic, together with insufficient supply of Central Bank (BCH) bonds, that led to banks deciding to also invest in SEFIN bonds. The domestic debt has an average maturity of 5 years, showing an improvement from 4.2 years in 2016. The government aims to further develop the domestic debt market, with longer maturities to be increasingly held by pension funds and other institutional investors and to reach a larger proportion of debt denominated in lempiras.

**Figure 4 - Share of CG Domestic Debt by Investor – 1Q21 (%)**




Source: Quarterly Report of CG Public Debt

In March 2021, domestic debt was largely (92.5 percent) composed of bonds, with the remaining 7.5 percent corresponding to loans. Most of the domestic debt (84.6 percent) has fixed interest rates and almost all bonds have a fixed rate, except for inflation-indexed bonds with a 10 year maturity[2]. The CG issues bonds with maturities of 3, 5, 7, 10 and 15 years. Most domestic debt is denominated in HNL, but a smaller part remains in US dollars, mostly from the loans mentioned above.

**Debt is largely being placed though auctions, and direct placements- which were very prevalent in the past- have diminished.** The SEFIN's bonds with Central Bank issued for the fulfillment of the BCH recapitalization agreement recapitalization and liability management purposes, are direct placements. For example, in 2020, total bond issuance was for HNL 29,044 million, of which 76 percent was placed through 17 competitive auctions, and the remaining 24 percent (HNL 6,907 million) were debt exchanges that were directly placed with Central Bank.

**According to the joint Bank-Fund Debt Sustainability Analysis (DSA) in 2021, Honduras remains at low risk of debt distress both for public external and overall debt.[3,4]** Given the large and unavoidable effects of the COVID-19 pandemic and two tropical storms on public finances, the Honduran authorities triggered the escape clause within the Fiscal Responsibility Law (FRL). Public debt increased significantly in 2020 due to the adverse effects from the pandemic and two tropical storms. Public and Public guaranteed debt

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[2] Inflation-indexed bonds only represented 1.2 percent of bonds placed in 2020.

[3] The DSA updates the previous joint IMF/WB DSA prepared in June 2020 in the context of the Honduras Second Reviews staff report (IMF Country Report No. 20/186).

[4] Honduras's debt carrying capacity is assessed to be strong based on a composite indicator of 3.13 that uses the October 2020 WEO vintage and the 2019 CPIA.

is projected to peak at around 59.7 percent of GDP in 2022 and start declining thereafter, supported by stable primary surpluses as well as declining interest payments, reaching around 50 percent of GDP by 2031 (Table 1). Public debt dynamics remain vulnerable to contingent liabilities and exogenous shocks, especially to those related to natural disasters. Nonetheless, Honduras' proven record of compliance with the FRL provides confidence that the response to the pandemic will not jeopardize debt sustainability. Honduras maintains a strong debt carrying capacity and none of the debt burden indicators breach their respective thresholds. Going forward, continuous adherence to the FRL and institutional reforms to boost inclusive growth and increase the economy's potential are important to safeguard debt sustainability.

Table1: Key Macroeconomic Indicators, 2016-2023

| | 2016 | 2017 | 2018 | 2019 | 2020 | 2021e | 2022e | 2023e |
|---|---|---|---|---|---|---|---|---|
| **Real Sector** | *Annual percentage change, unless indicated* | | | | | | | |
| Real GDP growth | 3.9 | 4.8 | 3.7 | 2.7 | -9.0 | 4.9 | 4.4 | 3.5 |
| Inflation - CPI (average) | 2.7 | 3.9 | 4.3 | 4.4 | 3.5 | 4.6 | 3.7 | 4.0 |
| **Fiscal Accounts (NFPS)** | *Percent of GDP, unless indicated* | | | | | | | |
| Overall Fiscal Balance | -0.5 | -0.8 | -0.9 | -0.9 | -5.5 | -5.4 | -2.3 | -1.0 |
| Primary Balance | 0.3 | 0.1 | 0.0 | 0.2 | -4.2 | -4.3 | -1.3 | 0.5 |
| Total Public Debt* | 40.1 | 40.1 | 42.8 | 46.5 | 54.5 | 58.7 | 59.7 | 59.3 |
| **External Sector** | *Percent of GDP, unless indicated* | | | | | | | |
| Current Account Balance | -2.6 | -0.8 | -5.8 | -1.4 | 3.0 | -3.2 | -3.4 | -3.6 |
| Foreign Direct Investment | 4.2 | 4.5 | 3.7 | 2.0 | 1.6 | 2.0 | 2.4 | 2.7 |

Source: IMF and Work Bank (MPO) estimates and projections.
Notes:
p: preliminary; e: estimations
* Includes both public and private sector external debt

# III. Debt Management Performance Assessment (DeMPA)

## III.1. DeMPA Methodology

**The DeMPA 2021 methodology (pilot) comprises a set of 14 debt performance indicators (DPIs), which encompass the complete spectrum of government debt management operations, as well as the overall environment in which these operations are conducted.** While the DeMPA does not specify recommendations on reforms and/or capacity and institution building, the performance indicators are based on sound practices and stipulate a minimum level that should be met. Consequently, if the assessment shows that the minimum requirements are not met, this clearly indicates an area requiring attention and priority for reform. A complete description of the methodology can be found on https://www.worldbank.org/en/programs/debt-toolkit/dempa.

## III.2. Summary of Performance Assessment [5]

| Debt Performance Indicator | | Score 2021 | Score 2014 |
|---|---|---|---|
| DPI-1 | 1.1. Central Government's Legal Framework | D | D |
| | 1.2. Public Sector Entities' Central Government's Legal Framework | A | N/C |
| DPI-2 | 2.1. Managerial Structure: CG Borrowing and Debt-Related Transactions | A | C |
| | 2.2. Managerial Structure: Issuing Loan Guarantees/On-Lending | A | D |
| | 2.3. Staff and Human Resources | C | N/C |
| DPI-3 | 3.1. DMS: Quality of Content | A | D |
| | 3.2. DMS: Decision-Making Process | D | N/R |
| | 3.3. ABP: Annual Borrowing Plan | C | N/C |
| DPI-4 | 4.1. Central Government Debt Report- Content and Timeliness | C | D |
| | 4.2. Reporting to the Legislature | B | N/C |
| | 4.3. Public Sector Debt Report- Government Coverage | D | N/C |
| DPI-5 | 5.1. Audit: Frequency, Comprehensiveness and disclosure (Financial, Compliance, Performance) | C | D |
| | 5.2. Audit: Degree of commitment to address audit outcomes | D | N/R |
| DPI-6 | 6.1. Fiscal Policy: Provision of Debt-Service Forecasts | A | C |
| | 6.2. Fiscal Policy: Fiscal Risks Monitoring in the Non-Financial Public Sector | B | N/C |
| | 6.3. Fiscal Policy: Availability of Key Macro and Fiscal Variables and DSA | A | A |
| DPI-7 | 7.1. Monetary Policy: Separation between Monetary Policy and DM Operations | A | B |
| | 7.2. Monetary Policy: Information Sharing with the CB on current and future debt transactions and CG cash flows | D | C |
| | 7.3. Monetary Policy: Limits of direct access to CB Funding | D | D |
| DPI-8 | 8.1. Domestic Borrowing: The publication of a borrowing calendar for wholesale securities and publication of issuance results | D | N/C |

[5] The DeMPA methodology was revised in 2015 and 2021, and not all indicators are directly comparable between 2011 and 2021. See DeMPA 2021 – Annex III and https://www.worldbank.org/en/programs/debt-toolkit/dempa

| | | | |
|---|---|---|---|
| | 8.2. Domestic Borrowing: Clarity in rules and procedures | A | N/C |
| DPI-9 | 9.1. External Borrowing: Appropriate organizational arrangements and processes for external borrowing from all sources, including financial analysis of terms and conditions | C | N/C |
| | 9.2. External Borrowing: Availability and degree of involvement of legal advisers before signing the loan contract | B | D |
| DPI-10 | 10.1. Loan Guarantees: Issuance of central government loan guarantees | D | D |
| | 10.2. On-lending: Management of On-lending Operations | D | D |
| | 10.3. Derivatives: The use of Derivatives | NA | NA |
| DPI-11 | 11.1. Effectiveness of forecasting the aggregate level of cash balances in government bank accounts | D | D |
| | 11.2. Effectiveness of cash balance and liquidity management | D | D |
| DPI-12 | 12.1. Recording debt-related transactions | A | N/C |
| | 12.2. Debt Payments | B | N/C |
| DPI-13 | 13.1. Data access, backups and IT infrastructure | B | N/C |
| | 13.2. Business Continuity (BC) and Disaster Recovery (DR) Plans | D | D |
| DPI-14 | 14.1. Debt Records: Completeness and Timeliness of CG records | A | D |
| | 14.2. Debt Records: Registry System and Debt Holders | A | B |
| DPI-15 | 15.1. The use of Debt Management Information Systems (DMIS) | B | N/C |

See Annex 4 for the highlights of DeMPA scores observed between 2014-2021.

# IV. Performance Indicator Assessment

## IV.1. Governance and Debt Management Strategy

### DPI 1 - Legal Framework

| DPI | Score |
| --- | --- |
| 1.1 - Central Government's Legal Framework | D |
| 1.2 - Public Sector Entities' Legal Framework | A |

### DPI 1.1 - Central Government's Legal Framework

*Institutional Aspects*

1. **The content of Central Government's legal framework is comprehensive and detailed**. Article 357 of the Constitution states that primary legislation governs the authorization of new borrowings of external and domestic debt of the CG, decentralized organizations, and municipal governments. In addition, Article 205 (36) requires the Legislature to approve borrowing undertaken by the Executive power. Article 358 gives local governments power to issue domestic debt under their own financial responsibility, with prior authorization from the central authority, in accordance with the Organic Budget Law - LOP (2004).

2. **The LOP (2004) is the Public Financial Management (PFM) law in Honduras and contains several provisions related to debt. The authorization to borrow and to undertake on-lending rests with the Minister of Finance (SEFIN[6]) according to Articles 64-81**. Debt management operations shall be undertaken by SEFIN (which harbors the DGCP – *Dirección General de Crédito Público*- the principal DMO),[7] which is entitled to delineate the rules and procedures to borrow. For that, the LOP is further detailed in regulations (NTSCP)[8] which provide guidance on how to conduct debt operations and to process guarantees / on-lending.

3. **LOP's Articles 71-78 state that the Minister of Finance has to authorize the issuance of guarantees**. **On-lending is authorized through the NTCP-Public Credit Technical Notes.** Article 71 requires that all external guarantees have SEFIN's approval: *"No public sector entity is entitled to initiate external debt transactions without written authorization from Sefin (…)".* Article 78 extends the approval to the President and to the Legislature, which needs to ratify the guarantees. Article 76 says that *" The executive power may use bonds, bills and contract public debt obligations in accordance with the budget approved by the Legilsature. (…) The issuance of public debt must be formalized by the Minister of Finance (Secretario de Finanzas)"* while Article 77 says that *"Sefin may issue bonds in the*

[6] *Secretaría de Finanzas Públicas*
[7] The LOP authorizes the TGR (Treasury Unit) to issue short-term securities to cover cash needs, but that has also been performed by the DGCP.
[8] *Notas Técnicas del Subsistema de Crédito Público.*

*capital market"*. The Minister of Finance also has to authorize domestic guarantees and this is required by the NTCP Articles 18 and 19. The secondary regulation clearly differentiates guaranteed debt from direct debt (on-lent) and, the practice is to apply the same rules towards the beneficiaries of credit enhancement schemes, requiring: (i) authorization to borrow and (ii) credit risk assessment, which considers a set of indicators on debt levels, and repayment capacity.

**4. The definition of debt instruments used by the government is defined by LOP in Articles 64-67**, which recognize that any repayable financial resources obtained domestically or externally should be considered debt. Article 65 lists the following as debt:

i. Issuance of Treasury Bills for cash management purposes
ii. Contracting of new obligations with national and international financial institutions
iii. Acquisition of new debt for goods and services and other obligations that will be repaid in more than one year (*Pagarés*)
iv. Issuance of longer-term instruments with maturity of more than a year
v. Guaranteed obligations coming from Public Sector (PS) entities after formalized by SEFIN and other provisions stipulated by LOP.

Agreement n. 846-2018 reforms a series of NTCP articles aligning the debt definitions and criteria to the LOP. In particular, Article 9 (3)(c) clarifies that unpaid fiscal obligations "*crédito a proveedores*" is considered CG direct debt.

**5. The purpose of borrowing is explicit in LOP Article 64.**

i. Instigating productive investments with justified economic and social benefits
ii. Addressing evident cases of national necessity
iii. Supporting sector policies, which is undertaken through the budget execution and the Public Borrowing Policy (PEP)
iv. Refinancing the liabilities.

**6. Clear DM objectives are defined in the PEP which is required by LOP Art.66.** Section IV.1 of the PEP says that the general DM objective is to *"(…) finance the government in accordance with the fiscal targets and to maintain prudent risk levels."* Section IV.2 states that *"The CG debt management shall seek the best cost-risk balance possible considering the external and domestic financing available" and (…) domestic debt can be used to minimize the exposure to currency risk and to develop the domestic market".* The preparation of the PEP has to be undertaken by the Executive level of governance and approved by the Public Credit Commission (PCC), which was created by the same Law, and is comprised by SEFIN, as the head, and the BCH. According to the LOP, the PEP should contain, among others, the following information: (a) Maximum amounts contracted by the Public Sector each year in both external and internal debt; (b) Minimum level of concessionality accepted for external debt; (c) Maximum amount of debt acquired, in net terms, for other public sector institutions.

