

## Honduras

In 2009 the Honduran economy experienced its first recession since 1999. GDP is estimated to have contracted by 3%, with a 5% decline in per capita GDP, owing to effects of the international financial crisis and the political crisis in the country. Inflation fell significantly, closing the year at 3.5%. The slowdown in economic activity led to a sharp reduction in the current account deficit, which dropped from 14% in 2008 to 7.9% in 2009. By contrast, the central government deficit expanded from the equivalent of 2.4% of GDP, to 4.5% of GDP.

The impact of the international crisis was transmitted to the Honduran economy through external demand, FDI, remittances and tourism revenues, which all contracted. These effects were magnified by the domestic political crisis that followed the removal from office of President Zelaya in June. The rupture of democratic order for first time in 30 years produced deep polarization within Honduran society. The international community, meanwhile, imposed restrictions on external financing and international cooperation.

The new government due to take office in January 2010 will face an extraordinarily difficult situation. The country is now profoundly divided politically and its economic growth is being severely limited by the aftermath of the events of 2009, combined with more deep-rooted structural factors. The latter include a high level of inequality, a poverty rate of over 60%, scant opportunities for formal employment for the vast majority, and even undernutrition, particularly among children. Macroeconomic policy faces additional challenges posed by, on the one hand, the complicated footing of public finances and, on the other, a real exchange rate that is around 20% overvalued, in comparison with the average for the last 20 years. At this juncture, broad consensus—at present, a seemingly difficult proposition—is needed to overcome these problems.

As a consequence of the crisis, fiscal revenues fell by approximately 13% in real terms, while revenues from foreign trade taxes plunged by 25% as a result of the major contraction in imports. Direct taxes slipped by 13%, with sales taxes the category least affected. Grants were down by 10%.

Overall public spending decreased slightly, by around 2% in real terms. Current expenditures grew by 2%, owing largely to wage increases (4%). The adjustment variable

was capital spending, which contracted by more than 15%. Public finances are being weighed down—and could even find their sustainability threatened, if current patterns continue—by certain expenditures, such as benefits mandated by union by-laws, which are in need of overhaul. The former government had implemented a number of positive measures, which remain in force, such as free school enrolment and snacks during school hours, but no financing sources had yet been identified.

As a result of the drop in revenues and the inability to access external financing, floating debt and domestic indebtedness increased. Domestic debt grew by nearly 80%, from 3.5% of GDP in 2008 to 5.9% in 2009. External debt continued to decline as a proportion of GDP, owing to the country's participation in various debt forgiveness initiatives for highly indebted poor countries and limited access to new financing.

Monetary policy passed through two distinct stages during the year. In the first semester it was expansionary, aimed at bolstering economic activity against the effects of the international financial crisis. The monetary policy rate was reduced, from 7.75% in December 2008 to 3.5% in June 2009. The reserve requirement was lowered to 0% and the open market operations that had been used to absorb excess liquidity were suspended.

As of July, the focus has been on shoring up net international reserves and ensuring exchange rate stability. The monetary policy rate increased to 4.5%, the reserve requirement rose to 6% and the mandatory investments of financial institutions in government bonds, rose from 9% to 12%. These measures slowed the decline in reserves and secured the funds to finance the fiscal gap. The nominal interest rate on deposits rose from 6.0% to 7.2%, with nominal lending rates increasing from 17.4%, on

average, between January and September 2008, to 19.6% in the same period of 2009. Due to the sharp slowdown in inflation, real interest rates rose significantly. In the financial system, indicators for non-performing, overdue and other troubled loans deteriorated, but did not reach alarming levels.

The excess liquidity seen during the first part of the year was drawn into covering the fiscal deficit through the sale of government bonds, and went into purchases of dollars that drained international reserves, which declined 11% between December 2008 and September 2009. The nominal exchange rate remained unchanged, signalling a slight real appreciation with respect to the dollar.

Economic activity contracted by around 3% after having expanded 4% in 2008—a contraction that would have been even greater but for the creation of a fund controlled by the Honduran Bank for Production and Housing (BANHPROVI). The fund's loan portfolio grew by approximately 80% in 2009. Gross domestic investment slumped 29%. Consumption shrank slightly (by 2.1%), with the private component declining by 5% and the public by 2.5%.

The sectors worst affected by the crisis were construction and manufacturing, which contracted by 6.0% and 5%, respectively. The agricultural sector—highly important, particularly as a source of employment—contracted by more than 3%, in spite of some positive factors such as very good harvests for a number of grain crops. By contrast, the services sector performed well, with the highest growth rates in public administration and defence.

The consumer price index showed the effects of the economic slowdown combined with falling international prices for food and petroleum. The year-on-year rate to December fell from 10.8% in 2008 to 3.5% in 2009. Urban unemployment rose from 4.1% in 2008 to 4.9% in May 2009. In January 2009 there was an increase (unprecedented in the country's recent past) in the minimum wage—by as much as 96%, depending on the kind of activity—which made up some of the lag in wages from prior years and helped sustain consumption among the lower-income population.

The current account deficit declined by a significant 6 percentage points of GDP owing to the contraction in

#### HONDURAS: MAIN ECONOMIC INDICATORS

	2007	2008	2009 <sup>a</sup>
<b>Annual balance growth rates</b>			
Gross domestic product	6.3	4.0	-3.0
Per capita gross domestic product	4.2	1.9	-4.9
Consumer prices	8.9	10.8	2.7 <sup>b</sup>
Real minimum wage	2.8	0.2	70.3
Money (M1)	16.3	1.8	2.1 <sup>c</sup>
Real effective exchange rate <sup>d</sup>	-0.3	-3.5	-8.7 <sup>e</sup>
Terms of trade	-1.9	-6.1	9.2
<b>Annual average percentages</b>			
Urban unemployment rate	4.0	4.1	4.9 <sup>f</sup>
Central government overall balance/GDP	-2.9	-2.3	-4.2
Nominal deposit rate	7.8	9.5	10.9 <sup>g</sup>
Nominal lending rate	16.6	17.9	19.6 <sup>g</sup>
<b>Millions of dollars</b>			
Exports of goods and services	6 344	6 956	6 117
Imports of goods and services	9 594	11 603	9 204
Current account balance	-1 225	-1 977	-1 129
Capital and financial account balance <sup>h</sup>	1 063	1 912	374
Overall balance	-162	-65	-755

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

<sup>a</sup> Preliminary estimates.

<sup>b</sup> Twelve-month variation to October 2009.

<sup>c</sup> Twelve-month variation to September 2009.

<sup>d</sup> A negative rate indicates an appreciation of the currency in real terms.

<sup>e</sup> Year-on-year average variation, January to October.

<sup>f</sup> Figure for May.

<sup>g</sup> Average from January to October, annualized.

<sup>h</sup> Includes errors and omissions.

imports of goods and services (19% and 17%, respectively). Exports of goods and services saw a less severe drop (12% and 15%, respectively). Traditional exports were the hardest hit, declining by 17.4%, followed by maquila exports, which were down by 12.1%. Imports of capital goods suffered a sharp 28.1% drop as a result of the economic slowdown, while most of the decline in the value of commodity and intermediate goods imports (25.4%) was due to the drop in international prices. After 12 consecutive years of deterioration, terms of trade improved, thanks to steep falls in international food and petroleum prices. Family remittances, one of the pillars of consumption and exchange-rate stability, slipped by 11%, while FDI flows fell by nearly 40%.