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Signed: 1/9/74

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Report No. P-1325a-HO

REPORT AND RECOMMENDATION  
OF THE  
PRESIDENT  
TO THE  
EXECUTIVE DIRECTORS  
ON A  
PROPOSED LOAN  
AND  
CREDIT TO  
THE REPUBLIC OF HONDURAS FOR AN EDUCATION PROJECT

December, 7, 1973

Latin American and the Caribbean Regional Office

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<u>Currency Unit</u>		<u>Honduras Lempiras (L)</u>
US\$ 1.00	=	L 2.00
L 1	=	US\$ 0.50
L 1,000	=	US\$ 500.00
L 1,000,000	=	US\$ 500,000
Fiscal Year	=	January 1 to December 31

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

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REPORT AND RECOMMENDATION OF THE PRESIDENT  
TO THE EXECUTIVE DIRECTORS  
ON A PROPOSED LOAN AND CREDIT TO  
THE REPUBLIC OF HONDURAS FOR AN EDUCATION PROJECT

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1. I submit the following report and recommendation on a proposed loan and a proposed development credit, each for the equivalent of US\$3 million, to the Republic of Honduras to help finance an education project. The loan would have a term of 30 years, including 10 years of grace, with interest at 7 1/4 percent per annum. The development credit would be on standard IDA terms.

PART I - THE ECONOMY

2. The economy of Honduras was discussed in paragraphs 2-11 of the President's Report dated September 25, 1973 on a proposed credit to the Republic of Honduras for the Second Livestock Development Project (Report No. P-1293a-HO). These paragraphs, together with a Country Data Sheet, are attached hereto as Annex 1; they cover among other things the reasons for regarding Honduras as a blend country for purposes of Bank/IDA lending.

PART II - BANK GROUP OPERATIONS IN HONDURAS

3. Beginning with a loan of US\$4.2 million for roads in 1955, Honduras has to date received twelve Bank loans totalling US\$89.2 million and six IDA credits totalling US\$30.6 million, both net of cancellations. The proposed loan and credit would raise the total of Bank and IDA assistance from US\$119.8 million to US\$125.8 million; they cover among other things

4. Execution of Bank Group financed projects has, on the whole, been satisfactory. Annex II contains a summary statement of Bank loans, IDA credits and IFC investments as of August 31, 1973, and notes on the execution of on-going projects.

5. In the past, Bank and IDA lending has been heavily concentrated on transport and power, where inadequate facilities hampered the development of the country. The livestock development credit approved in 1970, however, marked a first step towards diversifying lending. In our future

Lending to Honduras, we plan to support the priorities of the Government's investment plan by giving increased emphasis to investment in the social and the commodity producing sectors while continuing to lend for physical infrastructure, where there are still substantial deficiencies to be overcome.

6. As the agricultural sector remains the decisive element in the country's economic and social development we intend to expand our activities in the sector. The objectives of lending for agriculture will be to assist in diversifying the economy, developing competitive exports in high-value products, and supporting the Government's efforts in agrarian reform and manpower training. The livestock sector will be further supported by an IDA credit approved by the Executive Directors in October 1973. Also, the IBRD/FAO Cooperative Program has begun assisting the Government in the preparation of the proposed first phase of the Comayagua Valley integrated rural development project. In furtherance of our objectives in the agricultural sector, the proposed project includes an agricultural education component.

7. In transport, we hope to continue to assist the Government to complete the highway links between the main regions of the country, but would in the future place greater emphasis on assistance in the construction of a network of feeder and access roads to support the Government's agricultural program.

8. We plan to assist industry in Honduras as well as in the other Central American countries by lending to the Central American Bank for Economic Integration (CABEI). Lending for industry through a multinational institution such as CABEI would support the Central American integration effort; foster rational industrialization in the area where national markets are too small to permit efficient industrial development; and assist in diversifying the region's economy. The appraisal mission for a first lending operation to CABEI is now preparing its report.

9. IFC has participated in two projects in Honduras. A total of US\$387,000 was invested in a leather tanning project in 1964 and 1966. A second operation was a pilot project for the pulp and paper industry to utilize the wood resources of the Olancho Reserve. A pilot company, Compania Pino Celulosa de Centroamerica, A.A. (COPINO), was established in June 1968, under the leadership of International Paper Company (IPC), to investigate and possibly carry out a project. IFC invested US\$75,000 in COPINO in 1969 and 1970. In March 1971, IPC discontinued its participation in COPINO, and efforts to find other technical partners have so far been unsuccessful. The new Government, which took office in December 1972, wishes to exploit the Olancho forest, but specific plans are still being formulated.

PART III - EDUCATION IN HONDURAS

10. The Honduran education system has undergone rapid growth in the last ten years. Enrollments between 1962 and 1972 increased annually by about 6 percent in primary education, 12 percent in secondary education, and 15 percent in higher education. The sector, however, still suffers from major weaknesses. Imbalances favoring urban areas have not been corrected, nor has the expansion stressed the training of middle-level technical manpower to meet the needs of the economy. Moreover, the system still operates with inadequate curricula and a shortage of trained teachers and physical facilities. There are also deficiencies in education management stemming from an over-centralized administrative structure. The lack of educational opportunities, both formal and non-formal, has created a work force with a very low level of education and training which seriously affects productivity. Fewer than 1 percent of the labor force has had higher education, about 3 percent has had secondary education, and only 12 percent has completed primary education.

Education Administration

11. The Ministry of Education has the major responsibility for formulating policy and administering formal public education and training in Honduras. The Ministry also has control over some types of literacy programs, but most of the non-formal education and training activities are under the control of the Ministries of Labor and Natural Resources and various autonomous institutions and private organizations. Higher education is in the hands of the National University and one private and three public institutions.

12. Educational administration suffers from an overcentralized, slow decision-making process, duplication of services, weak planning, and inadequate financial and accounting procedures. Lines of authority and responsibility are poorly defined, as is personnel policy in general, and there is a clear lack of coordination between the Ministry of Education and the other agencies dealing with education and training. There is, therefore, a pressing need to improve educational administration and decentralize responsibility to the regional level.