**7. Article 66 also requires the PEP to be published** and the document has been presenting debt figures since 2017 for the CG and for other entities within the public sector.

**8. A DM strategy and a sustainability analysis are required to be published by the PEP**, which also provides limits and conditions to each government level to conduct credit operations.

**9. There is no framework in place to guide the management of guarantees or on-lending.** Although the PEP determines some limits and other regulations specify how they should be issued, they are more related to the operational side and fall short to define eligibility criteria on the policy side. On the institutional aspect and content, this is the only component of the institutional legal framework that is missing for the highest score.

*Implementation Aspects*

**10. The assessment gathered evidence for each aspect cited above and recognized that almost all aspects above are implemented. The exception refers to the implementation of LOP Article 78 and NTCP regulation regarding the issuance of guarantees and on-lending to one SOE beneficiary: the ENEE (National Electric Energy Company).** Although duly authorized by the President and ratified by the Legislature, ENEE is granted guarantees without complying with all requirements of the legislation by-passing the regulation, in particular in regard to the requirement of undertaking credit assessments as it turns out that the SOE would not qualify to receive the credit support. It is understood that ENEE faces structural financial problems and that the use of official guarantees may not be the most adequate instrument to support the company. All other beneficiaries of guarantees and on-lending operations follow the track dictated by the legal framework.

**11. The institutional aspect of the legal framework is sound, but the implementation is lacking in the aspect described above and the score is a D.** The DeMPA methodology requires both institutional and implementation sides to be observed. All else being equal, the indicator could be a B if all guarantee beneficiaries would comply with the current ruling. Scoring remains the same as in 2014's assessment under similar rationale[9].

## DPI 1.2 - Public Sector Entities' Legal Framework

*Institutional Aspects*

**12. The LOP (Article 2) defines public entities as those where the government has a stake higher than 50% of the capital and Article 53 requires that all entities report to SEFIN their economic and financial results.** Article 71 determines that all public entities need a written authorization from SEFIN to seek external financing. In case of domestic borrowing, public entities need to solicit a credit risk evaluation from SEFIN. In addition, NTSCP Art. 18 establish that all government related entities need to submit financing requests (external and domestic) for SEFIN to provide an opinion. Article 87 of the Municipalities Law (*Decreto Legislativo 134-90*) states that municipalities can borrow domestically or externally if and only if they follow the instructions embedded in the LOP and SEFIN's regulations. The

[9] See Annex 4 for the evolution of DeMPA scores.

same process would apply to municipal corporations.

13. **The legislation requires the CG to report the debt of NFPS bodies.** Article 66 of the LOP requires SEFIN to elaborate the PEP for the NFPS (Non-Financial Public Sector) and the main debt figures for different government levels have been reported in the document.

14. **The legislation describes the role of the CG in authorizing borrowing and the issuance of guarantees for NFPS bodies.** The PEP (Section IV) specifies the maximum amount and the type of debt activities public entities can undertake. There is guidance on concessionality requirements for new borrowings and authorization for disbursement on outstanding loans broken-down for municipalities and SOEs.

*Implementation Aspects*

15. **The mission assessed that the PEP and the LOP (various articles), together with the NTSCP regulations are binding to the criteria for this DPI and the score is an A.** The PEP has been an important document to facilitate the implementation of the fiscal policy and has provided transparency and guidance to borrowing from NFPS entities. The document's coverage has been expanded to the NFPS since 2017 and currently describes the outstanding debt, recent operations and sets limits and guides borrowing for each type of public entity. Due to methodological changes, this indicator was not rated in the previous assessment.

## DPI 2 - Managerial Structure

| **DPI** | **Score** |
|---|---|
| 2.1 - The managerial structure for central government borrowings and debt-related transactions. | **A** |
| 2.2 - The managerial structure for preparation and issuance of central government loan guarantees. | **A** |
| 2.3 – Staff and Human Resources | **C** |

### DPI 2.1 - Managerial Structure for Debt

16. **DGCP within SEFIN is the sole unit responsible for CG debt management.** This is defined as part of its role as Technical Coordinating Bureau of the Public Credit. Loan negotiations are the responsibility of SEFIN through DGCP. In addition, SEFIN plays a controlling role in NFPS external borrowing (DPI-1).

17. **The General Treasury of the Republic (TGR) of SEFIN is legally allowed to issue CG short-term debt, but it has to go through the DGCP.** Though the TGR is authorized to issue securities to cover

temporary cash imbalances, it has not done so and T-bills have been issued through the DGCP[10].

**18. To carry out its duties the DGCP organized its structure along functional front, middle and back office lines:**

***A. Front Office***

The front office functions are performed by the Department of External Financing (DFE) with 7 staff, and the Department of Securities Management (DGV) with 4 staff. The former carries out the borrowing from multi and bilateral creditors, the international capital markets[11] and much less so from private financial institutions. In turn, DGV takes the decisions for issuing bonds in the domestic market and carrying out liability management operations to improve the portfolio's risk profile, the operational part of which corresponds to BCH (see below) and manages the contact and meetings with the domestic market participants.

***B. Middle Office***

The Department of Debt Management and Risk (DGDR) with 2 staff carries out the middle office functions. It drafts the PEP, the medium-term debt management strategy (EDMP), the Annual Financing Plan (PF) together with the front office, makes the credit risk analyses related to guarantees, on-lending and requests for new external borrowing of entities from NFPS including municipalities, produces reports and coordinates with other units such as DGPMF in preparing the DSA, among others. Additionally, a new unit was created with 2 staff to converge official statistics to the IMF's Government Finance Statistics Manual (2014).

***C. Back Office***

The Department of Operations (DO) with 8 staff carries out the functions of debt confirmation, registration of operations in SIGADE, payments, document filing, prepares the debt service forecasts, and keeps track of loan disbursements, among others. The Department of Quality Control (DCC) with 4 staff implements an oversight of the activities of the other DGCP's departments.

**19. In practice the DGCP is the only CG debt issuer.** It is also in charge of liability management operations related to central government debt, including exchanges to alter the risk profile and debt buy-backs. The CG only issued T-bills during a brief period (2012-2013) and the short end of the yield curve has for many years been used for monetary policy implementation (see DPI-7). Therefore, the DGCP can plan and to implement the debt management strategy.

**20. The BCH conducts domestic borrowings as an operational agent for the CG.** According to RNVG[12] (Art.25), SEFIN is authorized to establish an agency contract with BCH or another specialized implementing entity. In 2018 the two parties signed an agency agreement (*Contrato Marco de Negociación de Valores*) that is published on SEFIN's website; it establishes the general obligations and responsibilities of the two parties and clearly states that SEFIN makes the relevant decisions (e.g., auction cutoff) while BCH's scope is limited to operational implementation. It is up to the DGCP to

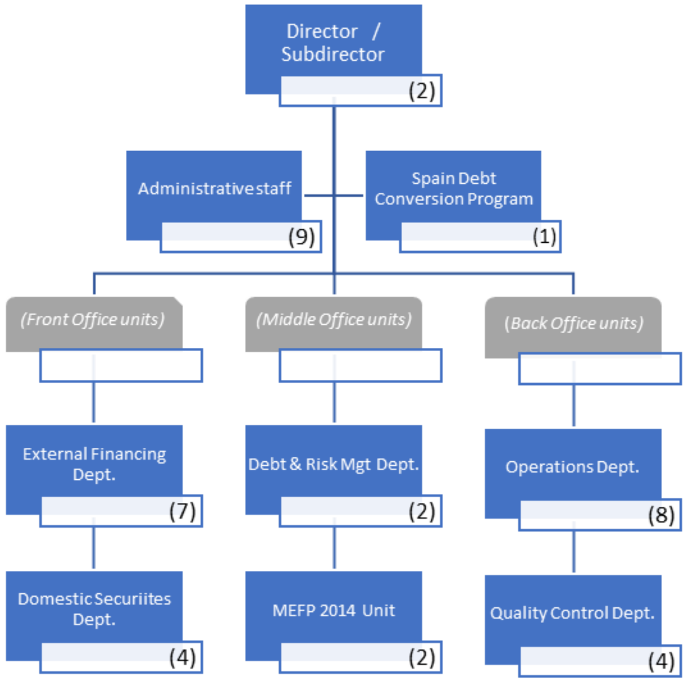
[10] LOP Art.90

[11] In recent years SEFIN has issued bonds in the international markets with the assistance of external advisors and with permanent assistance from the U.S. Treasury Department resident.

[12] Rules of Procedure for Public Securities' Negotiation *(Reglamento de Negociación de Valores Gubernamentales)*

define the financial conditions of auctions and liability management operations and the RGNVG defines the framework for debt issuance; the operational responsibilities of BCH and the fees charged.

**Figure 5 – Managerial Structure of the DGCP (DMO)**




Source: DGCP

**21. The score is an A, given that central government borrowing is undertaken by a single DM unit** and that debt-related activities are carried out by BCH acting as agent for the government under a published contractual agreement. The previous assessment granted a C score for this indicator.

## DPI 2.2 - Managerial structure for issuing guarantees

**22. The organizational structure for granting loan guarantees and on-lending is clearly established**. SEFIN, through DGCP, is the sole entity responsible for preparing and granting CG's guarantees for debt and on-lending. This is clearly stated within the regulation and both external and domestic guarantees follow the same regulation for guarantees and on-lending (see DPI-1.1). The main unit involved is the middle office, which is responsible for analyzing the potential beneficiary's creditworthiness.

**23. The DGCP issues all guarantees and on-lending.** Once the President and the Legislative have formalized the decision to make these transactions, the DGCP is the only entity that implements them and later registers the transactions in SIGADE and provides reports.

**24. Guarantees were granted during the past five years.** The most recent external debt guarantee (2016) was given to the UNAH, the national university. DGCP analyzed its financial conditions and indebtedness capacity, which allowed a positive technical decision. More than 90 percent of external debt guarantees are granted to ENEE. Guarantees for internal debt have also been given within the past five years, exclusively for ENEE's, which is composed mostly by of bonds issued in the domestic market and a much smaller amount of syndicated bank loans. The nominal amount of external debt guarantees in December 2020 was USD 293 million, or approximately HNL 7,104 million, and of internal debt almost doubling (HNL 15,103 million - see DPI-10 and Annex 3).

**25. A significant amount of on-lending (*créditos reasignados*) has been made, some in the past five years** (Annex 3). On 31 December 2020, CG on-lending totaled HNL38,741 million or USD1,613 million, of which 93 percent corresponds to ENEE (HNL35,903 million or USD1,495 million), consisting in the past mostly of IDB loans, and more recently, a USD700 million loan from BNY Mellon (2017) and a CG Eurobond of USD600 million (2020).

**26. The score is an A as SEFIN through DGCP is the only entity responsible for issuing both external and internal debt guarantees and on-lending, in addition to centralizing the CG's debt management.** The previous score was a D. The unsatisfactory aspects of guarantees management rest to the operational area and have been reflected in the assessments of DPIs 1.1 and 10.1.

### DPI 2.3 – Staff and Human Resources

**27. The DGCP has a total of 39 employees divided into three main areas, front (11), middle (4) and back office (12)** – See DPI 2.1 for a complete description. These three departments, in charge of core functions, concentrate 69 percent of all staff. In addition to the Director and Deputy Director, there is an administrative office with 9 employees and one person who manages the debt conversion program with Spain.

**28. According to the staff interviewed, the number of employees in DGCP are sufficient to perform the core functions.** Nevertheless, the workload has increased since COVID 19, the management has shown intentions to hire new staff due to the high volume of funding and analytical work. Moreover, the level of complexity of the operations has increased due to the access to new non-traditional creditors that provide less concessional resources.

**29. The recruitment process is competitive and is led by the Human Resource (HR) department within SEFIN.** There are two hiring processes: directly from outside SEFIN or as civil servants. The first seeks qualified personal from outside the bureaucracy, for example from the private sector. The civil service route follows the regular hiring method for public officials, who may eventually move up the ranks of the DGCP, as in the case of the current Director and Deputy Director.

**30. Staff turnover is low, as on average employees remain for 12 years.** However, key staff from the middle office are often transferred to other areas within the SEFIN; given the complexity of the middle office functions, this could represent a certain level of risk.

**31. According to the staff interviewed, training is required in the middle office to assure new employees can use all the tools available in that area.** The DGCP has access to online training from the WB-IMF, but as most courses are offered in English, participation is limited. Other key capacity-building areas include training in the new DSA framework, MTDS and Excel macros for generating debt projections.

**32. Currently, career plans are under development and training plans are discussed with the staff at the beginning of the year.** Key staff are fairly experienced and core functions are performed without any interruptions. As the level of complexity of the debt portfolio changes, more training will be necessary. Annually, the SEFIN staff are evaluated by HR.

**33. Employees are required to sign a code of conduct, which is binding for all SEFIN staff.** The code is not specific to debt-related transactions, but addresses issues related to information confidentiality and disclosure.

**34. Salaries are considered to be competitive**. This is shown by the hiring of a private sector expert in recent years and the relatively low staff turnover ratio.

**35. In sum, DGCP staff are specialized and can perform all core debt management functions and the score is a C**. The recruitment process followed is acceptable and turnover ratio is low. At the beginning of the year training plans are discussed with the personnel who performs according to job descriptions. All staff must sign a code of conduct, a confidentiality agreement and there has been no evidence of misconduct. Higher scores could be achieved if career plans were in place. This indicator was not rated in the previous assessment due to methodological changes.

