



INTERNATIONAL MONETARY FUND

Technical Memorandum of Understanding

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1. This memorandum sets out technical understandings between the Honduran authorities and the Fund for monitoring the economic program during 2008 supported by a Stand-By Arrangement. It defines the concepts used to assess observance of quantitative performance criteria and benchmarks specified in Tables 1 and 2 of the Memorandum of Economic Policies (MEFP). It also specifies the frequency of the data to be provided to the Fund for monitoring the program.

I. FISCAL TARGETS

2. **The deficit of the combined public sector (CPS)** will be measured from the financing side, and corresponds to the net borrowing requirements of the CPS, from both external and domestic sources. The combined public sector comprises the nonfinancial public sector (NFPS) and the operating result (quasi-fiscal balance) of the central bank. The NFPS covers the central government (including its agencies), local governments and decentralized agencies, the social security institute (IHSS), the pension institutes for executive branch staff (INJUPEMP) and teachers (INPREMA), and the public enterprises.

3. **The deficit of the central government** will also be measured from the financing side. The central government includes the executive, judicial, and legislative branches of government. It consolidates the operations of trust funds created to support agricultural loans and so-called deconcentrated agencies.

4. **The current primary expenditure of the central government** is defined as total current expenditure less interest payments.

5. **The central government wage bill** is defined as all central government wages and salaries including severance payments, plus employer social security and pension contributions, and other remunerations (such as special bonuses and performance related remuneration to teachers under the *PASCE*).

6. **Anti-poverty spending** comprises all spending on programs and projects of the Poverty Reduction Strategy (whether financed by domestic savings, HIPC debt relief, grants, and external loans), as defined in the relevant annex of the 2003 PRSP and the latest update to the PRS. Programs and projects in the PRSP will be labeled in the 2008 budget and tagged through the SIAFI. Anti-poverty spending will be presented by economic classification, type of program, and source of financing.

7. **The operating surplus of the public enterprises** is the difference between the operating revenue (excluding interest earnings and transfers) and the operating expenditure (excluding interest payments and transfers) of the enterprises. For the purposes of the program, the public enterprises comprise the State Electricity Company (ENEE), the State

Telecommunications Company (HONDUTEL), the State Water and Sewerage Company (SANAA), and the State Ports Company (ENP).

8. **Net domestic financing of the CPS** comprises the operating result of the central bank and the change relative to end-2007 in the stocks of: (1) outstanding indebtedness of the NFPS (direct bank credit plus bank holdings of public sector bonds less deposits) to the domestic financial system (central bank, commercial banks, and other financial institutions); (2) outstanding public sector bonds held outside the financial system; (3) outstanding deposits held abroad; (4) outstanding suppliers' credit and floating debt (uncashed and undelivered checks, and unpaid invoices and orders) of the central government, and unpaid orders of the rest of the NFPS (all domestic debt is in domestic currency); and (5) proceeds from the sale of the mobile phone license.

9. **Discrepancies.** The authorities will undertake periodic reconciliations to minimize discrepancies between above-the-line and financing data. If needed, these reconciliations should be carried out prior to completion of the first and second reviews under the program.

II. MONETARY TARGETS

10. **Net International Reserves (NIR) of the central bank.** For program purposes, NIR will be measured as gross international reserves that are readily available (including the balance of the Trust Fund instituted to manage financing from Petrocaribe) minus short-term reserve liabilities (including purchases and credits from the Fund), as described in the international reserves table prepared by the central bank according to the new monetary statistics presentation (MEMF). Readily available reserves also exclude those assets that are pledged or otherwise encumbered, including but not limited to reserve assets used as collateral or guarantee for a third-party external liability. NIR excludes (1) any conversion of short-term reserve liabilities; (2) foreign assets stemming from foreign currency deposits of financial institutions at the central bank; and (3) transfer to the central bank of foreign currency deposits of HONDUTEL, INJUPEMP, and IHSS held abroad, which amounted to US\$121 million at end-2007. NIR will be valued at current exchange rates.

11. **Net domestic assets (NDA) of the central bank** will be measured as the difference between currency issue and NIR, both measured on the basis of end-of-period data.

12. **Prior action.** Monetary measures equivalent to 2 percentage points in reserve requirements (MEFP ¶6) will be defined over a base of end-December local currency deposits. The stock of central bank bills in the hands of nonbank local investors will be defined as the total stock of central bank bills less the stock in the hands of commercial banks (otras sociedades de deposito).

13. **Adjustor:** The end-June performance criterion for the floor on net international reserves of the central bank will be adjusted downwards by the amount of the proceeds from the sale of the mobile phone license that are unrealized by that date, or the amount of the

proceeds that are realized in lempiras, by up to US\$80 million. Conversely, the end-June performance criterion for the ceiling on net domestic assets of the central bank will be adjusted upwards by up to the same amount.

III. EXTERNAL TARGETS

14. **External debt.** As indicated in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted by the IMF Executive Board on August 24, 2000, debt will be defined as a current (not contingent) liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms: (i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property. (b) Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt."