The Formal System

13. The formal education system consists of six years of primary education, five to six years of secondary education, and post-secondary education varying in length from two to seven years. Primary education, covering ages 7-13, is provided free in public schools and is compulsory. In spite of some recent gains, primary education is still inefficient. Enrollment, at 412,000 in 1972, represents 81 percent of the relevant age group, but wastage is high, and only about 36 percent of the students entering the system in urban areas and about 8 percent in rural areas finish primary

education. Aside from deficient teaching facilities and inadequate curricula, this high wastage rate can be attributed to the rigid examination system, non-enforcement of the attendance law, and the fact that a large number of rural schools offer fewer than six grades, thus preventing the rural children from continuing their education. The supply of primary teachers, while above required levels from a quantitative point of view, has been qualitatively very low.

14. About 71 percent of the students completing primary education enroll in secondary schools. Public secondary education is free, but not compulsory. In 1972 the total enrollment in secondary education amounted to 51,000, representing 14 percent of the relevant age group. Secondary education comprises a three-year lower cycle of general subjects followed by two to three years of upper secondary education with courses in the humanities, sciences, technical and vocational subjects, as well as primary teacher training and agricultural education. Most secondary education is conducted by private institutions. In 1972 only 26 percent of the total enrollment was in public secondary schools. In general, the quality of secondary level education is deficient, particularly in the areas of primary teacher training, technical and vocational education, and agricultural training, all of which suffer from a lack of qualified teachers, outdated programs and inadequate facilities.

15. Honduras' higher education system includes the National University and four institutions specializing in forestry, agriculture, social services and secondary teacher training. The University of Honduras has considerably expanded in recent years, and, with IDE support, has established the new Faculties of Agriculture and of Mechanical, Electrical and Chemical Engineering. The National School of Forestry, the Pan-American Agricultural School and the School of Social Services offer three-year post-secondary courses in their respective areas. The UNDP and FAO are presently assisting the School of Forestry, and USAID has in the past provided technical and financial assistance to the Agricultural School. The Secondary Teacher Training College prepares secondary school teachers through a four-year program. Although the annual requirement of new teachers is about 400, the school's output has averaged only 55 during the past five years. The Government has obtained technical assistance from the UNDP to reorganize the college, introduce modern educational techniques and establish new areas of training.

#### Non-Formal Education and Training

16. Honduras has few non-formal education and training programs, and those that exist -- for the training of skilled workers, artisans, supervisors and managers -- have had so far little impact on the economy. The creation in December 1972, however, of the Instituto Nacional de Formacion Profesional (INFOP) as an autonomous agency to promote the training of industrial workers is expected to lead to an improvement in the quality of the work force and to provide new training opportunities for adults and out-of-school youths. INFOP is currently receiving technical assistance from UNDP/ILO and bilateral sources to help set up its training programs. The upgrading of existing workers and the establishment of vocational training centers are some of INFOP's most immediate concerns.

### Education Finance

17. The Central Government has the major responsibility for financing public education, although local governments help by meeting the costs of some primary school construction and maintenance. The Government also provides private secondary schools with subsidies, which account for about 17 percent of Central Government recurrent expenditures for secondary education. The National University is autonomous and entitled by law to receive 2 percent of the national budget.

18. Public expenditure in education has increased in recent years and now stands at 18 percent of total public expenditure and 4 percent of GDP. On a per capita basis, central government expenditure in education grew from US\$6.6 in 1967 to US\$10.5 in 1972, but this latter figure is still low when compared with similar expenditures in other Central American and Caribbean countries.

19. The Ministry of Education's share of central government investment grew from 4.5 percent in 1967 to 9 percent in 1972, indicating increasing attention to fixed investment in the education sector. Major investments in the sector have included the CARE-supported primary school expansion program, the construction of secondary schools with AID assistance, and the expansion of the National University with IDB financial support. With recurrent expenditures increasing at about 12 percent per year, however, the share of fixed investment still represented only 10 percent (excluding investment in non-formal training) of total public expenditures in education in 1972. One of the principal reasons for the rise in recurrent expenditures has been a rather liberal Government policy with respect to teacher's salaries, which account for about 97 percent of recurrent expenditures in primary schools, 93 percent in secondary general schools, and 73 percent in secondary vocational schools. This leaves an inadequate proportion of expenditures for educational aids and teaching equipment.

### Development Program

20. The Government is anxious to improve the quality and efficiency of the educational system by modernizing teaching methods and curricula; by upgrading the teaching staff and improving physical facilities; by correcting existing imbalances through providing increased educational opportunities in the rural areas and in public secondary schools; and by reforming technical education and expanding non-formal vocational training. To carry out these plans in an effective manner, it proposes to regionalize the administration of education, giving local governments and communities greater responsibility for management and school supervision while retaining policy-making functions in the Ministry of Education. The Government wants also to consolidate primary teacher training - now offered at 47 institutions - in four schools located in key areas of the country. The Government has already enlisted the support of the UNDP and UNESCO to help in strengthening educational planning, and is

also receiving CARE and USAID financial and technical assistance in the construction of additional school facilities. The new facilities are expected to provide some 200,000 additional student places in rural primary schools and about 20,000 new places in secondary schools. This would increase the percentage of age group enrollment by 1980 to 93 percent at the primary level and 25 percent at the secondary level, and change the present ratio of enrollment in public secondary education from 26 to 46 percent of total secondary enrollment. The proposed project, which would help in improving and rationalizing the training of primary and secondary school teachers as well as in strengthening technical and vocational education, would be a suitable complement to the above efforts.

21. Implementation of the above plans would require an investment expenditure of about US\$6 million equivalent a year up to 1980, about one-half of which the Government hopes to obtain from external sources. Current expenditure would increase at an annual rate of about 12 percent, which is similar to the growth rate during the past five years. As a result, total public expenditure in education is expected to grow from 3.5 percent to 5 percent of GDP by 1980. To carry out its education development program as a whole the Government will need to adopt new revenue measures in the course of the next few years. We have reviewed this matter with the Government during negotiations and we intend to continue our dialogue in the context of our country economic work. Moreover, the Government has agreed to undertake periodic reviews of its plans and targets at the primary and secondary education levels to ensure that these plans and targets are compatible with its financial capacity. These reviews will also highlight the need for additional revenue measures.