## DPI 3 - Debt Management Strategy

| DPI | Score |
|---|---|
| 3.1 - The quality of the DM strategy document | **A** |
| 3.2 - The decision-making process and publication of the DM strategy | **D** |
| 3.3 - The Annual Borrowing Plan | **C** |

### DPI 3.1 - The quality of the DM strategy document

**36. Honduras has been annually designing a Medium-Term Debt Management Strategy (MTDS) since 2015 for a 4-year horizon.** The latest strategy document at the time of the mission covers the period 2020-2024, assessing and updating the previous MTDS for the years 2019-2023[13].

**37. The scope of the strategy is the Non-Financial Public Sector (NFPS) debt, including domestic and external debt according to currency denomination/exposure.** The current regulatory framework described in DPI 1 enables the DGCP to elaborate and implement the borrowing plans for the Central Government (the most representative government level) while controlling the borrowing activities undertaken by other government entities (see DPI 6). In effect the DGCP monitors the debt cash flows for the entire public sector and the document highlights the composition of the existing debt portfolio and identifies cost and risk indicators using the WB-IMF MTDS Analytical Tool (AT). Namely, foreign exchange, refinancing and interest rate risks are measured, as well as maturity profile and creditors disclosed.

[13] https://www.sefin.gob.hn/politicas-y-estrategias/ sections 3 and 4.

**38. Fiscal and macroeconomic projections used in the MTDS are consistent with figures assumed in the Macro-Fiscal Framework (2021 – 2024) and other policy documents.** Specific numbers for 2020 and 2021 are shown at Table 6 of the MTDS document. A baseline and (described) shock scenarios for interest and exchange rates are assumed in the simulation of alternative strategies, and a detailed discussion about external and domestic sources of funding is also presented. Expected external financing is detailed by creditor and consistent with the 2020-2023 Public Indebtedness Plan. Domestic instruments by tenor and interest rate type is also defined as part of the strategy.

**39. Four alternative strategies are thoroughly described in the MTDS document, the first of them considered as the baseline.** All strategies are assessed according to cost and risk indicators (under a baseline and shock scenarios) and the rationale for choosing a preferred alternative is provided. There is also a description of government policies and actions needed for the implementation of the strategy, including the ones related to the development of the domestic market. For example, the creation of benchmarks and the establishment of a well-defined term structure; improving liquidity in the domestic market; enhancing transparency for market participants. The implementation of specific actions on those areas have improved the activity in the domestic market amidst the challenges imposed by the pandemics in 2020 (see DPI 8).

**40. Quantitative strategic targets for debt levels and cost-and-risk indicators are specified[14].** Targets for the minimum share of debt denominated in local currency, ranges for the debt average time to maturity, the share of debt maturating within 1 year and within 3 years, as well as a minimum share of debt hired on fixed rate terms are defined. Targets for debt levels and debt service are deemed to be realistic and are also published.

**41. Considering the elements above mentioned, Honduras Debt Management Strategy document present all the needed requirements for the A score.** The previous assessment granted a D score and the improvement in the debt management strategy results from capacity building activities, management support to produce and publish a DMS and enhanced coordination within other branches within SEFIN.

## DPI 3.2 - The decision-making process and publication of the DM strategy

**42. The debt management strategy is prepared by the Debt and Risk Management Department (*middle-office)* of DGCP, according to internal regulations[15].** This regulation provides details about all the steps to be undertaken for the three involved tasks: i) collection and production of needed data for the design and update of the MTDS; ii) analysis and write-up of the MTDS document; and iii) publication of the document. The above-mentioned tasks are then broken down into thirteen sub-tasks where their description, responsible areas and an estimated range of days needed to conclude the sub-tasks are provided.

**43. The debt management strategy has been annually updated and published on the Finance Secretary official website, but the BCH's views are not obtained. The score is a D.** The DMS is formally approved by the Undersecretary of Public Credit and Investment (Vice-Minister) conferring ownership

[14] Pages 23-34 of the DMS.
[15] *Procedimiento* PRO-DGCP-GDR-01, April 2019.

and accountability for the approved strategy. The Central Bank (BCH) plays an important operational role on debt auctions, but its participation on the debt planning is missing. Consulting the BCH would grant the highest score for this indicator. This indicator was not assessed in the previous DeMPA because there was no strategy in place.

### DPI 3.3 - Annual Borrowing Plan (ABP)

**44. Honduras has developed and published an Annual Financing Plan (PF) since 2014, according to documents available at SEFIN's website[16].** The Financing Plan presents a breakdown between domestic and external financing by type of debt instrument, and follows what is established in the General Annual Budget. The breakdown in terms of external debt loans and bonds are consistent with the Public Borrowing Policy (PEP).

**45. The Financing Plan (PF) defines a detailed strategy for the issuance of domestic bonds.** Benchmark tenors (3 to 15 years) are defined, along with ranges for the share of each instrument over the total expected domestic financing. Moreover, the coupon for each instrument is already specified. The plan provides flexibility for SEFIN to access other domestic sources of funding. Domestic borrowing is expected to be fully undertaken by using market-based instruments.

**46. The implementation of the PF is monthly followed by the *front-office* and reviews are published if needed.** Although market participants have mentioned the frequency of auctions have increased towards the end of the fiscal year[17], the ABP has been fairly adhered to. Quarterly debt bulletins inform the updated progress of the debt plan execution contrasting domestic bond issuances against the annual financing plan.

**47. The minimum requires are met and the score is a C.** Higher scores would require the ABP (or PF) to present key cost and risk indicators for the portfolio at the start of the year and estimate those indicators for the end of the year. Detailed information about indicative volumes/shares of the issuance of domestic instruments by tenors is currently provided in the PF document, and the breakdown about external debt borrowing through loans and bonds is publicly available. The connection of this data with information about the existing debt portfolio available at the MTDS document facilitates the calculation of the required risk indicators. This was not rated in 2013 due to methodological changes.

## DPI 4 - Public Debt Reporting

| DPIs | Score |
|---|---|
| 4.1 - Central Government (CG) debt report - Content and timeliness | **C** |
| 4.2 - Reporting to the legislature | **B** |
| 4.3 - Public debt report – Government coverage | **D** |

[16] https://www.sefin.gob.hn/politicas-y-estrategias/

[17] The main reason for that is that the issuances were front loaded and reached the yearly maximum budgetary limit.

## DPI 4.1 - Central Government Debt: Content and timeliness

**48. Honduras has many products related to transparency,** that together provide information on (a) Stock (composition and type of instrument; currency denomination; creditors); (b) Flows (maturity profile; principal and interest)[18]; (c) Costs[19]; (d) Guarantees[20]. SEFIN (DGCP) regularly publishes individual reports on:

i. the execution of programs and projects externally financed
ii. quarterly standard debt indicators
iii. annual stock of guaranteed/on-lent debt

**49. Risk indicators, historical series of the main stock and flow indicators are also available respectively in the DMS (strategy) document and the Quarterly Debt Reports** that stretches back to 2005. All information is publicly available at the official website.

**50. Debt reporting is very detailed in Honduras and the score is a C.** If the guaranteed stock were to be published at least semi-annually, in line with the methodology, the score could have been an A. The guaranteed portfolio could be published in the degree of details evidenced to the mission, e.g., showing the beneficiaries, terms and conditions etc. (see Annex 3). The score from last assessment is not comparable due to methodological changes.

## DPI 4.2 - Reporting to the Legislature

**51. Section III.1 of the PEP provides an annual report of outstanding debt and main DM operations.** The content shows the evolution of the debt on a yearly basis for the CG. The report is part of the legal structure of authorizing documents provided by the LOP and the LRF and it is directed to the Legislature as well.

**52. The PEP also presents the main debt indicators referenced to the medium-term analysis**, describing the pressures over the cash flows over time (see pages 21-22 - section III.1). There are tables showing the outcomes for the last 5 years for selected indicators: debt composition (domestic and external); cost (interest/revenues and average interest rate); debt structure (average maturity); risk exposure (variable and fixed).

**53. The implementation of the PF (Borrowing Plan) is presented in the Quarterly Debt Report - Section III.5[21], showing the outcomes against the planned strategy.** The 3Q edition brings the annual perspective and is mostly centered in the domestic debt because that's where the DGCP have more leeway to actively change the portfolio compared to the external debt, where the strategy consists in maximizing the concessional envelope. Details on Eurobonds and recent transactions are presented in the Quarterly Report. External debt disbursements follow the estimates set in the PEP. The reports are sent to the Legislature within days after the publication and the last quarter takes into account the developments in the year against the strategy.

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[18] See Debt Quarterly Reports
[19] See DMS
[20] See PEP
[21] https://www.sefin.gob.hn/informes/ - *Informe Trimestral de Deuda Pública de la Administración Central.*

**54. The level of debt transparency in Honduras has increased over the years and the score is a B.** Although the Quarterly Debt Report contains sections that describes the outcomes compared to the DMS, there is no fuller discussion of the deviations from the targets and implications for the future, which could be presented in a standalone document. As it stands the Legislature benefits from existing reporting has an active role in approving borrowing and is informed timely about debt operations. As such, reporting is considered sound. This indicator was not rated in the last assessment due to changes in the methodology.

### DPI 4.3 - Public Debt Report: Government Coverage

**55. The initial sections of the PEP show debt stocks and currency denomination for the CG, discerning the outstanding debt instruments.** However the mission acknowledged there exists unreported liabilities reaching HNL 10 bn (USD 415 million -1.76% GDP) that is not captured in the debt stock. About half of those liabilities consists of a flow of expenditures that are delayed and cleared, in accordance with the LOP and the regulations binding to the Treasury financial programing (*Subsistema de Tesorería).* The remaining part consists of past fiscal arrears (with suppliers) that has not been reported.[22]

**56. The General Government (GG) debt stock can be computed based on the local government (LG) debt published in the PEP – Section III.2.[23]** The document explains the dynamics of the LG debt by showing the borrowing activities with the SFN (National Financial System). Local governments mostly borrow from domestic banks to finance infrastructure projects and must provide information to SEFIN, who engages with the banks to complete the debt dataset when necessary. Local governments currently do not borrow directly from external creditors. A historical series of GG debt (domestic and external) can be found on SEFIN's website[24].

**57. Domestic and external debt for other Non-Financial Public Sector entities are included in PEP's Section III.3.** There is information on the stock, variation factors, creditor structure (on-lent obligations to the CG, SFN, other). The report brings data since 2017 for the whole group and singles out the ENEE (the main SOE). In this case, the debt is segregated by securities and loans.

**58. The coverage of the public debt data reaches all NFPS entities. However, because there are unreported fiscal arrears in the CG total debt, the criteria is not met and the score is a D.[25]** The authorities have advised that there is an ongoing task force to scrutinize the stock of arrears and there is an internal decision to publish the numbers after the work is completed. Once the total CG debt stock reflects the arrears, the score could reach the highest level. This indicator was not assessed in the previous assessment due to methodological changes.

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[22] The mission was advised that the past fiscal arrears (about HNL 5 bn) has been an object of forensic audits and shall be written off the government's balance sheet if remains unclaimed, as it would not configure an outstanding liability.

[23] GG= CG + LG.

[24] https://www.sefin.gob.hn/informes/

[25] Note that CG debt includes debt instruments and other types of liabilities.

## DPI 5 - Audit

| DPI | Score |
|---|---|
| 5.1 - Frequency and comprehensiveness of external audits (Financial, Compliance, Performance) and their public disclosure | C |
| 5.2 - Degree of commitment to address audit outcomes | D |

### DPI 5.1 - Frequency and comprehensiveness of external audits (Financial, Compliance, Performance) and their public disclosure

59. **In Honduras, the highest audit institution is the Supreme Court of Accounting (TSC), responsible for undertaking external financial, compliance and performance audits on DM transactions.**[26] The TSC is an autonomous public entity, governed by three magistrates. The President of the Republic nominates each candidate and the Legislature must ratify them with at least 67 percent of the total votes. Each magistrate is elected for a period of seven years and the presidency is rotated every year among its members.

60. **The TSC is responsible for *ex post* supervision of the use of public resources managed by the state, municipalities and other institutions**. In reference to performance audits, the TSC has not engaged in this type of evaluation; most of the work related to public debt operations is focused on legal compliance and financial audits. There is a department dedicated to auditing public debt operations. The main function of the team is to analyze and verify public debt data. According to the 2020's annual report for 2020, the department has 13 employees. Individual auditors are present in both the BCH and the SEFIN and undertake the audits. The mission was informed that both auditors have complete autonomy and cannot be removed by the organization. If a conflict arises, then it should be reported to the TSC where the case would be evaluated by the magistrates.

61. **The TSC conducts yearly financial and compliance audits of debt management activities**. A yearly report includes a chapter on public debt activities and the document must be presented to the Legislature by July 31st of every year. The scope of the report includes a comparative analysis of public debt stock in relation to previous years, consolidation of debt stock within SIAFI-SIGADE and in 2019 evaluated the internal controls of the DGCP. Also, the report includes an analysis of debt service payments, evolution of macroeconomics conditions and it calculates financial ratios to evaluate the evolution of debt stock.

