

***HONDURAS******2024 -******June******Component: Spending******Module: SM II – Managing Public Finance***

HONDURAS

PROJECT SUMMARY	
COUNTRY:	Honduras
LEAD DEPARTMENT:	FAD
REGION:	WHD
PROGRAM ID:	[To be filled out by Secretariat]
PLANNED DATES:	FY25-26
FUNDING PROGRAM TITLE:	[to be added by Secretariat]
PROJECT MANAGERS:	Gores, Laura (FADM2)
SM II – MANAGING PUBLIC FINANCES:	Gores, Laura (FADM2)
ESTIMATED BUDGET	\$196,042
BUDGET FOR ENDORSEMENT:	\$196,042

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*HONDURAS***ACRONYMS**

CAPTAC-DR	IMF's regional technical assistance center for Central America, Panama and the Dominican Republic
CD	Capacity development
C-PIMA	Climate public investment management assessment
ECF	Extended credit facility/extended fund facility
EFF	Extended credit facility/extended fund facility
FAD	IMF's Fiscal Affairs Department
PFM	Public financial management
PIM	Public investment management
PIMA	Public investment management assessment
RSF	Resilience and Stability Facility
STX	Short-term expert

*HONDURAS***I. PROJECT PURPOSE**

The project supports the authorities' commitment on strengthening public financial management (PFM) in the context of the Extended Fund Facility (EFF) and the Extended credit Facility (ECF), approved by the Executive Board of the IMF. This is a 33-month project structured around one component, which is public financial management.

This project will help strengthen PFM to improve the efficient delivery of public spending including with a climate change angle. Honduras faces difficulties with delivering efficient and timely public spending, especially in public investment, and faces repeated challenges from natural disasters – both seen as two major reasons for weak economic growth in the past decades. Several previous capacity development (CD) missions by IMF headquarters and the regional technical assistance center for Central America, Panama and the Dominican Republic (CAPTAC-DR) on budget execution and cash management (November 2023), public investment management (PIM) including from a climate change perspective (February 2024) and the closing of trust funds (April 2023) have highlighted the need for progress in various areas—such as budget preparation, green PIM, budget execution processes, and cash and debt management—to enhance the country's capacity to deliver public investment in support of economic growth.

The IMF's Fiscal Affairs Department (FAD) will deliver CD on the spending side to lift bottlenecks and strengthen budget formulation and execution phases, including climate change considerations. More specifically, the project will (1) support progress in strengthening budget preparation, and (2) enhance budget execution management, both with a special focus on green spending. The assistance will respond flexibly to support the authorities' efforts to conduct reforms in the context of their access to the Resilience and Sustainability Facility (RSF), for which negotiations are presently ongoing.

This project proposal has been discussed with the authorities and the objectives and outcomes were agreed upon. The estimated budget for the first year is \$196,042, and endorsement is requested for the full amount through FY25.

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II. BACKGROUND

Macro-fiscal situation

For 2023, the Honduran non-financial public sector fiscal deficit stood at 1.3 percent of GDP, well within the 2.0 percent target of the ECF/EFF program, approved in September 2023. Revenues have been performing well and current expenditures have remained under control, and both stood within their respective targets also. The only target that has likely been missed is priority on social expenditures, which the government did not manage to expand as quickly as expected, given that newly designed programs are still improving their execution. Under the program, the baseline fiscal deficit is expected to gradually converge to the 1 percent of GDP deficit ceiling under the fiscal stability law by 2026.

The IMF program will support a scaling-up of productivity-enhancing public capital investment while safeguarding debt sustainability. An increase is warranted by Honduras' urgent need for public investment to reduce poverty, bolster resilience to climate change (especially through dams for flood control and investments in the energy sector) and increase the economy's growth potential. To this end, an adjustor under the program envisages that public investment (and therefore the fiscal deficit) in 2024 could be up to 1.3 percent of GDP higher than under the baseline should additional external financing materialize for capital spending.

Country engagement and alignment to reform priorities

In the field of PFM, the ministry of finance has been pursuing several reforms over the past years with extensive support from FAD. Honduras faces difficulties with delivering efficient and timely public spending, especially in public investment, and faces repeated challenges from natural disasters—both seen as two major reasons for weak economic growth in the past decades. Several CD missions by IMF/FAD headquarters and CAPTAC-DR on budget execution and cash management (November 2023), PIM including from a climate change perspective (PIMA/C-PIMA, February 2024) and the closing of trust funds (April 2023) have highlighted the need for progress in various PFM areas—such as budget preparation, green PIM, budget execution processes, and cash and debt management—to enhance the country's capacity to deliver public investment in support of economic growth. The authorities have requested follow-up support from FAD in these general PFM areas, but also in implementing the recommendations from the C-PIMA, which are likely to inspire some of the reform measures currently under discussion as part of a possible Resilience and Sustainability Facility (RSF) program. More broadly, given Honduras extensive needs in strengthening its public financial management system, on the long run the presence of a resident PFM advisor should be examined.