#### PART IV - THE PROJECT

22. A report entitled "Appraisal of an Education Project in Honduras" (No. 247-HOa, dated December 7, 1973) is being distributed separately. The main features of the project and of the proposed loan and credit are summarized in Annex III.

23. The proposed project, which would be the Bank Group's first for education in Honduras, was identified by a UNESCO mission which visited Honduras at the request of the Government in July/August 1971. The mission's report served as a basis for discussions between the Bank/IDA and the Government in the second half of 1972 regarding the items to be considered for possible financing, and for the subsequent preparation of the project by the Government with UNESCO assistance. The project was appraised in the field during March/April 1973, and negotiations were held in Washington from October 29 to November 1, 1973. The Honduran delegation was led by the Minister of Finance, Mr. Manuel Acosta-Bonilla, and included the Honduran Ambassador in Washington, Mr. Roberto Galvez, and representatives from the Ministries of Education and Natural Resources, the Planning Office and INFOP.

Project Description

24. In line with the Government's development strategy, the proposed project would aim at (a) alleviating the present shortage of qualified teachers and improving and broadening the training of primary teachers to include rural community leadership; (b) increasing training opportunities for middle-level agricultural manpower and for industrial workers to meet regional needs and upgrade the labor force; (c) establishing experimental rural training centers that would provide, in addition to farmer training, training of women in home economics and of youths in rural development schemes and rural community leadership. Many of the project institutions would be located outside urban centers, thus contributing to a more equitable distribution of educational opportunities throughout the country. The following would be constructed, furnished and equipped under the project:

- (a) Two new and two extensions of primary teacher training schools, and twelve new rural primary schools for practice teaching ("application primary schools").
- (b) One secondary teacher training college and one "application secondary school";
- (c) Two vocational training centers and one industrial training development center; and
- (d) Three new agricultural training centers and the expansion of the existing agricultural secondary school.

The project would also include related technical assistance and training. The project institutions would provide a total of 5,080 student places, including 4,480 new places of which more than 50 percent would be for teacher training.

25. When completed, the four primary teacher training schools, located in the capital city of Tegucigalpa and in the western, central and eastern regions of the country, would have an enrollment capacity of 2,000 and an annual output of about 600 teachers. The schools would also have facilities for upgrading the training of unemployed teachers, thus helping to meet the annual demand of about 800 trained primary teachers. The schools' new curriculum would be improved and broadened to orient the teacher training towards the needs of the rural areas for which purpose special facilities would be constructed in all four schools. Trainees would practice in twelve application primary schools to be constructed in selected rural areas. Present teaching staff of the primary teacher training schools would be trained to implement the new curriculum. The Government has agreed to commence the in-service training program for the teaching staff not later than December 31, 1974, so that the upgrading will have been accomplished by the time the schools are completed.

26. The new secondary teacher training college, to be built in Tegucigalpa, would help satisfy the demand for secondary school teachers created by the expansion of secondary education. The college would replace an existing unsuitable one and, operating on a double shift basis, would have a total enrollment of about 1600 and an output of about 350 teachers per year. It would provide pre-service training courses of four year's duration, and short courses to train university graduates for entry into teaching. Prospective teachers would gain practical teaching experience in the application secondary school to be annexed to the college. The college curriculum would be revised under a UNDP technical assistance program.

27. The two vocational training centers - one in Tegucigalpa and the other in the principal industrial city of San Pedro Sula - would have a total capacity of 510 student places. With a two-shift system, they would upgrade some 7,200 workers and train about 1,200 new entrants to the work force each year in line with estimated manpower needs. In addition, some 2,000 to 3,000 workers would be trained on the job through in-plant programs. INFOP would be responsible for the centers and the Government has agreed to have INFOP (i) adopt occupational analysis as the basis for the curriculum, (ii) use short, self-contained training modules as a means of ensuring flexibility of the curriculum, and (iii) carry out short, supplementary training courses for graduates of the technical schools to prepare them for employment. A placement service recently established by the Government in the Ministry of Labor will, in cooperation with INFOP, help trainees from the above centers find suitable employment.

28. Incorporated in the Tegucigalpa Vocational Training Center would be an Industrial Training Development Center to help plan and implement the above program and to assist enterprises to identify their training needs and undertake in-plant programs.

29. The expansion of the agricultural secondary school at Catacamas would help increase agricultural productivity by meeting the requirements for agricultural technicians. The capacity of the agricultural school would be increased from 100 to 240 student places with an annual output of about 70 technicians. The school would be completely reorganized under the Directorate of Agricultural Development in the Ministry of Natural Resources, and the curriculum would be revised to include a greater share of practical courses. A management board chaired by the Minister of Natural Resources and representing institutions in the agriculture and education sectors would set policy and oversee the school reorganization and activities. The reorganization of the school, to be carried out in consultation with the Bank/IDA, would commence not later than December 31, 1974, and would be finished by the time of the completion of the expansion of the school.

30. The three new agricultural training centers - one each at Catacamas, La Lujosa and La Esperanza - would offer courses to farmers and homemakers with emphasis on improved farming methods, organization of cooperatives, home management and community leadership. The centers would also train extension workers and youths in rural development activities. It is estimated that with an overall capacity of 150 places a total of about 2,000 persons would be trained each year. The centers, which would be also under the control of the Ministry of Natural Resources, would be experimental in nature and would be evaluated during project implementation with a view to nationwide expansion.

31. The project would include 23.5 man/years of technical assistance and 46 man/years of fellowships. The technical specialists, to be employed under terms and conditions satisfactory to the Bank and IDA, would assist the Government in the administrative reform of education (2 man/years); in implementing the reorganization of primary teacher training and upgrading the teacher trainers (6 man/years); implementing the national vocational training scheme (8.5 man/years); carrying out the development program of the agricultural secondary school (6 man/years); and reinforcing the project unit (1 man/year). In addition, UNDP will finance 7 man/years of specialist services for the improvement of the secondary teacher training program. Under the fellowship program, local counterparts would be trained abroad in various disciplines related to the project.