62. **The financial audit consists of consolidated financial statements of the public administration based on the numbers prepared by the accounting division within the SEFIN**. The statements reflect short and long-term liabilities, and breaks down the composition of CG debt into domestic and external and are compared with the records in the PFM and Debt systems. Some financial ratios are estimated for the debt stock and external debt service, and an evaluation is made of the financial conditions of external credit. Other aspects are presented within the document, such as the debt profile, interest rate, public debt composition, disbursements and external guaranteed debt. In reference to the domestic debt, the report maintains a similar structure to the external debt section. Debt service payments are compared to the original budget estimates and the eventual differences are explained.

[26] TSC's Organic Law (Decree No 10-2002) Article 3.

63. **An external compliance audit is conducted every year**. The TSC ensures compliance with the relevant laws and debt related documents, including the LOP, LRF, PEP and EDMP. For example, in chapter II: "*Resultados del Examen de Rendición de Cuentas, subsection A Endeudamiento Público de la Administración Central",* TSC states that all public sector institutions must comply with the EDMP. Additionally, the report, in page 280, gives a brief description of the relevant laws and norms that must be followed to maintain the government finances healthy. Finally, the report states that in the last four years, the Central Government has complied with the parameters established in the PEP 2016-2019 in relation to the fiscal deficit.

64. **Audit reports are publicly available on the TSC's website within six months after the final report is presented to SEFIN**[27]. According to the staff interviewed, after the audit report has been formally submitted to the audited institution the report is uploaded on the website.

65. **Both external financial and compliance audits are conducted each year and the report is public granting a C score**. For a higher score, a performance audit would be necessary in the past three years. The score was a D in the previous assessment.

### DPI 5.2 - Degree of commitment to address audit outcomes

66. **SEFIN/DGCP have 15 days, after notification, to provide a plan detailing the actions and a timetable to address the findings of the audit report**. Article 79 of the TSC's organic law states that all subject institutions are obligated to comply with the request made by the audit institution.

67. **The mission requested the action plan to the DGCP but no evidence was shared and the score is a D.** To the extent that the audit report has not been officially received by the DGCP to prepare an action plan for 2021 and onwards, the mission requested evidence from past action plans. The requests were made both in the written and oral forms. The mission did not have access to any plan and the lack of information yielded the score. This indicator was not assessed in the previous DeMPA.

## IV.2. Coordination with Macroeconomic Policies

### DPI 6 - Coordination with Fiscal Policy

| **DPI** | **Score** |
|---|---|
| 6.1 - Provision of debt service forecasts | **A** |
| 6.2 - Fiscal Risks monitoring in the NFPS | **B** |
| 6.3 - Availability of key macro and fiscal variables and DSA | **A** |

[27] https://www.tsc.gob.hn/web/Rendicion_de_cuentas/ 2019/Informe-Consolidaddo-RC-2019.pdf

## DPI 6.1 - Provision of debt service forecasts

**68. The DGCP estimates the debt service for the CG debt**. The estimates are requested by the Macro-Fiscal Policy Department (DGPMF) to prepare the budget numbers and to consolidate the debt projections and limits appearing in the PEP encompassing the CG and the remaining NFPS. The estimates stretch to the medium term as well.

**69. The debt service estimates are based on the macroeconomic forecasts used for the budget.** The DGPMF triggers the process of preparing and presenting to the DGCP the expected borrowing needs and the official macroeconomic assumptions, following the instructions of the LRF and its regulations, which are incorporated in the Mid Term Fiscal Plan -Section 5 (*Marco Macro Fiscal de Mediano Plazo* – MMFMP*)*[28]. The document is very detailed and has many estimates on the revenue and expenditure side, with breakdowns of the main types of revenues and expenditures, besides an analysis of the domestic and external economic outlook.

**70. The same macroeconomic assumptions are used in the budget, in the PEP, in the DSA, besides the EDMP and the FP (financing plan)**. The BCH contributes to forecast the foreign exchange rate for the relevant period. The mission obtained evidence of the assumptions as the PEP has to come out until June of each year (the budget preparation starts on February). For instance, Section 10 of the MMFMP presents debt paths that are consistent with the other documents mentioned above, in particular the PEP, ensuring that there is coordination between the key assumptions and debt service.

**71. The DGPMF undertakes debt service sensitivity analysis from different scenarios for key macro-fiscal variables, including interest and foreign exchange rates.** The analysis includes shock scenarios. Table 2 of Section V of the PEP shows the baseline and alternative scenarios and shocks (*pruebas de tensión*), which are well represented from 2021-2041. The main variables are GDP growth, primary balance, FX-rate; interest and other flows incrementing the debt stock and generating a series of debt service estimates. Such estimates are published yearly in the context of the PEP and the DSA (see DPI-6.3).

**72. The DGPMF and the DGCP are well coordinated which facilitates the dissemination of debt service estimates and macro-fiscal assumptions and the score is an A.** The DGPMF centralizes and consolidates the forecasts which end up populating the key policy documents in the context of the budget, and medium-term fiscal planning and debt management strategy. There are detailed fiscal projections to the entire NFPS. This indicator is directly comparable with the previous assessment due to methodological changes.

## DPI 6.2 - Fiscal Risks monitoring in the NFPS

**73. The DGPMF (SEFIN) is responsible for collecting information about the largest public entities.** To produce the PEP the central authority accounts for all government related entities, namely the local governments (there are 298 municipalities and only 68 with outstanding debt) and 9 SOEs (where ENEE accounts nearly to all of it) and other decentralized entities (which are included in the PEP). The coverage of the NFPS is deemed to be complete.

[28] https://www.sefin.gob.hn/documentos-e-informes/

**74. SEFIN has published a Fiscal Risk Statement (FRS) for the NFPS as of Sep-2020.**[29] The document t includes an analysis of the CG explicit contingent liabilities (CLs- representing 31 percent of GDP) grouped into (a) PPPs -Public Private Partnerships; (b) Legal Claims; (c) Guarantees provided by the government. There is a section dedicated to implicit CL (3.3% of GDP) grouped into (d) SOEs debt; (e) Municipal Debt; (f) Public Banks – BANADESA and BAHPROVI; (g) Public Funds (Trusts-*Fideicomisos*). For each group, the FRS reports the main factors causing the risks in percentage of GDP and the maximum CG exposure if the state of the nature is unfavorable.

**75. SEFIN also publishes a report on the financial management and the risks associated with natural disasters**. The objective is to integrate policies that could reduce fiscal risks, strengthening public finances and respond to natural disasters effectively. There are five main strategic areas considered in the document: (a) Increasing awareness; (b) Strengthening the financial management in responding to the disasters; (c) Reducing the risk though public investments; (d) Increasing budget transparency when using public resources to offset natural disasters; (e) Strengthening the institutional capacity to manage this type of risk. To offset eventual disasters, the document lists a number of financial alternatives, including accessing donations and IFI contingent lines, together with budget reallocation, emergency funds, linking each funding to the expected severity and frequency of the event.

**76. Financial ratios of the main SOEs are not published and the score is a B.** No quantitative analysis of the SOE's performance is reported. Articles 20-21 of the NTSCP require computing some ratios such as Ebitda/ Debt and Assets/ Debt to assess the credit risk of such entities and to evaluate fiscal risks and conducting credit risk assessment for SOEs when borrowing. However, the fiscal risk unit (*Unidad de Contingencias Fiscales* -UCF/SEFIN) does not publish such ratios. The mission noted that the FRS analyzes the main Contingent Liabilities by each type of public entity, revealing the maximum exposure that could require budgetary resources. Key financial ratios for the SOEs and a quantitative analysis should be published for reaching the maximum score. This indicator was not assessed in the previous DeMPA due to methodological changes.

### DPI 6.3 - Availability of key macro and fiscal variables and DSA

**77. Key macro and fiscal variables are shared with the DMO annually, which is the same frequency of the DSA document.** As stated in DPI 6.1, there is a good degree of coordination between the unit centralizing the macro-fiscal forecasts (DGPMF) and the DM unit (DGCP) which undertakes the DSA. The DSA is part of the PEP (Section V) and is very detailed.[30]

**78. The DSA covers the NFPS, which is consistent with the PEP.** The document provides a definition of sustainability, delineates the coverage in line with the remaining policy document, presenting the analysis around five main solvency and liquidity indicators: (a) Debt/ GDP; (b) Debt / Exports of Goods and Services; (c) Debt/ Revenues; (d) Debt Service / Exports of goods and services and remittances; (e) Debt Service/ Revenues. The staff have produced their own DSA, which is in line with the WB-IMF's Debt Sustainability Framework (DSF).

[29] Fiscal Risk Statements and Natural Disaster Financial Recovery – The first is required by the Fiscal Responsibility Law and is an annual document.
[30] See https://www.sefin.gob.hn/politicas-y-estrategias/ . The fiscal risks unit (UCF) also monitors risks from SOEs.

**79. The DSA is updated in light of new borrowings.** Because all domestic and external borrowing has to be in line with the PEP estimates, any sizable new borrowing that could potentially disrupt the expected debt path is captured in the DSA that is published annually. Before an external transaction is undertaken, the DGPMF and the BCH must issue an opinion if the new borrowing could derail the debt trajectory. The opinion also captures the effects on the overall fiscal deficit and monetary policy. The Covid-19 crisis required the DSA to be updated during the course of the year 2020. The fiscal trajectory for 2021-24 was affected by the abrupt reversal of economic and financial expectations, and the effects of 2020's tropical storms (Eta and Iota), thus deteriorating the debt trajectory relative to previous DSA exercises. External borrowing remained mostly on concessional terms while domestic debt increased.

**80. In sum, the comprehensiveness and timeliness of the DSA is very good and the score is an A.** There are detailed inputs on the scenarios showing the variation factors of the NPSD and its flows such as the primary deficit broken-down by revenues (including donations) and expenditures; differential of interest and growth rates; other net flows generating debt (including the recognition of CL). Fiscal forecasts are detailed up to 20 years and includes real GDP growth, nominal and real interest rates; FX-rate devaluation, inflation (GDP deflator); primary spending growth and new external borrowing. The BCH also shares its views related to the BoP in the context of the DSA. Finally, alternative scenarios and stress tests (*pruebas de tensión*) are described, together with many output tables on expected debt paths for all the five solvency and liquidity indicators aforementioned[31]. The score is the same as the last DeMPA conducted in 2014.

## DPI 7 - Coordination with Monetary Policy

| DPI | Score |
|---|---|
| 7.1 - Separation between monetary policy and DM operations | A |
| 7.2 - Coordination with the CB through regular information sharing on current and future debt transactions and the central government's cash flows | D |
| 7.3 - Limits of direct access to CB funding | D |

### DPI 7.1 - Separation between monetary policy and DM operations

**81. The government of Honduras (represented by SEFIN) and the BCH issue their own securities differentiated according to the purpose and to the tenors.** SEFIN has been issuing bonds with tenors from 3 to 15 years[32], but is not active in the short-term of the curve (not even for cash management purposes). The BCH issues their own bills with tenors ranging from 1 day to 9 months and have issued 2-year bonds in the past with the objective of providing price reference to the market in the absence of government issuances in this part of the curve. The Budget Law authorizes a maximum amount of securities to be issued by SEFIN (although it does not consider securities' exchange operations or T-Bills refinancing)[33].

[31] Occasionally the DSA risk was considered moderate under the baseline scenario and could be low under alternative scenarios, which is in line with the WB-IMF' analysis.

[32] Detailed in the Annual Financing Plan (PF) (see DPI 3.3).

[33] According to article 3 of the Rules of Procedure for Public Securities' Negotiation (RNVG) , if bills are issued, they must be repaid withing the issuance year and the issuance must be undertaken in coordination with the central bank for monetary policy purposes.

**82. BCH has announced in March 2021 through its 2021-2022 Monetary Program the intention to use reverse repo transactions collateralized with government securities to dry up liquidity in the financial market.** The use of the new instrument will be gradually implemented, and it also targets the development of secondary market[34] and improvement of monetary policy transmission.

**83. SEFIN is entitled to define government securities issuance amounts, financial characteristics, as well as minimum and maximum prices in the auctions, according to the RNVG.** BCH carries out the auctions as a government (SEFIN) agent and participates in the auction decision meetings, but the final decision on amounts and cut-off rates is made by SEFIN. Market participants consulted by the mission[35] understand that SEFIN is the decision maker and BCH the operational agent for the offerings and settlement.

**84. The relationship between SEFIN and BCH concerning the government securities auctions and BCH role is formalized by the Securities Negotiation Contract *(Contrato Marco de Negociación de Valores).*** The contract is published at SEFIN's website[36].

**85. Given the clear separation between used instruments and performed functions by SEFIN and BCH, and the correspondent formalization and disclosure, the score is an A.** This is an improvement compared to the last assessment which granted a B score.

## DPI 7.2 - Coordination with the CB through regular information sharing on current and future debt transactions and the central government's cash flows

**86. The General Treasury of the Republic (TGR) shares on weekly basis with BCH information about projected cash inflows and outflows.** However, according to the spreadsheet (template) provided to the mission team, this information is limited to expected tax and non-tax revenues, and projected expenditures related to wages, providers payments and transfers, and other payments.

**87. The information provided to the mission does not include cash flows related to debt transactions and the score is D.** Although the DGCP shares with TGR (both housed in SEFIN) information about expected debt issuances and repayments, the monthly cash flow forecast sent to BCH does not include debt related flows -according to the evidence provided. While the frequency of cash flows information sharing with BCH would entice a score B for Honduras, the lack of complete evidence cannot corroborate that and the minimum requirement is not met. The score in 2014's assessment was a C based on the full coordination on a monthly basis.