15. **Stock of external debt arrears.** For the purpose of the program ceiling, external debt-service arrears are defined as overdue debt service arising in respect of obligations incurred directly or guaranteed by the public sector, except on debt subject to rescheduling or restructuring, as indicated by the respective creditors.

16. **Borrowing on nonconcessional terms.** For the purposes of the program, this ceiling applies to the contracting or guaranteeing of nonconcessional external debt by the CPS or any other agencies on their behalf. The ceiling applies not only to debt as defined above, but also to commitments contracted or guaranteed for which value has not been received.

17. **Concessionality** will be based on a currency-specific discount rate based on the 10 year (6-month) average of the OECD's commercial interest reference rates (CIRR) for loans or leases with maturities greater (less) than 15 years, and following the methodology set out in the following Fund documents: SM/96/86 (April 8, 1996) and EBS/00/128 (June 30, 2000). Maturity will be determined on the basis of the original loan contract. Under this definition of concessionality, only debt with a grant element equivalent to at least 35 percent (referring to the difference between the nominal value and the net present value of debt) will be excluded from the debt ceiling. In determining whether multiple financing instruments would be considered as an integrated incurrence of debt for the purposes of assessing the concessionality of that debt, the elements that Fund staff would take into account include: (i) identical intended use or purposes for the financing; (ii) inter-related schedules for disbursement; (iii) cross-conditions for entry into legal effect, availability of funds and default; and (iv) identical parties to the financing.

18. **Excluded** from the external debt ceiling are: (1) the use of Fund resources; (2) debts classified as international reserve liabilities of the central bank; (3) short-term import financing (with a maturity of less than one year); (4) debts to restructure, refinance, or prepay existing debts; and (5) central bank instruments placed in the domestic market held by nonresidents.

IV. STRUCTURAL REFORMS

A. Energy Policy

19. **Arrears of ENEE** are defined as overdue payments (principal and interest) as stipulated in the corresponding contracts. With proceeds from the issue of government bonds authorized in the 2008 budget, ENEE will clear all arrears to generators by end-June 2008. No new arrears to the private sector shall accumulate during 2008.

B. Monitoring and Reporting Requirements

20. **The information required to monitor the compliance with quantitative and structural performance criteria and benchmarks** specified in the MEFP will be supplied to the Fund at least monthly (electronically, to the extent possible) within 45 days of the end of the previous month (unless otherwise noted) according to the following sources:

21. **The ceilings on the deficit of the central government and of the CPS** will be monitored below-the-line on the basis of the monthly reports *Financiamiento de la Administración Central* and *Financiamiento del Sector Público Combinado*, respectively, prepared by the central bank, which contain:

- **Net external financing** of the central government and the NFPS, respectively, with detailed information on disbursements, amortizations, exceptional financing, zero-

coupon bond, and accumulation of arrears. This information is prepared by the central bank and reconciled with the Ministry of Finance.

- **Net domestic financing** of the central government and the NFPS, respectively, with detailed information on: (1) net domestic financing from the central bank and the rest of the financial system to the central government and the NFPS, as contained in the *Panorama Financiero* monthly report; (2) net placement of bonds (including stabilization bonds) by the central government and the NFPS outside the financial system, as reported by the central bank with data from the Public Credit Directorate of the Ministry of Finance; (3) change in foreign currency deposits held abroad by the central government and the NFPS; and (4) change in the outstanding stock of suppliers' credit and floating debt of the central government, as reported by the Treasury, and the rest of the NFPS as reported by the central bank. To monitor the net domestic financing to the CPS, the central bank will provide the Fund with detailed data on a cash basis on the operating revenue and expenditure of the central bank.

22. **The ceilings on the wage bill of the central government** will be monitored monthly on the basis of the ministry of finance report: *Información institucional por objeto de gasto - servicios personales y aportes patronales*.

23. **To complement the monitoring of fiscal performance, a breakdown of tax revenue** by type of tax will also be provided monthly to the Fund.

24. **Anti-poverty spending** will be monitored quarterly on the basis of the information provided by the ministry of finance. Anti-poverty spending will be obtained from the detailed central government report: *Cuenta Financiera*. The Ministry of Finance will also provide the breakdown between anti-poverty and other spending by expenditure category (i.e., wages and salaries, goods and services, current transfers, fixed capital formation, and capital transfers).

25. **The floor on NIR and the ceiling on NDA of the central bank** will be monitored on the basis of information produced by the central bank, in accordance with the new presentation of the monetary statistics (MEMF). This information will be provided within two weeks of the end of the previous month.

26. **The ceilings on the contracting of nonconcessional external debt and on the nonaccumulation of external payments arrears** will be monitored with information provided by the Ministry of Finance. The accounting of nonreschedulable external debt-service arrears by creditor (if any), with detailed explanations, will be transmitted by the Ministry of Finance on a monthly basis within four weeks of the end of each month. Moreover, a loan-by-loan accounting of all new loans contracted or guaranteed by the public sector, including detailed information on the amounts, currencies, and terms and conditions, as well as relevant supporting materials, will be transmitted by the central bank on a quarterly basis within four weeks of the end of each quarter.