32. To assure that quantity and quality improvements are met in the most efficient manner, the Government would periodically review the relationship between new students and in-service trainees to be admitted to the primary and secondary teacher training programs. The Government would also establish in all project institutions a system to trace student dropout, graduation and subsequent employment. This systematic follow-up would permit an assessment of the success of the project in attaining its objectives.

#### Costs and Financing

33. The total cost of the project is estimated at US\$8.7 million, of which US\$5.0 million, or 58 percent, represents foreign exchange costs. Construction costs make up 48 percent of the total cost; furniture and equipment, 20 percent; technical assistance, 11 percent; and physical and price contingencies, 21 percent. The proposed Bank loan and IDA credit totalling US\$6.0 million would finance about 69 percent of total project costs. US\$5.0 million of foreign exchange and US\$1.0 million equivalent of local costs. Local currency financing is justified in Honduras on the grounds that, in spite of its efforts to mobilize local resources for development, the Government must still rely upon external financing in excess of the foreign exchange component of individual projects to carry forward an effective development program. The balance of the project costs, equivalent to US\$2.7 million, would be financed by the Government. While the implementation of the education development program as a whole will be dependent on the adoption of new fiscal measures (paragraph 21), the execution of the proposed project would be needed and is feasible even in the absence of such measures. The teachers

trained under the project should be fully utilized even if enrollment ratios remained at current levels rather than being increased in accordance with the plan. The Government has agreed to make adequate annual budget provisions for the construction and subsequent operation of the project and should have the financial capacity to do so even in the absence of new fiscal measures.

#### Project Entity

34. The Government will establish a project unit within the Technical Secretariat of the Consejo Superior de Planificacion Economica (CONSUPLAN) to be responsible for overall administration of the project and to coordinate activities within the Government and provide liaison with the Bank/IDA. The unit would have a full-time director, appointed in consultation with the Bank/IDA, who would report to the Executive Secretary of CONSUPLAN but would be empowered to make all day-to-day decisions relating to the operation of the unit. The unit would also have a full-time architect or engineer experienced in school construction, an accountant and a procurement officer, all appointed in consultation with the Bank/IDA. The Ministries of Education and Natural Resources and INFOP each would appoint a project liaison officer who would, in cooperation with the project unit, be responsible for organizing within their institutions technical work required in project implementation. The Government would enter into a contractual arrangement with INFOP, satisfactory to the Bank/IDA, providing for the latter's participation in the project; the execution of such a contract would be a condition of disbursement of the loan and credit for INFOP activities. The establishment of the project unit and the appointment of the project director and architect (or engineer) would be conditions of effectiveness of the proposed loan and credit; all others mentioned above would be appointed within three months from the date of effectiveness of the loan and credit agreements.

#### Procurement and Disbursement

35. Furniture and equipment would be procured on the basis of international competitive bidding in accordance with the Bank/IDA procurement guidelines, the exception being contracts costing less than US\$5,000, which would be procured in accordance with Honduras' normal procurement procedures and which in the aggregate would not exceed the equivalent of US\$170,000. Contracts for civil works would also be awarded on the basis of international competitive bidding. However, because of their small size and dispersed location, contracts for the twelve rural primary application schools are not likely to attract foreign companies. Therefore, since there would be little, if any, advantage derived from international advertising, these contracts would be advertised locally only. Architectural and engineering design work not done by the Ministry of Education's own design group would be contracted to consulting firms under terms and conditions satisfactory to the Bank/IDA. For purposes of bid comparisons and contract awarding and at the request of the Government, Honduran manufacturers of furniture and equipment would be granted a preference of 15 percent of the c.i.f. price or the currently applicable import duty, whichever is lower.

36. For furniture and equipment the loan and credit would be disbursed against 100 percent of foreign expenditures of imported goods or 100 percent of the ex-factory cost of domestically manufactured goods. Disbursements would also be made against 100 percent of foreign expenditures for specialists' services, 100 percent of total expenditures for fellowships, and 52 percent of total expenditures for civil works and architectural and engineering design work. The disbursement schedule is indicated in Annex III.

#### PART V - LEGAL INSTRUMENTS AND AUTHORITY

37. The draft Loan Agreement and the draft Development Credit Agreement between the Republic of Honduras and, respectively, the Bank and the Association; the Report and Recommendation of the Committees provided for in Article III, Section 4 (iii) of the Articles of Agreement of the Bank and in Article V, Section 1(d) of the Articles of Agreement of the Association, respectively; and the text of two resolutions respectively approving the proposed loan and the proposed development credit are being distributed to the Executive Directors separately. Both the draft Loan Agreement and draft Development Credit Agreement conform to the normal pattern of loans and credits for education projects, and the effectiveness of one is conditioned on the effectiveness of the other.

38. I am satisfied that the proposed loan and development credit would comply with the Articles of Agreement of the Bank and the Association.

#### PART VI - RECOMMENDATION

39. I recommend that the Executive Directors approve the proposed loan and development credit.

Robert S. McNamara  
President

Attachments

December 7, 1973



COUNTRY DATA - HONDURAS

<u>AREA</u>	<u>POPULATION</u>	<u>DENSITY</u>
115,200 km <sup>2</sup>	2.7 million (mid-1972) Rate of Growth: 3.2% (from 1961 to 1972)	23.3 per km <sup>2</sup>
<u>POPULATION CHARACTERISTICS (1965-70)</u>		<u>HEALTH (1970)</u>
Crude Birth Rate (per 1,000)	49.0	Population per physician 3,707
Crude Death Rate (per 1,000)	17.1	Population per hospital bed 582
Infant Mortality (per 1,000 live births)	34.0	
<u>INCOME DISTRIBUTION</u>		<u>DISTRIBUTION OF LAND OWNERSHIP</u>
% of national income, lowest quintile	..	% owned by top 10% of owners ..
highest quintile	..	% owned by smallest 10% of owners ..
<u>ACCESS TO PIPED WATER</u>		<u>ACCESS TO ELECTRICITY (1971)</u>
% of population	35	% of population 16
<u>NUTRITION (1960-63)</u>		<u>EDUCATION (1972)</u>
Calorie intake as % of requirements	90.4	Adult literacy rate % 52
Per capita protein intake	53.6	Primary school enrollment % 87