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[34] Some market participants have manifested that SEFIN´s and BCH´s credit risks are seen differently in the market, with some banks lending just for BCH. There is a clear perception that BCH issuances are exclusively for monetary policy, leading to a perceived lower credit risk given the central bank independence and smaller concerns in case of debt restructuring. The use of government securities by BCH on reverse repo transactions will potentially contribute for the primary and secondary markets of these securities.

[35] *Banco Fichosa*, *Banco Ficensa* and *Banco Atlantida*.

[36] : https://www.sefin.gob.hn/download_file.php?download_file=/wp-content/uploads/2014/03/Contrato_Marco_Admon_Valores_firmado.pdf

### DPI 7.3 - Limits of direct access to CB funding

**88. BCH Law[37] establishes restricted conditions in which BCH can finance the government and official entities.** The monetary authority can provide credit to these entities exclusively by purchasing bonds in the secondary market. However, in case of emergency or severe calamity, monetary financing can be provided through unanimous approval of BCH Directory, ratified by a presidential decree, not applying the above referred mechanism.

**89. According to the BCH Law, the central bank can also exceptionally finance the government for temporary coverage of cash shortages.** This credit line must adhere to the following conditions: i) tenor limited to 6 months; ii) remunerated by market interest rates; and iii) limited to 10 percent of the average tax collection of the previous fiscal year. Likewise, it must be approved by unanimity of the BCH Directory.

**90. Although the legislation in place defines a maximum ceiling and tenore for accessing central bank financing, previous unmatured credit transactions between the government and BCH breaches the restrictions and the score is D.** Two credit lines conceded in 2010 and 2012 by BCH respecting the above-mentioned limits were rolled over by the issuance of government bonds maturing in 2022 and 2025[38]. Although the securitization of the loans have been made more than 3 years ago (time span of DeMPA analysis), the bonds still exist, effectively breaching the maximum tenores for the BCH financing. The DGCP informed that these bonds have not being repaid with cash to provide BCH with more bonds for monetary policy, once reverse repo transactions start to be undertaken. Early redemption of these bonds and the creation of an independent mechanism to the government provide to BCH with the needed securities for repo transactions would meet similar policy objectives without breaching the tenore cap imposed by the regulation, thus leading to higher scores. The score is a D, the same as in 2013.

## IV.3. Borrowing and Related Financing Activities

### DPI 8 - Domestic Borrowing

| Dimension | Score |
|---|---|
| 8.1 - Publication of a borrowing calendar and issuance results | **D** |
| 8.2 - Domestic market operations and clarity in rules and procedures | **A** |

### DPI 8.1 - Publication of a borrowing calendar and issuance results

**91. SEFIN, through DGCP (and BCH as a financial agent), issues government securities in a less predictable and transparent way than prior to the COVID pandemic.** In 2019 SEFIN used to announce the instruments and precise amounts to be offered in each auction for the next quarter. However, auction announcement in 2020 and 2021 became more general due to DGCP's perception of the pandemic's economic effects on the domestic market and the greater uncertainty in placing bonds. As a result, the 2021 annual borrowing calendar provides dates for the auctions (Wednesdays every fortnight) but does

[37] Decree 53, 1950, article 40, modified by Decree 228-96.
[38] Similar operation was undertaken in 2020.

not specify instruments or amounts and the 2021 PF (Financing Plan) includes only a range of the amounts to be placed during the year for each type of instrument (see below). The only occasion when the market is informed of the instruments and precise amounts to be auctioned is when SEFIN announces the auction five days before the event, but for one auction only (i.e., one fortnight) and not for the whole month. Thus, the minimum level of transparency and predictability is not being complied with.

**Figure 6 - Range of amounts (% of total authorized) to be auctioned in 2021**

| Maturity (years) | Currency | Ranges | Coupon (%) |
|---|---|---|---|
| 3 | Lempira | 5-15% | 6.0 |
| 5 | Lempira | 15-25% | 7.0 |
| 7 | Lempira | 15-25% | 7.7 |
| 10 | Lempira | 25-35% | 8.5 |
| 15 | Lempira | 15-25% | 9.0 |
| **TOTAL** | | **80-100%** | |

Note: the 2021 PF (Financing Plan) includes only a range of the amounts to be placed during the year for each type of instrument. Source: DGCP - PF 2021

92. **Even before the pandemic, however, the calendar for domestic wholesale securities issuance was not being followed in terms of dates, thus weakening the predictability of the CG's auction program.** No auctions were held in December 2019 and during the last quarter of 2020 detaching from the calendar. According to DGCP, the 2020 ceiling for internal debt was reached by September and even though market participants were informed at the time, they expressed concern with a relative weak predictability. In 2019 the CG placed larger amounts of bonds that those announced for specific auctions, citing high demand levels. Since February of this year SEFIN is limiting issuance to the amounts previously announced, despite exceptionally high demand. Even with this change, however, market participants are uncertain if the government will continue with its auction program through to December. Another factor that has heightened the unpredictability towards the year end is that ENEE issues bonds in the market with a CG guarantee and the assistance of SEFIN39 (see DPI-10). These operations have been supported by SEFIN and have contributed to an absence of CG auctions in December to avoid competition with ENEE. Market participants have mentioned they were often surprised by such operations.

93. **The results of the securities issuance are published on the day of the auction to all participants at the same time.** The auction results are published on the official SEFIN website with information of the volume of bids received and securities issued, cut off rate, minimum, maximum and weighted average of rates) [40] thus contributing to the market's transparency and reducing risk for the participants. [41]

[39] If ENEE defaults on its bonds, the STA of the government is automatically tapped to make payments to the bondholders.

[40] Market participants are interested in being informed of the results of the bids placed by all market participants, regardless of whether they were successful or not.

[41] Market participants mentioned that although they receive the communication by the BCH of the auction results on the same day, there can be some delay, once even at 7 pm, generating uncertainty for the financial entities that participated in the bidding. The results are usually shared by BCH between 4-5pm. DGCP informed of that exceptional event, caused by problems of the Securities Depositary of the BCH, which in any case was resolved that same day.

**94. In sum, improvements are necessary to provide the minimum level of transparency and predictability for this indicator and the score is a D.** At a minimum, the auction calendar should specify issue dates and instruments for the following month and be published at least one week ahead of the start of that month. In addition, the annual auction calendar must be followed for a definite score improvement. A positive aspect is that the auction results are still published on the same day of the auction on the official SEFIN website; this would contribute to a score of B once the publication of the auction calendar is improved and the calendar is followed. This indicator is directly comparable with the previous assessment due to methodological changes.

### DPI 8.2 - Domestic market operations and clarity in rules and procedures

**95. Central government domestic borrowing activities are mostly transparent and conducted through market-based instrument, although in 2020 one quarter of placements were made through direct issuances or exchanges with Central Bank as tenor (referenced to the market rate).** According to the PF 2021, about HNL 22,733 million should be financed through competitive auctions; direct placements should not be made except for liability management purposes. In 2020, 76 percent of total bond placements was made through 17 competitive auctions, and the remaining 24 percent (HNL 6,907 million) corresponded to debt exchanges negotiated directly with Central Bank issued for the fulfillment of the BCH recapitalization agreement recapitalization and liability management purposes, priced by DGCP according to market conditions. On the operational level, the DGCP calculates the prices of these transactions according to the prevailing interest rates and scrutinize the offers and decide on the prices and volumes. The BCH is (Depositario de Valores) informed about the results for registering the operations.

**96. DGCP issues bonds with maturities from 3 to 15 years, while the BCH issues T-Bills and 2-year bonds as part of its monetary policy program** (See DPI 7). In 2021 HNL 7,842 million was extraordinarily raised as an emergency measure for the pandemic[42].

**97. Written rules of business are prepared for all domestic borrowing operations and made public, as are the terms and conditions of the instruments issued.** The RGNV establishes the terms and conditions of T-bills and bonds,[43] including inflation-indexed bonds (the latter with links to a technical note produced by SEFIN) as well as the mechanism of auctions and direct negotiations; it also defines operations of debt buy-backs and exchanges and their modus operandi. Operating procedures are also found in the *Reglamento de Depositaria de Valores* of BCH, including among its services placements via direct negotiations, which is how debt exchanges and buy-backs are carried out. The BCH website has the forms for investors to present offers, with detailed instructions on how to do so. Auction offers are received from 9 am until 11:15 am, , the offers are communicated to SEFIN by 1 pm, the decision of the

[42] In 2020 the other exception was the loan from BCH from previous years that had been converted into a 5-year bond (source – PEP 2021)

43 The RGNV includes a description and the form of the various instruments; calculation of settlement prices and yield rates; computation of interest payments and accrued interests; day count conventions and eligible investors.

cut-off price is taken by the SEFIN (DGCP) and communicated to BCH by 3 pm[44] although sometimes this is done one or two hours later. Market participants were satisfied with the transparency and know how to be involved in debt operations[45].

98. **Internal procedures are clear.** A procedures manual for domestic borrowing was updated in April 2019 that includes procedures for auctions, direct placements and other liability management operations. Once Congressional approval for the annual Budget is given, the DGCP draws up a draft of the Minutes of Agreement that formalizes the amounts to be placed and the Minutes for Securities Issuance, that is revised by the Unit of Legal Advisors and then by BCH, returned to SEFIN for the Secretary's signature, and then for the signature of the President of BCH. The auction process begins with DGCP sending a request for the auction announcement to the BCH, which after revision is published. The offers are received, the price cut-off decision made by SEFIN committee (see above) and BCH proceeds with the operational placement of the bonds, and the information is sent for registration in SIGADE/SIAFI. In the case of debt exchanges, the DGCP establishes the price of the relevant bonds beforehand, and through the BCH sounds out potential investors. Once SEFIN takes the decision on prices and volumes, the BCH carries out the operation, which is then registered in SIGADE/SIAFI.

99. **DGCP regularly interacts with market participants.** DGCP meets twice a year (beginning and mid -year) with market participants to exchange views on the borrowing plan and its execution. These meetings include the financial sector, pension funds, exchange brokers, insurance companies, cooperatives and other interested investors. Participants were satisfied with this arrangement although they felt that the December meeting had a large input of marketing for the ENEE bonds. Participants considered that the current DGCP arrangements for continuous communication throughout the year were satisfactory, allowing for prompt reply to their queries.

100. **In sum, there is considerable clarity on domestic debt operations for all stakeholders and the score is an A.** Official websites provide terms and conditions for all instruments and borrowing guidelines in general. An updated procedures manual for domestic borrowing is in use, there are meetings of DGCP with market participants each semester with good communication throughout the year, all of which contribute to the highest score. This indicator is directly comparable with the previous assessment due to methodological changes.

## DPI 9 - External Borrowing

| DPI | Score |
|---|---|
| 9.1 - Organizational arrangements and processes for external borrowing; financial analysis of terms and conditions | **C** |
| 9.2 - Availability and degree of involvement of legal advisors before signing the loan contract | **B** |

[44] *Oficio de Adjudicacion de Subasta*
[45] There is no Primary Dealership program as of 2021.

## DPI 9.1 - Organizational arrangements and processes for external borrowing; financial analysis of terms and conditions

**101. Staff responsible for executing transactions are authorized to perform this role and is able to articulate the necessary steps to undertake the transactions.** The DGCP is authorized to issue external debt (DPI-1) and within DGCP the borrowing responsibilities correspond to the front office department in charge of external debt borrowing (DGNFE).[46] The DGCP follows a clear process for external borrowing as each step for external debt issuance is established in the LOP, NTSCP, and, in a more detailed manner, in the Procedures Manual for External Debt.[47] The maximum amount of external debt authorized for the year is included in the PEP, in terms of i) ceilings for loan disbursements of programs/projects; ii) ceilings of new loans for programs/projects; and iii) ceilings for budgetary support (loans and sovereign bonds).

**102. The procedure for new borrowing was clearly articulated by the staff.** From the highest level, the Presidential Direction of Planning, Budgeting for Results and Public Investment[48] must provide a certification of the Strategic Alignment of the new borrowing. Subsequently an internal SEFIN committee of budgetary appropriation issues the Technical Note confirming the financing's fiscal space, while DGIP[49] of SEFIN certifies the priority of the project/program being financed. After the financing request is sent to the lender and a draft contract received, the DGNFE staff review that the proposed new debt is compatible with the PEP, the EDMP, the annual FP and the Public Investment Program. The DDR[50] staff carry out the concessionality analysis to comply with regulations and ensure a minimum grant element of 35 percent with the option to comply with this requirement in aggregate if several sources are pooled to finance a given project/program. NTSCP also allows contracting non-concessional lending if the overall portfolio weighted average grant element is above 25 percent. In addition, the DGPMF and the BCH must issue a formal opinion on the new financing's effect on the fiscal deficit and on monetary policy, respectively. The negotiation itself includes a discussion of the level of concessionality required, the conditions prior to the first disbursement, the national counterpart's obligations and the responsibilities of the parties involved, resulting in the final version of the contract. The President issues an Executive Agreement that authorizes the Secretary of Finance to sign the external loan contract on behalf of the government. Subsequently, the signed contract is sent to the Legislature for ratification through a Legislative Decree that is published in the official gazette and then it is forwarded to the Attorney General's office for a legal opinion that guarantees the transaction's legality. Finally, the loan's information is summarized and sent to the DO for registration.