IMF priority areas / cross-cutting themes

Honduras aims to put its fiscal management at the service of fighting climate change. Honduras has announced its intention to apply for access to the RSF, which will entail CD needs in support of reform measures that address climate change. This project will finance CD as needed on green PFM, in synergy with the upcoming RSF arrangement.

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III. PROJECT MODULES – DESCRIPTION

This proposal will provide CD support to Honduras in the area of managing public finances. FAD CD will support improvements within the strategic objectives presented in Table 1 below:

Table 1. Summary of Objectives covered by the Proposal

Component	Module	Objective
Spending	SM II / Managing Public Finance	Strengthened Budget Management – PBM

A. SM II – Managing Public Finance

Scope

On the spending side, in the PFM module, this project will strengthen budget formulation and execution for improving the delivery of public spending and help mainstream climate change considerations into them. This will be done notably through advising on (1) how to strengthen budget preparation to formulate comprehensive and credible budgets, (2) how to lift bottlenecks to improve budget execution, (3) how to identify and track strategic budget allocations that will benefit the fight against climate change.

Program Objectives

The Ministry of Finance of Honduras received extensive support from FAD over the past years to strengthen fiscal management, but more remains to be done to achieve reform objectives.

Honduras faces difficulties with delivering public spending, especially in public investment, and faces repeated challenges from natural disasters—both seen as two major reasons for weak economic growth in the past decades. Several CD missions by IMF/FAD headquarters and CAPTAC-DR the need for progress in various PFM areas—such as budget preparation, green PIM, budget execution processes, and cash and debt management—to enhance the country’s capacity to deliver public investment in support of economic growth. The authorities have requested follow-up support from FAD in these areas, and in particular support to implement the reform measures currently under discussion as part of a possible RSF program.

As a core program objective, the project targets budget management as a centerpiece of PFM, to better put fiscal operations at the service of sustainable and inclusive growth. The CD activities will be focused on strengthened budget management, both as regards (1) annual budget formulation process, and (2) budget execution and control processes, while ensuring that climate change related spending is adequately identified and tracked at both stages. The activities in the first year (FY25) will help develop reform plans that in turn will allow to determine future CD needs and develop a long-term engagement plan.

Expected Results (outcomes)

The two project outcomes will strengthen budget management through the increase of capacity for reforms, enhanced risks management and strengthening core functions to improve public spending delivery. The expected results are as follows:

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Objective 1: Strengthened Budget Management

Outcome 1.1: Strengthened annual budget process, and effective allocation. Overall, the comprehensiveness and credibility of the central government budget requires further work on incorporating trust funds into normal PFM processes and budgeting with a better view on the multi-annual implications of public investment spending. More work is needed on gearing PFM processes towards a better identification and allocation of green spending. While Honduras has put in place a first climate budget tagging system and publishes a climate annex appended to the budget law, there is no clearly defined climate budget tagging methodology and no institutional underpinning to this effort. This could lead to risks of “greenwashing” in the absence of requisite quality controls. Further, this tagging does not yet provide a sound basis for strategic budget allocation decisions with view to national climate objectives, given that tags do not yet allow to identify spending going to national priority objectives.

Outcome 1.2 Strengthened budget execution and control processes. Budget execution need strengthening, especially the programming of budget execution processes, to increase its efficiency and timelines, avoiding at the time erroneous registers on budget execution data. Additionally, budget reporting needs to be enhanced to more clearly report on the spending effectively executed to benefit climate change objectives.

IV. ORGANIZATIONAL ARRANGEMENTS

A. Country Engagement

In the field of PFM, the Ministry of Finance received extensive support from FAD over the past years to strengthen fiscal management and remains committed to PFM reforms. Honduras receives an above average number of CD missions from FAD and CAPTAC-DR, which over the years have helped strengthen capacity in PFM. Honduras faces difficulties with delivering public spending, especially in public investment, and faces repeated challenges from natural disasters—both seen as two major reasons for weak economic growth in the past decades. Authorities particularly stress the need for progress in areas such as budget preparation, green PIM, budget execution processes, and cash and debt management—to enhance the country’s capacity to deliver public investment in support of economic growth. The authorities have also requested follow-up support from FAD in implementing the recommendations from the C-PIMA, which are likely to inspire some of the reform measures currently under discussion as part of a possible RSF program.