GNP PER CAPITA in 1971: <sup>1/</sup> US \$290

<u>GROSS NATIONAL PRODUCT IN 1972</u>			<u>ANNUAL RATE OF GROWTH (% , constant prices)</u>		
	<u>US \$ Mln.</u>	<u>%</u>	<u>1961-66</u>	<u>1966-72</u>	<u>1972</u>
GNP At Market Prices	780.8	100.0	4.1	4.7	4.9
Gross Domestic Investment	127.9	16.4	9.4	5.5	0.1
Gross National Saving *	125.6	16.1	-0.2	0.8	18.5
Current Account Balance	- 2.3	0.3	.	.	.
Exports of Goods, NFS	230.6	29.5	11.5	10.1	6.2
Imports of Goods, NFS	220.9	28.3	14.3	11.7	-2.0

OUTPUT, LABOR FORCE AND PRODUCTIVITY IN 1972

	<u>Value Added</u>		<u>Labor Force <sup>2/</sup></u>		<u>V. A. Per Worker</u>	
	<u>US \$ Mln.</u>	<u>%</u>	<u>Mln.</u>	<u>%</u>	<u>US \$</u>	<u>%</u>
Agriculture	235	36.2	0.540	65.1	435	55.6
Industry	147	22.6	0.099	11.9	1,485	189.7
Services	268	41.2	0.191	23.0	1,403	179.2
Total/Average	650	100.0	0.830	100.0	783	100.0

GOVERNMENT FINANCE

	<u>General Government</u>			<u>Central Government</u>		
	<u>(Lemp. Mln.)</u>	<u>% of GDP</u>		<u>(Lemp. Mln.)</u>	<u>% of GDP</u>	
	<u>1972</u>	<u>1972</u>	<u>1970-1972</u>	<u>1972</u>	<u>1972</u>	<u>1970-72</u>
Current Receipts	222	13.9	13.9	192	12.0	12.2
Current Expenditure	207	12.9	12.5	182	11.4	11.1
Current Surplus	15	0.9	1.3	10	0.6	1.1
Capital Expenditures	55	3.4	4.9	48	3.0	4.4
External Assistance (net)	24	1.5	2.3	23	1.4	2.1

<sup>1/</sup> The Per Capita GNP estimate is at 1970 market prices, calculated by the same conversion technique as the 1973 World Atlas. All other conversions to dollars in this table are at the average exchange rate prevailing during the period covered.

<sup>2/</sup> Total labor force; unemployed are allocated to sector of their normal occupation.

\* The Annual Growth Rates are calculated on the basis of Gross National Savings as Gross National Product minus Consumption.

.. not available  
. not applicable

COUNTRY DATA - HONDURAS

<u>MONEY, CREDIT AND PRICES</u>	<u>1965</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>
	(Million Lemp. outstanding end of period)			
Money and Quasi Money	167	335	373	431
Bank Credit to Public Sector	18	54	70	80
Bank Credit to Private Sector	135	347	369	414

(Percentages or Index Numbers)

Money and Quasi Money as % of GDP	16.4	23.5	24.7	27.0
General Price Index (1966 = 100) *	99.1	108.5	110.7	114.7
Annual percentage changes in:				
General Price Index	.	3.0	2.0	3.6
Bank credit to Public Sector	.	134.9	30.5	14.1
Bank credit to Private Sector	.	16.3	6.3	12.0

BALANCE OF PAYMENTS

MERCHANDISE EXPORTS (AVERAGE 1970-72)

	<u>1970</u>	<u>1971</u>	<u>1972</u>
	(Millions US \$)		
Exports of Goods, NFS	196	216	231
Imports of Goods, NFS	244	220	221
Resource Gap (deficit = -)	- 48	- 4	10
Interest Payments (net)	- 3	)	)
Workers' Remittances	.	) - 23	) - 19
Other Factor Payments (net)	- 20	)	)
Net Transfers	7	7	7
Balance on Current Account	- 64	- 20	- 2

	<u>US \$ Mln.</u>	<u>%</u>
Bananas	86	44.3
Coffee	26	13.4
Lumber	20	10.3
Beef	13	6.7
All other commodities	49	25.3
Total	194	100.0

EXTERNAL DEBT, DECEMBER 31, 1972

	<u>1970</u>	<u>1971</u>	<u>1972</u>
	(Millions US \$)		
Direct Foreign Investment	8	7	1
Net MLT Borrowing	34	19	15
Disbursements	35	20	18
Amortization	1	1	3
Subtotal	42	26	16
Capital Grants	-	-	-
Other Capital (net) <sup>2/</sup>	2	9	4
Other items n.e.i.	6	- 9	- 6
Increase in Reserves (+)	-14	6	12
Gross Reserves (end year)	24	27	40
Net Reserves (end year)	9	15	27

	<u>US \$ Mln.</u>
Public Debt, incl. guaranteed	119 <sup>3/</sup>
Non-guaranteed Private Debt	..
Total outstanding & disburs.	..
<u>DEBT SERVICE RATIO FOR 1972<sup>1/</sup></u>	<u>%</u>
Public Debt, incl. guar'nd.	3.4
Non-guaranteed private debt	..
Total outstanding & disburs.	..

RATE OF EXCHANGE

IBRD/IDA LENDING, Dec. 31, 1972 (Mln. US \$):

<u>Through - 1971</u>
US \$ 1.00 = Lempiras 2.00
Lempiras 1.00 = US \$ 0.50

	<u>IBRD</u>	<u>IDA</u>
Outstanding & Disbursed	34.1	22.2
Undisbursed	24.2	2.6
Outstanding incl. Undisbursed	58.3	24.8

<u>Since - 1971</u>
US \$ 1.00 = Lempiras 2.00
Lempiras 1.00 = US \$ 0.50

\* Consumer Price Index.

<sup>1/</sup> Ratio of Debt Service to Exports of Goods and Non-Factor Services.