**103. Clear steps are also applicable for Eurobond issuance[51].** The Legislature must approve the bond issuance and specify the maximum amount to be placed. The DGCP invites the banks that could potentially place the bonds, receives offers, analyzes them within an internal SEFIN committee, and selects the bank(s), which are then approved by the Secretary of Finance. There are well-defined steps in terms of selecting and contracting domestic and international lawyers, drawing up the Offering Circular and carrying out the necessary due diligence, dealing with the rating agencies, undertaking roadshows, issuing the bond and signing the legal agreements.

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[46] *Departamento de Gestión y Negociación de Financiamiento Externo*
[47] Updated in April 2019.
[48] *Dirección Presidencial de Planeación, Presupuesto por Resultados e inversión Publica*
[49] General Directorate of Public Investment.
[50] Debt and Risk Management Department *(Departamento de Gestión de Deuda y Riesgo).*
[51] Although this is not formally included in the Procedures Manual.

**104. Most external borrowing (75 percent) corresponds to multi and bilateral borrowing (as of March 31, 2021) and an annual analysis is made of the financial terms and conditions offered by these entities**. There is evidence that the EDMP includes an annuall analysis of the currency, interest rate, maturity and grace period of financing of the IDB, WB, CAPEI and bilateral entities such as KfW and Exim Bank of China Taiwan. In addition, updated studies are made of the degree of concessionality of each new borrowing. As sovereign bonds represent 22 percent of total external funding, the international markets are continuously monitored, in particular when a new bond issuance is planned for the year.

**105. In sum, the organizational structure is capable of analyzing the financial conditions and of processing external debt transactions. The score is a C.** Staff responsible for external borrowing are able to describe external borrowing procedures, there is an annual analysis included in the debt management strategy of the terms and conditions of potential sources of funding (as well as more continuous analysis of international markets and of the concessionality of new loans), and staff ensure new transactions comply with the PF, EDMP and PEP. For a B score they staff would have to undertake financial analyses throughout the year and would have to formalize sovereign bond and commercial bank borrowing in the procedures' manual (22 and 3 percent of external debt, respectively). The staff is working on this matter, so this dimension could improve in the future. This indicator is directly comparable with the previous assessment due to methodological changes.

### DPI 9.2 - Involvement of legal advisors before signing the loan contract

**106. Legal advisors provide their opinion both during the loan negotiation process and after the loan has been formalized granting a B score.** According to the procedures' manual, the DGCP must request a legal opinion of the draft contract from the legal unit (*Dirección Legal*) of SEFIN's General Secretariat and there is evidence that this is being complied with. It is only after this clearance is given that the negotiation process can continue with the potential lender, sometimes accompanied by the entity implementing the project/program. There is another instance –but less relevant for this DPI- when a legal opinion is sought, although it takes place after the contract has been negotiated, formalized, signed and registered in SIGADE, and the Legislature has ratified the loan with a Legislative Decree to be published in the official gazette. In this moment, the DGCP requests a legal opinion from the Attorney General of the Republic to confirm the legality of the operation. However, what is relevant for this sub-DPI is that SEFIN's internal legal unit provides a legal opinion of the draft contract during the negotiation process. The score was upgraded from the last assessment which rated a D for the equivalent indicator.

## DPI 10 - Guarantees, On-lending and Debt-related Transactions

| DPI | Score |
|---|---|
| 10.1 - Issuance of loan guarantees | D |
| 10.2 - On-lending operations | D |
| 10.3 - The use of derivatives | NA |

## DPI 10.1 - Issuance of loan guarantees

**107. Although a regulation on loan guarantees exists, it is only partially followed.** The procedures for the issuance of guarantees are found in LOP, Art.78 and 71, RELOP, Art.22 and the NTSCP, Art. 17-26. The DGCP provides the technical input (indebtedness analysis) prior to granting the guarantee to control for credit risk and registers and provide statistics of all guaranteed operations. However, the ENEE has obtained guarantees without observing all steps defined by the regulation given the weak capacity to repay the government (see DPI 1).

**108. Of the total external debt guarantees (USD 295 million), 90 percent were provided to ENEE (USD 263.6 million.** The internal bonds issued by ENEE, with BCH as an agent, have the GG's guarantee. The total amount of internal guarantees granted to ENEE (nominal debt stock) is HNL 15,103 million, of which a large proportion corresponds to bonds issued in the domestic market, an activity that started in 2016, gained even more importance in 2019 and 2020 and which has always taken place in the month of December. The other type of guaranteed loans corresponds to two syndicated loans organized by FICOHSA BANK for a total of HNL 4,950 million in 2017 and 2018 (See Annex 3 for details).

**109. The process of granting guarantees for the external loans of public sector entities, which requires a prior authorization by the President of Honduras and the Legislature, is clearly established.** The regulation governing CG guarantees and on-lending (as described above) determines that SEFIN, through DGCP, is the sole entity responsible for preparing and granting CG guarantees for debt and on-lending. This is clearly stated with relation to external debt guarantees. Although there is no reference in LOP to internal debt guarantees, SEFIN also centralizes the granting of guarantees of internal debt, deciding to apply the same normative framework used for external debt guarantees, which is backed by NTCP's provisions. A total nominal amount of HNL 22,207 million (not expected loss) is currently outstanding (See Annex 3).

**110. No evidence was provided of an internal DGCP procedures manual for debt guarantees**, only a diagram that describes three general steps for the analysis of a potential guarantee[52] by conducting a credit risk analysis through an evaluation of the beneficiary's indebtedness capacity. A comprehensive framework is lacking for DGCP to guide guarantees and on-lending on the policy level and such policy would typically include: annual ceilings to granting guarantees/on-lending; priority beneficiaries, by type of project and/ or economic sector; creating mitigating factors in case of default (e.g., fees), risk monitoring during the guarantee's life, reporting, etc.).[53]

**111. As previously discussed, the guarantees granted to ENEE reflect a policy decision that marginalizes the technical input of the DGCP so that in practice the regulations are not fully followed, leading to a D score.** The guarantees granted to ENEE were approved by the President of Honduras and the Legislature and made as "exceptions" to the normal procedure that should include DGCP's technical indebtedness analysis. However, ENEE has been facing structural financial problems and lacks the audited financial statements required for the credit risk analysis. In sum, the minimum requirements are not met despite the fact the technical staff is able to articulate the steps necessary to issue guarantees. To meet the minimum requirement, all entities should comply with the regulation binding to guarantee's issuance. The score remains the same as in the last DeMPA under similar rationale.

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[52] The diagram refers to "avales" considered equivalent to guarantees.
[53] See DPI 1.1.

## DPI 10.2 - On-Lending Operations

**112. There is clarity on the decision-making processes for undertaking on-lending credit and the operations follow the policy in place.** There are clear on-lending procedures, found primarily in LOP, its Regulations, the NTSC and the procedures manual for external debt. The most important part of the procedure is the analysis of the beneficiary's capacity for indebtedness that summarizes its credit risk, as with guarantees.

**113. A significant amount of on-lending (*créditos reasignados)* has been undertaken recently.** On 31 December 2020, there was a total nominal amount of HNL38,742 million or USD1,613 million on-lent, of which 93 percent corresponds to ENEE (HNL35,903 million or USD1,495 million), mainly from a N. York Mellon loan and one Eurobond placed in 2020, as well as various smaller IDB loans (See Table 4 of Annex 3).

**114. The DGCP staff is able to articulate the decision-making process for on-lending and can refer to the regulation that applies to this process, but as in the case of loan guarantees its technical input and responsibility in the process is not being fully implemented- the score is a D.** In the case of ENEE, the middle office should be analyzing its indebtedness capacity, but it lacks the audited financial statements necessary for the evaluation, and in any case it is understood that the evaluation's result would be to not authorize the transaction due to ENEE's weak finances. Nonetheless, the Legislature and the President have taken the decision to authorize on-lending to ENEE, so the DGCP grants the on-lending, registers the transactions in SIGADE and produces statistics. To meet the minimum requirement, all entities should comply with the regulation binding to on-lending credit. The score remains the same as in the last DeMPA under similar rationale.

## DPI 10.3 - The Use of Derivatives

**115. There is no reference to derivatives transactions in the LOP, although the PEP does mention that financial derivatives contracts may be made (pg. 29).** In any case, as there are no outstanding derivatives and there is no intention to use such instruments in the coming future, the score is NR- the same as in the last DeMPA.

## IV.4. Cash Flow Forecasting and Cash Balance Management

### DPI 11 - Cash Flow Forecasting and Cash Balance Management

| DPI | Score |
|---|---|
| 11.1 - Effectiveness of forecasting the aggregate level of cash balances in government bank accounts | D |
| 11.2 - Decision of a proper cash balance (liquidity buffer) and effectiveness of managing this cash balance in government bank accounts (including the integration with any domestic debt borrowing program, if required) | D |

### DPI 11.1 - Cash Flow Forecasting

**116. TGR develops a cash flow forecast for the full budget year with daily breakdown of flows and daily updates.** Once the budget is approved, it underpins an annual cash plan, which is then turned into an annual cash flow forecast. The forecast is based on historical daily patterns and up-to-date estimates from the main spending units, and includes a detailed list of above the line items and debt related inflows and outflows which are weekly shared between the TGR and the DGCP.

**117. There is no formal mechanism for information sharing between DGCP and TGR, however the entities meet on regular basis.** Cash flow forecasts inform financing needs and there is good coordination between cash and debt management, despite of some important areas for improvement (e.g. the use of short-term instruments to cover temporary cash imbalances). As a result, the DFCP executes the financial programing and regulates the stream of expenditures according to the forecasts and the fiscal limits.

**118. The Treasury Single Account (TSA) coverage goes beyond the Central Government (CG) cash balances/flows (e.g., it includes municipalities and decentralized entities), but the coverage of cash flow forecasts are limited to the CG** (funds from the other mentioned entities can be observed but cannot be used by the CG). The mission learned from the authorities that the cash flow forecast covers the most relevant flows affecting the TSA, however a historical series of forecast versus realized values were not provided to the mission. The TGR provided a spreadsheet with the cash flow forecast and realized cash flows for 2020 (and deviation between them), however the file did not contain actual numbers and was interpreted as an operational template by the assessment team.

**119. Actual data was not provided to the mission to corroborate the views and the score is a D.** Considering the existence of a cash flow forecast with sufficient horizon, breakdown and updates, Honduras would be well positioned for an A score. However, insufficient evidence of the produced forecast and deviation analysis resulted in a D score. Although there has been significant improvement on how cash flow forecasts are undertaken, the conclusion is similar as in the last assessment in 2014.

### DPI 11.2 - Cash Balance Management

**120. Cash balances are deposited at BCH with no remuneration.** Article 67 of BCH Law prohibit the central bank to pay interest rates to any received deposit. On the other hand, the government pays fees to BCH for its agent role as high as 0.5% of the government domestic debt outstanding. While it has been recently reduced from a previous 1% fee, there is still an unbalanced agreement between SEFIN and BCH in favor of the latter that should be reviewed to consider sound practices.

**121. Temporary cash shortages are covered by the issuance of medium- and long-term debt instruments.** Although T-bills (*Letras*) have been issued in the past, the government of Honduras has just been issuing T-bonds with maturities from 3 to 15 years for cash and debt management purposes. The issuance of these instruments and the coordination between DGCP and TGR have ensured that the government does not incur in negative cash balances. However, the lack of short-term instruments and auctions been carried fortnightly leave low flexibility to the government in the case of unexpected outflows. This is even more critical in the absence of a formalized cash buffer. In some occasions, expenditures payments had to be postponed and cash rationing may be applied (debt service is not subject to such constraint).

**122. Article 56 of BCH law authorizes the investment of government cash balances in the market, but this has not been observed.** BCH acknowledges the existence of such authorization but understands that further regulation is needed before the government starts investing excess of cash in the market.

**123. The score granted is a D because the government cash balances deposited at BCH are not remunerated and no investment is made in the market.** Although there are methodological changes the score is the same as in the last assessment under similar rationale.

## IV.5. Debt Recording and Operational Risk Management

### DPI 12 - Debt Administration and Data Security

| DPI | Score |
|---|---|
| 12.1 - Recording debt-related transactions | **A** |
| 12.2 - Debt payments | **B** |

### DPI 12.1- Recording debt-related transactions

**124. There is an organizational separation for registering debt related transactions.** To initiate the process, one of the front office departments (DNFE) submits the original documents to the DO (back office). The head of the department assigns the case to the officer in charge of that creditor. At this point, the officer checks all original documents to make sure they are complete and in accordance with current practice; if a document is missing, he requests the missing item. Once the information is complete, the officer is authorized to create a SIGADE identification code and inputs the information into the system, thus completing the first step validation. To initiate the second validation process, the DO sends the documents to the Quality Control Department (DCC) for verification. All the documents are checked against the original inputs in the system. If all the information is correct, the DCC signs-off and sends the documents to the DO. Once this step is complete, the unit's head is authorized to complete the operation, and the final registry is created.

**125. The process to record debt related transactions is clearly detailed in a procedure's manual[54] and all debt related transactions are recorded within 30 days (securities are recorded within a week)**. The back office provided evidence that the whole cycle takes less than 30 days. Analogous procedures are followed to register domestic debt transactions (securities). The back office receives the auction's announcement and results and checks against the credit on the Treasury account (*Cuenta de Tesorería*). In addition, the DO registers loan guarantees and on-lending operations. The mission obtained evidence that all debt transactions are recorded within one month and securities are recorded in the CSD within a week of the auction which is replicated in the SIGADE.

**126. The debt recording process complies with best practice and the score is an A**. Due to methodological changes the score is not directly comparable with the previous assessment.