B. Delivery Modalities

CD will comprise of a mix of remote and in-person activities. Virtual deliveries will be used to provide efficiencies to in-person support, including pre-engagement meetings and post-follow-up meetings. The following CD activities will be delivered as a package:

- **Headquarters-led (HQ) missions and staff visits** to provide strategic recommendations, conduct regular follow-ups, assess progress, ensure STX work is aligned to plans, coordinate with other CD providers, and adjust reform implementation plans.
- **Short-term expert (STX) visits** to help implement the recommendations delivered by the HQ missions; a limited number of STXs will be assigned to provide specialized assistance in specific areas of revenue administration and PFM. The project will seek to use Portuguese-speaking experts.

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- **Workshops**, during the HQ missions, staff visits, or STX visits, to share experiences, provide stakeholders with a view of progress achieved and challenges faced, and discuss with the managers and staff their views on the reforms and particular technical subjects.

C. Coordination / Cooperation

Coordination			
Partner	Type of coordination	Area of coordination	Frequency
CAPTAC-DR	Continuous support, backstopping, design and delivery of CD, data sharing.	Objectives and outcomes covered by the project	Permanent
Cooperation			
Partner	Type of coordination	Area of coordination	Frequency
Inter-American Development Bank, World Bank, United Nations Development Programme	Exchange information and agree on areas to be covered by each donor	CD support on PFM, notably on green PFM and public procurement	As needed

V. RISK ASSESSMENT AND MITIGATION

General or Module	Description	Risk Assessment	Mitigation Measures
External climate/conditions			
SM II	Natural disasters and other external shocks could hinder CD delivery in the field.	Low	Ensure sufficient flexibility in program execution and allow for ability to adjust activities in the case of adverse events.
Management and Technical Staff Support and Commitment			
SM II	Continuous rotation and lack of preparation of managers undermine the absorptive capacity	Medium	The missions will work with stable staff and officials encouraging authorities to implement administrative reforms that contribute to a more stable staff. Continual/regular high-level engagement and monitoring.
Resource Adequacy			
SM II	Availability of funding and staff for CD.	Low	Careful preparation and planning of CD activities.

*HONDURAS***VI. CD DELIVERY PLAN****Table 2. Summary of Indicative CD Delivery**

CD Modalities (Remote or Field-based CD)	FY25	FY26	FY27	FY28	FY29	Grand Total
SM II – Managing Public Finances						
HQ led CD mission	1	-	-	-	-	1
STX visits	1	-	-	-	-	1
Total	2	-	-	-	-	2

Note:

- In-person delivery was chosen in all instances to support the engagement in a program country.
- Hybrid delivery was chosen in several instances to enable AD colleagues and other DPs to join the opening and closing meetings.
- Collectively the blend of CD delivery proposed over the duration of this project/program reflects the optimal balance of in-person, remote, and hybrid activities needed to achieve the project/program outcomes taking into account the needs of the country and the resources available.

Table 3. First year workplan

Timing	CD Modality	Proposed Topics of CD
SM II – Managing Public Finances		
Q4/FY25	Field-Based work	HQ Mission – Budgeting
Q4/FY25	Field-Based work	STX Visit – Budgeting

VII. PROGRAM FINANCIALS

	FY25	FY26	FY27	FY28	FY29	Total
SM II – Managing Public Finances	\$183,217	-	-	-	-	\$183,217
Subtotal	\$183,217	-	-	-	-	\$125,870
Trust fund management fee (7%)	\$12,825	-	-	-	-	\$12,825
Total	\$196,042	-	-	-	-	\$196,042

The estimated budget for this project is \$196,042, and endorsement is requested for the full amount.

VIII. TARGETED LOGICAL FRAMEWORK

A. SM II – Managing Public Finances

Objective	
Strengthened Budget Management	
Outcome(s)	Indicator(s)
Strengthened budget execution and control processes	Improved effectiveness of budget execution and controls for non-salary expenditure including capital spending and priority areas (Record Score: PEFA PI-25. PIMA 12a)
Strengthened annual budget process, and effective allocation	Improved allocation to priority areas including climate, gender, and Sustainable Development Goals