<sup>2/</sup> Net medium and long-term capital to private non-monetary sector and to the banking system.

<sup>3/</sup> Debt repayable in foreign currency disbursed.

.. not available  
. not applicable

EXCERPTS FROM PRESIDENT'S REPORT DATED SEPTEMBER 25, 1973, ON A  
PROPOSED CREDIT TO THE REPUBLIC OF HONDURAS FOR A  
SECOND LIVESTOCK DEVELOPMENT PROJECT (REPORT NO. P-1293a-HO)\*

PART I - THE ECONOMY

Recent Developments and Prospects

2. A report entitled "Basic Report on the Economy of Honduras" (CA-19a) was distributed to the Executive Directors in June 1972 (R72-190). The main recommendations of this report stress the importance of policies to diversify the economy, especially through Government action to encourage forestry, the necessity of negotiating a reasonable basis for renewed full participation of Honduras in the Central American Common Market (CACM), and the desirability of increasing tax revenues. A mission to update economic information visited Honduras in August 1973. Its findings are reflected in this summary; an Updating Economic Report is scheduled for distribution to the Executive Directors late this year.\*\* A country data sheet is attached as Annex I.

3. Honduras has a small open economy, heavily dependent on the export of bananas, although a modest degree of diversification has taken place in the last decade through the development of new export products such as meat, simple manufactures, cotton and tobacco. Its limited resources consist mainly of the fertile coastal plain in the north, a few fertile valleys in the east, and extensive but largely unexploited natural pine forests. Known mineral deposits are not extensive; they include silver, lead and zinc, which have been exploited on a small scale for decades, and low-grade iron ore. Although the average population-to-land ratio is favorable, population has traditionally concentrated in the mountainous west, the poorest agricultural area of the country, and on the north coastal plain. In the future, as population pressure increases in these areas, heavy investment in physical infrastructure will be necessary to facilitate the movement of population to less heavily settled areas further to the east. This process has already started as the road network was improved and expanded in recent years.

4. With per capita income of about US\$290 in 1971,<sup>1/</sup> Honduras is the poorest country in Central America. Real GDP rose at an average annual rate of 4.7 percent during 1965-72, but much of this expansion took place during the first three years of this period, as a consequence of substantial investment and large increases in output and export of bananas. From 1969 through 1972 economic growth has been quite low, real per capita income growing at a yearly rate of 1.2 percent. Inflation has been limited: the consumer price index rose at a rate of 2.1 percent per year from 1965 to 1972. Several factors contributed to the slow growth of the economy during the last few years, including severe hurricane damage to banana and other crops in 1969,

<sup>1/</sup> Calculated according to World Bank Atlas methodology.

\* Distributed under covering memorandum IDA/R73-103 of September 26, 1973.

\*\* Distribution has been delayed to permit a review of the findings with the Government; the report is now expected to be distributed in February 1974.

coinciding with the armed conflict between Honduras and El Salvador and the consequent reduction in private investment and the withdrawal by Honduras from the free trade arrangements of the Central American Common Market (CACM), a move which adversely affected a number of export industries. Widespread drought in 1972, and storms and floods in the banana plantations in 1973 have resulted in a large loss in agricultural production. By mid-1973, however, there were signs that the economy was pulling out of this period of relative stagnation. Export prices were improving and the Government's budgetary position was stronger. Following the severe deterioration in the balance-of-payments in 1969-70, the net international reserves' position improved during 1971-72, a move which will probably be continued in 1973. The rate of inflation in 1973 will, however, be above the historical rate and may be of the order of 5 percent, both because of the production problems in the agricultural sector and because of higher import prices.

5. The CACM was an important element in the growth of the Honduran economy during the 1960's. The CACM absorbed Honduran exports of staples which have no ready market elsewhere, and it provided the additional markets necessary for the establishment of factories making textiles, clothing, chemicals and metal products. The Honduran authorities felt, however, that the benefits of integration, especially in terms of industrial investment, were unequally distributed among the member countries. The other CACM members recognize the basis for the Honduran complaints, and during the past two years have sought solutions to the problem. As an interim solution to basic Common Market problems, Honduras has negotiated bilateral trade agreements with all its CACM partners except El Salvador. In the meantime, the Common Market Secretariat (SIECA) has prepared a study which proposes solutions to existing problems, and makes recommendations geared to the formation of a Central American Economic Community. The report has been well received by the CACM member governments, including Honduras. Once a political settlement is reached between Honduras and El Salvador -- which the two governments have indicated they expect to reach in early 1974 -- there should be more rapid progress toward integration objectives.

6. During most of the 1960's the Government sharply increased its investment in development projects. Among the major achievements in this period were the establishment of a basic transport network connecting the main population centers, the expansion of electric power and telecommunications services, and the doubling of primary school enrollment. Until 1968, there were no financial difficulties in carrying forward these schemes, mainly because of the fast growth of government revenues based on the introduction of a general sales tax and higher income tax rates in 1964, and larger tax payments by the banana companies. After 1969, however, the public sector experienced a sharp deterioration in its finances, initially because of defense and other emergency expenditures connected with the 1969 conflict with El Salvador, and later because the normal growth of government current expenditures outstripped the current revenues. Public sector savings declined from an average of 2.7 percent of GDP in 1966-68 to 1.6 percent of GDP in 1969-71. In spite of this, the public sector maintained an impressive investment effort with the average investment ratio rising from 3.6 to 6.2 percent of GDP over the same period. A large increase in net foreign financing did not cover the overall public sector deficit, and the Central Bank was required to finance the gap, equivalent to about 1.3 percent

of GDP in 1969-71. In 1972 the Central Government was able to improve its financial position, but this was in large part the result of a 20 percent drop in investment expenditures. In the first half of 1973, the Government's financial position continued to improve, but this year it was the result of an increase in current revenues and tight control over current expenditures. Investment expenditures, although not being further reduced, continued at relatively low levels in the first half of 1973. This low level in both 1972 and early 1973 results from the small number of new project starts in the preceding years. One of the Government's major concerns at present is building up a new pipeline of sound development projects responsive to the country's development objectives.