### DPI 12.2 - Debt payments

**127. There is an organizational separation between the payment initiation and processing.** Payments are initiated when the official invoice is received and checked against the registry in the SIGADE-SIAFI[55] interface (amortization table). After the verification process, the DO official generates the documents required and elaborates F-01 form. The system does not allow the official to edit or modify the payment information. It is important to mention that debt payments are based on the information generated by the system, manual adjustments are made manually before they payments are made due to exchange rate. To continue with the validation process, the DO sends, via memo, the documents to the DCC for revision. The information is checked against the original documentation and if correct, the unit's head signs-off and sends the payment notice to the TGR to be executed via the BCH. Debt payments for securities are also prepared based on the system's records and follow similar steps.

**128. The procedures manual is followed, and payments are recorded timely.** The process to undertake and record debt payments is clearly detailed in a procedures manual*, "Registro y Pago Deuda Pública, PRO-CP-OP-01"* that was updated in April 2019. Once payments are made, the BCJ sends a list of executed payments and the information is checked against SIGADE-SIAFI within a week.

[54] "*Registro y Pago Deuda Pública, PRO-CP-OP-01*" that was updated in April 2019
[55] PFM system.

**129. Payment instructions are subject to a two minimum validation process and the score is a B.** To obtain the highest score, the system would have to prepare and issue the order electronically and use a straight though processing. It is understood that the system has an interface with the PFM system, but final payments are adjusted manually before execution, mostly because of different exchange rate cut-off date on the invoices. Due to methodological changes the score is not directly comparable with the previous assessment.

## DPI 13 - Data Security and Business Continuity

| DPI | Score |
|---|---|
| 13.1 - Data access, backups and IT infrastructure | B |
| 13.2 - Business Continuity (BC) and Disaster Recovery (DR) Plans | D |

### DPI 13.1 - Data access, backups and IT infrastructure

**130. There is restricted access to the debt management information system**. The Quality Control Department (DCC) in coordination with the DGCP's administrative team, is in charge of granting access to SIGADE through the assigned desktops. Access to SIGADE is assigned to personal properly identified according to their responsibilities. In case of a new user, the DCC fills out a form detailing the type of permission that should be granted to the incoming staff. Most users are limited to manipulate data based on their job descriptions. To enter the system, an individual password must be assigned and updated regularly to verify access privileges. When leaving the DGCP, the staff goes through a similar procedure to be excluded from the system.

**131. There are daily backups and all signed copies are stored electronically.** Debt records and signed contracts are stored in a safe location in a nearby site outside of SEFIN. Based on information received, the data center counts with the highest standard of security. The site is protected against fire, flooding and theft. In addition, cameras are in place and to enter the room, access must be granted. Within the DMO, debt records and original contracts are kept safe in a separate room within the securities management department. Access is limited and entry must be authorized by the DMO head.

**132. The IT infrastructure allows the DGCP to undertake debt recording and payments, and supports data security**. There is one person in charge of providing service to the debt management team and most IT issues are sorted in-house. The person in charge of this task has received training from UNCTAD, the IT provider. In case a solution cannot be found, the DGCP can access the help desk of UNCTAD and a solution is usually provided within a couple of days.

133. **Current practice allows the staff to access the system remotely**. The system can be reached through SEFIN's VPN (Virtual Private Network) and has proven to be operational during the Covid-19 lockdown. At the time of the mission, the staff was still operating remotely.

134. **Data access, backups and the IT infrastructure are considered sound and the score is a B.** In the absence of audit trails a higher score cannot be assigned. According to DGCP staff, the SIGADE system does not have that option available**.** The score is not directly comparable with the previous assessment due to methodological changes.

### DPI 13.2 - Business Continuity (BC) and Disaster Recovery (DR) Plans

135. **A business continuity plan is in place but does not cover debt management operations**. In 2012, SEFIN in collaboration with Deloitte finalized a business continuity plan, *"Plan de Contingencia de Unidad de Modernización".* According to the staff interviewed, the plan contemplates recovery of payment system and key financial information. Additionally, it was informed that the plan did not contain any guidelines in relation to debt operations. Also, the plan has not been tested and needs to be updated.

136. **The score is a D. Business continuity plan does not include guidelines for public debt operations, has not been tested and is outdated.** The score is not directly comparable with the previous assessment, but a BCP was also missing on that occasion.

## DPI 14 - Debt Related Records

| **DPI** | **Score** |
|---|---|
| 14.1 - Completeness and timeliness of central government debt records | **A** |
| 14.2 - Secure registry systems and debt holder | **A** |

### DPI 14.1 - Completeness and timeliness of central government debt records

137. **All debt related transactions are recorded in the SIGADE: loans, securities, loan guarantees and on-lent operations**. Debt restructuring operations are also recorded in the system. Based on the procedure's manual described in DPI 12.1, the DGCP is able to capture all debt related transactions.

Guarantees are monitored by the same process described above and records are up-to-date as the DGCP verifies the disbursements and payments with the creditors and beneficiaries.

**138. The information extracted from the system is used to produce public debt reports**. Also, the flows generated from SIGADE are used as inputs to elaborate the EDMP, the medium-term public debt strategy. Cost risk analysis are based on the information provided by the debt records stored in the system.

**139. Debt records related to loan guarantees are complete**. At the time of the mission, the DGCP provided detailed debt data in relation to loan guarantees (see DPIs 4 and 10). In the past, some debt guarantees were not timely updated, but in recent years this situation has been addressed and the records are up to date (within a month) and complete.

**140. The completeness and timeliness of debt records are sound and the score is an A.** Based on the evidence provided and the current practice. The previous score was a D on the basis that domestic guarantees were not fully reflected in the records.

### DPI 14.2 - Secure registry systems and debt holders

**141. Dematerialized securities are kept at the Central Securities Depository (CSD) at the BCH**. The BCH acts as the financial agent of the government and all auctions are operated by that institution. Secondary market operations are tracked within the system and the system maintains information on debt holders. The mission verified that market participants are comfortable with current settlement practices.

**142. The CSD is subject to yearly audits by the BCH and CNBS[56].** Backups and storage of CSD's records meet the highest standard. Within the BCH, the IT department oversees the securities management of the system; servers are stored in a safe location (fire and waterproof) and daily backups are available. Security protocols are in place to control and monitor the CSD's access.

**143. The settlement of debt securities is performed on a delivery vs payment (DvP) basis.** Settlement happens on the operation's same day (T+0) and the private sector and other market participants are comfortable with the standards applied in Honduras[57].

**144. There is a secure registry system keeping track of debt holders and the score is an A.** The current practice shows that settlement processes have been updated un the past years and the highest standards are achieved. Previous assessment rated B as there was no evidence of delivery versus payments settlement.

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[56] Banking and Insurance National Committee - *Comisión Nacional de Bancos y Seguros*
[57] The mission held a meeting with market participants who confirmed the ongoing practice.

## DPI 15 - Debt Management Information Systems

| DPI | Score |
|---|---|
| The use of Debt Management Information Systems (DMIS) | **B** |

### DPI 15.1 – Use of Debt Management Information Systems

**145. Based on the evidence provided[58], the mission assessed that all debt related transactions are registered in the system.** The debt management information system in Honduras is currently provided by UNCTAD (SIGADE 6.1) and the DGCP reported that it records all debt instruments in the system.

**146. Reporting and cost-risk indicators are based on the data from the debt system.** This task requires the DGCP to manually treat the primary information coming out of the SIGADE to make sure the cash flows are correct and to keep updated indicators facilitating the production of reports and analytical work.

**147. The system generates the initial payment order and the officer in charge checks the order against the invoice received from creditor.** A procedures manual is being followed and all payments are made on time. Also, a two-step validation process is in place.

**148. The process for registering new debt related transactions is detailed in a procedures manual, updated as of April 2019.** There is a two-step validation process that minimizes human error. Additionally, the DNFE (front office) does not get involved in this part of the process. All new transactions are registered within 30 days.

**149. Corrections in the system are performed in a timely manner.** As far as technical support is concerned, the IT department has an employee that has been trained to resolve most issues in-house. If needed, the DGCP can reach the help desk of UNCTAD for support. It was informed that most problems are resolved within a few days.

**150. In relation to IT infrastructure, the DGCP is equipped to perform all debt related activities.** During the pandemic, remote access through VPN was granted and personnel were able to access the SIGADE. It is worth mentioning that the system can only be accessed through SEFIN's network (VPN).

**151. Based on the above information, the SIGADE contains all debt related transactions and payments are generated by the system and the score assigned is a B.** Payments are executed on the due

[58] Print-screen of the debt records.

date and as mentioned above, the DGCP receives support to resolve issues with the system in- house and if needed UNCTAD’s help desk is available. Also, staff can work remotely and have full access to the system. There is some degree of integration with other PFM systems. To obtain the highest score, audit trails would have to available in the system. Currently, SIGADE does not provide that option. This indicator was not rated in the previous assessment due to methodological changes.

## Annex 1: Staff met during the DeMPA mission (May 2021)

| Name | Organization |
|---|---|
| Liliam Rivera | Subsecretaria de Crédito e Inversión Pública, SEFIN |
| Roxana Rodriguez | Subsecretaria de Finanzas y Presupuesto, SEFIN |
| Angel Moncada | Contaduría General de la República-SEFIN |
| Belkis Zelaya | Unidad de Contingencias Fiscales, SEFIN |
| Carlos Cuadra | Director de la Unidad de Contingencias Fiscales, SEFIN |
| Daniel Godoy | Unidad de Contingencias Fiscales, SEFIN |
| Gilma Iscoa | Contadora General de la República-SEFIN |
| Gloria Rosario Garcia | Contaduría General de la República-SEFIN |
| Jacobo Jose Herrera Gamez | Sub Director General de Crédito Público, SEFIN |
| Jania Ramirez | Directora General de Crédito Público, SEFIN |
| José Chávez | Dirección General de Crédito Público, SEFIN |
| Melissa Matamoros | Unidad de Contingencias Fiscales, SEFIN |
| Miguel Medina | Unidad de Contingencias Fiscales, SEFIN |
| Patricia Dacarett | Unidad de Contingencias Fiscales, SEFIN |
| Saul Coca | Unidad de Contingencias Fiscales, SEFIN |
| Jorge Cruz | Jefe de Riesgos, Dirección General de Crédito Público, SEFIN |
| Roger Sanchez | Jefe de Gestión de Valores, Dirección General de Crédito Público, SEFIN |
| Marco Castro SEFIN | Asesor SEFIN |
| Antonieta Mejia | Directora de la Dirección General de las Instituciones Descentralizadas, SEFIN |
| Glenda Rico | Dirección General de las Instituciones Descentralizadas, SEFIN |
| Olga Trejo | Dirección General de las Instituciones Descentralizadas, SEFIN |
| Karen Sierra | Jefe de Departamento de Control de Calidad, Dirección General de Crédito Público, SEFIN |
| Mario Bonilla | Dirección General de Crédito Público, SEFIN |
| Marlon J. Gómez R. | Analista, Dirección General de Crédito Público, SEFIN |

| | |
|---|---|
| Diana Funes | Dirección General de Crédito Público, SEFIN |
| Ricardo Rivera | |
| Elizabeth Rivera | Directora de Dirección General de Política Macrofiscal |
| Yahir Urbina | Dirección General de Política Macrofiscal |
| Julio Salmeron | Dirección General de Política Macrofiscal |
| Ariel Rodriguez Corea | Dirección General de Política Macrofiscal |
| Iris Maradiaga | Jefe de Análisis, Dirección General de Presupuesto, SEFIN |
| Tomas Cálix | Jefe del Departamento de Operaciones Monetarias |
| Karla Enamorado | Banco Central de Honduras, Jefe del Departamento de Estadísticas |
| Juan Adolfo Matamoros | Jefe del Departamento de Análisis Macroeconómico |
| Luis Agurcia | Jefe del Departamento de Estabilidad Financiera |
| Roy Pineda Castro | Magistrado, Despacho, Tribunal Superior de Cuentas |
| José Juan Pineda | Magistrado, Despacho, Tribunal Superior de Cuentas |
| Tania Melissa Euceda Gómez | Técnico III, Verificación de la deuda Pública, Tribunal Superior de Cuentas |
| Carmen Pineda | Sub Gerente, Coordinación General, Tribunal Superior de Cuentas |
| Dulce Villanueva Rodas | Gerente, Verificación y Análisis, Tribunal Superior de Cuentas |
| Héctor Díaz | Jefe, Verificación de la Deuda Pública, Tribunal Superior de Cuentas |
| Domingo Salomón Hernandez Rodriguez | Dirección General de Crédito Público |
| Dulis Cordova | Tesorería General de la República |
| Brenda Quiroz | Recursos Humanos, SEFIN |
| Lourdes Argueta | Dirección General de Crédito Público |
| Maria Lydia Solano Directora Ejecutiva (AHIBA AHIBA) | Directora Ejecutiva, AHIBA |
| Jose Mauricio Guillen Valenzuela | FICOHSA |
| Lucy Roxana Arias | FICENSA |
| Alejandra Tome | Banco Atlántida |

| | |
|---|---|
| Denis Rodriguez | Unidad de Innovacion y Tecnologia (UIT) |
| Janeth Contreras | Unidad de Modernización |
| Karla López Bonilla | Directora, Unidad de Modernización |
| Arnaldo Rodas | Unidad de Innovación y Tecnología |
| Ediut Cárdenas | Unidad de Innovación y Tecnología |
| Juan Antonio Nolasco | Unidad de Innovación y Tecnología (UIT) |
| Ricardo Madrid | Unidad de Innovación y Tecnología (UIT) |

## Annex 2: DeMPA 2021 vs 2015 scores

| **Debt Performance Indicator** | | **Score DeMPA 2021** | **Score DeMPA 2015** |
|---|---|---|---|
| DPI-1 | 1.1 Central Government's Legal Framework | D | D |
| | 1.2 Public Sector Entities' Central Government's Legal Framework | A | Not comparable |
| DPI-2 | 2.1 Managerial Structure: CG Borrowing and Debt-Related Transactions | A | A |
| | 2.2 Managerial Structure: Issuing Loan Guarantees/On-Lending | A | A |
| | 2.3 Staff and Human Resources | C | - |
| DPI-3 | 3.1. DMS: Quality of Content | A | A |
| | 3.2. DMS: Decision-Making Process | D | D |
| | 3.3. ABP: Annual Borrowing Plan | C | - |
| DPI-4 | 4.1. Central Government Debt Report- Content and Timeliness | C | A |
| | 4.2. Reporting to the Legislature | B | B |
| | 4.3. Public Sector Debt Report- Government Coverage | D | Not comparable |
| DPI-5 | 5.1. Audit: Frequency, Comprehensiveness and disclosure (Financial, Compliance, Performance) | C | C |
| | 5.2. Audit: Degree of commitment to address audit outcomes | D | D |
| DPI-6 | 6.1. Fiscal Policy: Provision of Debt-Service Forecasts | A | A |
| | 6.2. Fiscal Policy: Fiscal Risks Monitoring in the Non-Financial Public Sector | B | Not comparable |
| | 6.3. Fiscal Policy: Availability of Key Macro and Fiscal Variables and DSA | A | A |
| DPI-7 | 7.1. Monetary Policy: Separation between Monetary Policy and DM Operations | A | A |
| | 7.2. Monetary Policy: Information Sharing with the CB on current and future debt transactions and CG cash flows | D | B |
| | 7.3. Monetary Policy: Limits of direct access to CB Funding | D | D |
| DPI-8 | 8.1. Domestic Borrowing: The publication of a borrowing calendar for wholesale securities and publication of issuance results | D | Not comparable |
| | 8.2. Domestic Borrowing: Clarity in rules and procedures | A | Not comparable |
| DPI-9 | 9.1. External Borrowing: Appropriate organizational arrangements and processes for external borrowing from all sources, including financial analysis of terms and conditions | C | Not comparable |

| | | | |
|---|---|---|---|
| | 9.2. External Borrowing: Availability and degree of involvement of legal advisers before signing the loan contract | B | B |
| DPI-10 | 10.1. Loan Guarantees: Issuance of central government loan guarantees | D | D |
| | 10.2. On-lending: Management of On-lending Operations | D | D |
| | 10.3. Derivatives: The use of Derivatives | NA | NA |
| DPI-11 | 11.1. Effectiveness of forecasting the aggregate level of cash balances in government bank accounts | D | A |
| | 11.2. Effectiveness of cash balance and liquidity management | D | D |
| DPI-12 | 12.1. Recording debt-related transactions | A | Not comparable |
| | 12.2. Debt Payments | B | Not comparable |
| DPI-13 | 13.1. Data access, backups and IT infrastructure | B | Not comparable |
| | 13.3. Business Continuity (BC) and Disaster Recovery (DR) Plans | D | D |
| DPI-14 | 14.1. Debt Records: Completeness and Timeliness of CG records | A | A |
| | 14.2. Debt Records: Registry System and Debt Holders | A | A |
| DPI -15 | 15.1 Use of Debt Management Information Systems (DMIS) | B | - |

## Annex 3 - Central Government Guarantees and On-Lending

**Figure 7 - External Debt CG Guarantees - as of 2020 end - USD thousands**

| Lender | Interest Rate | Project | Beneficiary | Outstanding Principal (12/31/2020) |
|---|---|---|---|---|
| KFW | 0.75 | Fortalec.Sector Financ. MIPYME | BANHPROVI | 6.518 |
| KFW | 0.75 | Fortalec.Sector Financ. MIPYMEII | BANHPROVI | 13.528 |
| BNP | 1.956 | Pago Iporte Gtos.Loc.Aper/2 | ENEE | 0.233 |
| BID | 2 | Sist.Inter.Elec. Paises Am.C. | ENEE | 17.474 |
| Swiss Export Risk | 0.5 | Reorg. Deuda Cparis V | ENEE | 0.143 |
| Swiss Export Risk | 4.5 | Reorg. Deuda Suiza CPVI | ENEE | 1.987 |
| Ind.Com.Bk Chin | 5.905 | Proy. Hidroele. Patuca III | ENEE(1) | 243.789 |
| KBC Bank | 0 | Dragado AccesoPto.Cortes | ENP | 3.587 |
| Unicredit Austria AG | | Adqu.Equipo e Instal. | N/D | 7.991 |
| **TOTAL** | | | | **295.25** |
| *ENEE/TOTAL* | | | | *89.30%* |

**Figure 8 - Summary of CG Domestic Guarantees' issuance -2016-2020 - Lempiras (HNL) mn**

| Year | New Guaranteed Debt (Lempira million) |
|---|---|
| 2016 | 1,235 |
| 2017 | 1,875 |
| 2018 | 2,450 |
| 2019 | 5,335 |
| 2020 | 4,208 |
| **TOTAL** | **15,103** |

## Figure 9 - Domestic CG Guarantees -as of 2020 end- Lempiras (HNL)

| Borrower | Type of debt | Lender | Type of interest rate | Interest rate | Signature date | Outstanding Principal Dic.31, 2020 |
|---|---|---|---|---|---|---|
| **Total Debt in Lempiras** | | | | | | **15,103,378,000** |
| | | | | | | - |
| **Total Debt in Lempiras** | | | | | | **15,103,378,000** |
| E.N.E.E. | BONDS ENEE | BCH | CPI INDEXED | 8.100 | 20.12.2019 | 996,602,000 |
| E.N.E.E. | BONDS ENEE | BCH | CPI INDEXED | 7.630 | 20.12.2019 | 612,122,000 |
| E.N.E.E. | BONDS ENEE | BCH | CPI INDEXED | 8.100 | 20.12.2019 | 800,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 10.400 | 20.12.2019 | 7,500,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.750 | 30.12.2019 | 226,246,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 8.100 | 20.12.2019 | 453,756,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 10.900 | 20.12.2019 | 161,356,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.750 | 20.12.2019 | 199,666,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 8.100 | 20.12.2019 | 250,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.100 | 20.12.2019 | 1,070,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.750 | 20.12.2019 | 50,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.750 | 20.12.2019 | 7,500,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.750 | 20.12.2019 | 500,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 6.300 | 22.12.2020 | 1,014,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 7.600 | 22.12.2020 | 1,651,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 7.700 | 22.12.2020 | 758,300,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 8.500 | 22.12.2020 | 621,000,000 |
| E.N.E.E. | BONDS ENEE | BCH | FIXED | 9.000 | 22.12.2020 | 164,000,000 |
| E.N.E.E. | SYNDICATED LOAN I | Bank FICOHSA | FIXED | 10.000 | 27.12.2017 | 1,875,000,000 |
| E.N.E.E. | SINDICATED LOAN II | Bank FICOHSA | FIXED | 10.000 | 27.12.2018 | 2,450,000,000 |
| E.N.E.E. | BOND ENEE | BCH | FIXED | 9.250 | 02.08.2016 | 20,000,000 |
| E.N.E.E. | BOND ENEE | BCH | INFLATION RATE | 6.790 | 22.01.2016 | 1,215,330,000 |

Source: DGCP

## Figure 10 - On-lent debt - as of 2020 end - Lempiras (HNL)

| New Borrower | Lender Ref. | Date of Signing | Loan Currency | Principal of On-Lending Dec.31, 2020 |
|---|---|---|---|---|
| ***TOTAL*** | | | | ***38,741,749,679*** |
| **1.-BANADESA** | | | | **551,275,282** |
| | US$ 30.0 MM | 25.01.2010 | USD | 551,275,282 |
| **1.-BANHPROVI** | | | | **2,287,450,742** |
| | 6020125005 | 18.02.1997 | HNL | 120,798,857 |
| | BCIE-2248 $100.0 MM | 04.06.2020 | USD | 506,396,100 |
| | BCIE-2248 $100.0 MM | 04.06.2020 | USD | 1,298,544,285 |
| | BID 5082/BL-HO (COR) | 02.09.2020 | USD | 126,599,025 |
| | BID 5082/BL-HO (CO) | 02.09.2020 | USD | 235,112,475 |
| **1.-E.N.E.E.** | | | | **35,903,023,655** |
| | BID 1584/SF-HO | 19.12.2005 | USD | 357,397,598 |
| | BID 2016/BL-HO (FCO) | 27.02.2009 | USD | 471,666,665 |
| | BID 2016/BL-HO (FOE) | 27.02.2009 | USD | 206,537,267 |
| | IDA 4536-HO | 27.02.2009 | USD | 602,852,500 |
| | BID 3103/BL-HO (FCO) | 19.12.2013 | USD | 387,055,419 |
| | BID-3103/BL-HO (FOE) | 19.12.2013 | USD | 165,880,894 |
| | BID 3435/BL-HO (CO) | 26.03.2015 | USD | 307,099,256 |
| | BID 3435/BL-HO (FOE) | 26.03.2015 | USD | 204,732,837 |
| | JICA HO-P6 | 26.03.2015 | JPY | 69,669,708 |
| | N. YORK MELLON | 27.01.2017 | USD | 16,879,870,000 |
| | 6021583003 | 27.12.2019 | USD | 1,781,801,512 |
| | US$ 600.00 MM | 24.06.2020 | USD | 14,468,460,000 |

Source: DGCP

## Annex 4 – Evolution of DeMPA scores over time

This annex aims to briefly describe the evolution of DeMPA selected scoring since the last assessment undertaken in 2014. Some scores are not directly comparable, and the description below adjusted for different scores reflecting similar assessment (content evaluated).

Of the current 35 DPIs, 9 (25.7%) remained the same, 10 (28.5%) improved, and 13 (37%) were not comparable (N/C) due to changes in the methodology. Two DPIs changed from N/R to a score of D and one deteriorated, due to a lack of information.

**Areas that remain to observe progress:**

- The legal framework is not fully complied regarding the management of debt guarantees and on-lending, specifically for the case of ENEE and waiving the credit risk analysis as imposed by the regulation, falling short to meet the minimum requirements (DPI 1.1 and 10.1-10.2);
- In spite of legal limits to government's access to BCH financing, on both occasions the former did not cancel its debt with the BCH within the specified period, (DPI 7.3);
- Although the staff has described the forecasting process which would configure a relative improvement on how cash flows are estimated, the score has not improved (remained as a D) due to insufficient evidence of the produced forecast shared with the DeMPA team. Likewise, government cash balances deposited at BCH are not remunerated and no investment is made in the market. (DPI 11.1-11.2).

**Highlights of scoring upgrades**:

- A change in methodology: measured managerial structure (DPI 2.1 and 2.2) by itself separate other DPIs so as to not doubly penalize the debtor. For example, the managerial structure for debt was scored separately from whether a formal MTDS was in place (DPI-3), and the managerial structure for guarantees was scored separately from the legal framework (DPI-1).
- The introduction of a debt management strategy (DPI 3), with good quality of content, although in one of the sub-DPIs the decision-making process doesn't comply with the minimum as the BCH is not consulted.
- An improvement in reporting (DPI 4): before there was no formal debt management strategy and no adequate annual reporting of DM activities to the authorized parties, whereas now and annual borrowing plan has been published and implemented. The Quarterly Debt Report shows the outcomes against the planned strategy.
- A change in methodology for scoring auditing (DPI 5): in both occasions external financial and compliance audits were conducted and the report was public, but the lack of a performance audit led to a D in 2014 and to a C in 2021. The evidence provided to assess the degree of commitment of address the audit outcomes was not enough and the score has changed from N/R to D (DPI 5.2). According to the DeMPA 2021, if there is insufficient information for the assessment, then the score is a D, contrasting to N/R in 2014's methodology.
- The formal agreement between the central government and BCH for the latter's role as agent to the government was made public (DPI 7.1) which was not the case in 2014.

- The completeness and timeliness of debt records (DPI 14) are sound, and an improvement from 2014 because domestic guarantees are recorded. In addition, there is a secure registry system keeping track of debt holders, with an improvement in terms of the introduction of delivery versus payments settlement.

**Highlights of scoring downgrades:**

- The monthly cash flow forecast sent to BCH (sub-DPI 7.2) does not include debt related flows - insufficient evidence provided in the latest assessment. The previous score was a C based on the full coordination on a monthly basis.

**Note on scores that are not comparable:**

- Domestic borrowing sub-DPIs are not comparable. However, one favorable development is that before 74% of domestic debt placements were made directly and only 26% via competitive auctions, whereas now 75% of placements were made via auctions. Also, DGCP has achieved a much better communication with market participants, with biannual meetings and also ongoing communication for resolving queries.
- External borrowing DPIs are not comparable. However, progress was achieved in including within the debt strategy an annual analysis of terms and conditions of major funding sources, as well as implementing a continuous monitoring of international bond markets, in addition to the concessionality element of new borrowing. Also, legal advisors are involved during the negotiation process, following the internal procedures manual.