7. The military Government that took power in December 1972 announced its intention to pursue progressive development policies, and to tackle the country's fundamental economic and social problems. The new Government's development plan -- mainly a definition of objectives and policies rather than specific projects -- is expected to be ready in December 1973. Pending its completion, the new Government has been working closely with international agencies in an effort to revise and accelerate the execution of a tentative investment program prepared last year. The program provides for continued investments in physical infrastructure, especially power and transport, and a substantial increase of investment in the social sectors, particularly education and water supply and in directly productive sectors, giving special emphasis to agricultural diversification. The forestry sector offers the best opportunity for the medium-term diversification of production with good export potential. Since the first of the year, the Government has taken a number of important actions, among them the enactment of agrarian reform measures designed to resolve emergency land tenure problems while a long-term agrarian plan is designed, the formation of the long-awaited skilled labor training center and steps towards the development of forest-based industries. The new Government has indicated that it intends to introduce any necessary tax measures when the financing needs of the revised development and public investment plans are fully established.

8. Over the next five years or so, the economy is expected to recover from its recent stagnation. Banana exports, which still constitute slightly more than 40 percent of Honduras' total exports, will grow only moderately, but this is expected to be more than offset by rapidly rising exports of coffee, meat, timber and cotton. Total export growth may be of the order of 8 percent per year, thus strengthening Honduras' balance-of-payments and contributing to a faster rate of growth of GDP. The more intensive development effort expected in the public sector, along with the renewed private sector expansion (stimulated by Government activities, favorable export markets and the expected re-establishment of regional integration arrangements) will add to both import demand and development financing requirements. Thus in the medium-term the favorable prospects also mean an increased need for external assistance.

#### External Assistance

9. The external lending agencies have strongly supported public investment in Honduras. Outstanding external public debt, including undisbursed, amounted to US\$252.4 million as of December 1972. Of this total, more than 32 percent is repayable in local currency, and the ratio of debt service

payable in foreign exchange to export earnings is very low - 3.4 percent. Excluding the large proportion of the external debt repayable in local currency, the Bank's share of external debt - including undisbursed - is 34.3 percent and the IDA's share is 14.6 percent. During 1972, the percentage of Bank Group debt service in total debt service repayable in foreign currency was about 50 percent.

10. Apart from the Bank Group, external financing is provided by USAID, the Inter-American Development Bank (IDB) and the Central American Bank for Economic Integration (CABEI). USAID has been active in education, health, feeder road construction, water supply and agriculture; it was also instrumental in the formation of a private industrial finance company. IDB has been involved in housing, education, water and sewerage, and highways. It also supports agricultural and industrial projects by means of general credit lines to the government-owned development bank. CABEI is financing projects with a regional impact, primarily in transport, industry and telecommunications. Past lending of these agencies is summarized below.

COMMITMENTS BY MAJOR OFFICIAL LENDING AGENCIES

(Net of cancellations, as at June 30, 1973)

(US\$ millions)

	IBRD	IDA	AID	IDB	CABEI
Lending 1950-65	<u>25.9</u>	<u>11.9</u>	<u>26.7</u>	<u>27.2</u>	<u>18.3</u>
Lending 1966-72	<u>63.3</u>	<u>12.1</u>	<u>26.6</u>	<u>62.5</u>	<u>77.5</u>
Transport	38.0	-	-	11.6	32.9
Power	25.3	9.5	-	-	7.2
Telecommunications	-	-	-	-	4.4
Education	-	-	9.0	7.6	-
Health	-	-	2.6	-	-
Housing	-	-	-	12.5	9.7
Agriculture	-	2.6	13.0	28.6	0.1
Industry	-	-	1.5	2.2	19.8
Other	-	-	0.5	-	3.4
	-----	-----	-----	-----	-----
Total	89.2	24.0	53.3	89.7	95.8
	=====	=====	=====	=====	=====

IDB and CABEI are expected to continue financing projects in the sectors which they have financed in the past, although CABEI will focus increasingly on tourism. USAID, on the other hand, may concentrate its future lending in agriculture, depending on the results of an ongoing sector survey which it is financing.

11. Since its poverty, meager resource endowment and balance-of-payments performance have made it difficult for Honduras -- one of the least developed countries in Latin America -- to borrow substantial amounts on conventional terms, external agencies have extended financial assistance on fairly soft terms so that debt service, while it has risen significantly in the last few years, is still low. Honduras does have some margin for borrowing on conventional terms; assuming that the average terms of external borrowing were to remain more or less the same as in the past, the debt service ratio would rise to about 6.5 percent by the end of the decade, which is manageable for the Honduran economy. However, in view of Honduras' poverty, it is desirable to maintain reasonably soft average terms of assistance in the future in order to limit the burden of debt service upon both the budget and the balance-of-payments; further IDA credits are accordingly being planned.



THE STATUS OF BANK GROUP OPERATIONS IN HONDURAS

A. STATEMENT OF BANK LOANS AND IDA CREDITS (as of October 31, 1973)

Loan or Credit Number	Year	Borrower	Purpose	US\$ Million		
				Amount Bank	(less cancellation) IDA	Undisbursed
Eleven loans and credits fully disbursed				38.0	21.4	-
495	1967	Honduras	Roads	8.6	-	- 1/
179	1970	Honduras	Livestock development	-	2.6	0.7
692	1970	Honduras	Generation and transmission	5.5	-	3.9
767	1971	Empresa Nacional Portuaria	Ports	6.0	-	5.8
841	1972	Empresa Nacional de Energia Elec- trica	Generation and transmission	12.3	-	7.8
896	1973	Honduras	Roads	18.8	-	18.8
434	1973	Honduras	Second Livestock Development	-	6.6	6.6
Total				<u>89.2</u>	<u>30.6</u>	<u>43.6</u>
of which has been repaid				<u>13.7</u>	<u>0.2</u>	
Total now outstanding				75.5	30.4	
Amount sold				2.6		
of which has been repaid				<u>2.5</u>	<u>0.1</u>	
Total now held by Bank and IDA 2/				<u>75.4</u>	<u>30.4</u>	
Total undisbursed				<u>36.3</u>	<u>7.3</u>	<u>43.6</u>

1/ A balance of \$5,876 has been cancelled.

2/ Prior to exchange adjustments.

B. STATEMENT OF IFC INVESTMENTS (as of October 31, 1973)

Year	Obligor	Type of Business	Amount in US\$ million		
			Loan	Equity	Total
1964/66	Empresa de Curtidos Centroamericana S.A. (ECCASA)	Tannery	0.30	0.08	0.38
1969/70	Compania Pino Celulosa de Centroamerica (COPINO)	Pulp and Paper	-	0.08	0.08
	Total gross commitments		0.30	0.16	0.46
	less cancellations, terminations, repayments and sales		0.28	0.09	0.37
	Total commitments now held by IFC		0.02	0.07	0.09
	Total undisbursed		-	-	-

C. PROJECTS IN EXECUTION <sup>1/</sup>

Ln. No. 495 Western Highway Paving Project: US\$8.6 million Loan of May 26, 1967;  
Closing Date: September 28, 1973.

The project has been completed and final disbursement applications are being processed. A balance of \$5,900 has been cancelled.

CR. No. 179 Livestock Development Project: US\$2.6 million Credit of March 2, 1970;  
Closing Date: December 31, 1975.

The credit has been fully committed and disbursements are now proceeding on schedule.

Ln. No. 692 Fourth Power Project: US\$5.5 million Loan and US\$5.5 million  
Cr. No. 201 Credit, both of June 24, 1970; Closing Date: June 30, 1974.

Engineering studies carried out after the signing of the Loan/Credit suggested, partly because of the proposed interconnection with Nicaragua, a number of changes in the design of the project which made necessary amending the original project description. These changes have delayed bid preparation for and construction of the project's transmission and sub-transmission components by about six months. However, disbursements may still be completed on schedule by June 30, 1974.

Ln. No. 767 Second Port Project: US\$6.0 million Loan of June 25, 1971;  
Closing Date: June 30, 1975

The project provides for the expansion of Puerto Cortes in the north of Honduras, and the construction of the new port of Henecan in the South. After loan signing, the Honduran Congress, partly for political reasons associated with the border issue with El Salvador, expressed reservations about the construction of a port at Henecan. However, the Government that took office in December 1972 and the Port Authority decided to proceed with the construction of Henecan. As a result of these delays, and in spite of reasonable progress in the construction work for the expansion of Puerto Cortes, execution of the project as a whole is about 18 months behind schedule.

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<sup>1/</sup> These notes are designed to inform the Executive Directors regarding the progress of projects in execution, and in particular to report any problems which are being encountered, and the action being taken to remedy them. They should be read in this sense, and with the understanding that they do not purport to present a balanced evaluation of strengths and weaknesses in project execution.

Ln. No. 841 Fifth Power Project: US\$12.3 million Loan of June 28, 1972;

Closing Date: June 30, 1976.

In addition to the installation of diesel generating equipment, this project provides for the Honduran portion of the interconnection between the power systems of Honduras and Nicaragua. Installation of the diesel units is proceeding on schedule. Initial delays in the negotiations with the Nicaraguan utility company and major local customers may cause a slippage in the completion of the transmission components of the project; but full disbursements are still expected by the closing date of June 30, 1976.

Ln. No. 896 Sixth Highway Project: US\$18.8 million Loan of May 30, 1973;

Closing Date: June 30, 1977.

This loan became effective on August 27, 1973. Preparation of bidding documents for the construction of the Tegucigalpa-Talanga road are well advanced and tenders should be invited shortly.

HONDURAS - EDUCATION PROJECT  
LOAN, CREDIT AND PROJECT SUMMARY

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- BORROWER: Republic of Honduras.
- AMOUNT: Loan: US\$3.0 million  
Credit: US\$3.0 million
- TERMS: Loan: 30 years, including 10 years of grace;  
interest at 7-1/4% per annum.  
Credit: Standard.
- PROJECT DESCRIPTION: The project consists of:
- (1) Construction, furniture and equipment for:
    - (a) Primary teacher training
      - (i) two new and **extension of two** existing regional teacher training schools;
      - (ii) **twelve new rural application primary schools**
    - (b) Secondary teacher training
      - (i) one new teacher training **college**
      - (ii) one application secondary school.
    - (c) Vocational training
      - (i) two vocational training centers.
      - (ii) one industrial training development center.
    - (d) Agricultural education and training
      - (i) **three new agricultural training centers**
      - (ii) **expansion of the existing agricultural secondary school**
  - (2) Technical assistance covering 23.5 man-years of specialists' services and 46 man-years of fellowships for Honduran staff.

ESTIMATED COST:  
(US\$ millions)

	<u>LOCAL</u>	<u>FOREIGN</u>	<u>TOTAL</u>
Furniture and equipment	0.22	1.50	1.72
Civil works, professional services	2.57	1.62	4.19
Technical Assistance and Fellowships	0.07	0.90	0.97
Contingencies	0.81	0.97	1.78
TOTAL	3.67	4.99	8.66
(%)	(42.4)	(57.6)	(100.0)

FINANCING PLAN:  
(US\$ millions)

	<u>LOCAL</u>	<u>BANK/IDA</u>	<u>TOTAL</u>
Furniture and equipment	0.02	1.70	1.72
Civil Works	2.02	2.17	4.19
Technical Assistance	0.07	0.90	0.97
Unallocated	0.55	1.23	1.78
TOTAL	2.66	6.00	8.66
(%)	(30.7)	(69.3)	(100.0)

ESTIMATED DISBURSEMENTS:

(Loan and Credit combined)

US\$ Thousands by Fiscal Year

<u>1974</u>	<u>1975</u>	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>Cum. Total</u>
20	430	1,590	2,790	1,170	6,000

PROCUREMENT ARRANGEMENTS:

Furniture and equipment contracts estimated to cost the equivalent of US\$5,000 or more will be subject to international competitive bidding in accordance with the Bank/IDA procurement guidelines. For purposes of bid comparison and contract awarding goods manufactured in Honduras would be granted a preference of 15 percent of the c.i.f. bid price or the currently applicable import duty, whichever is lower.

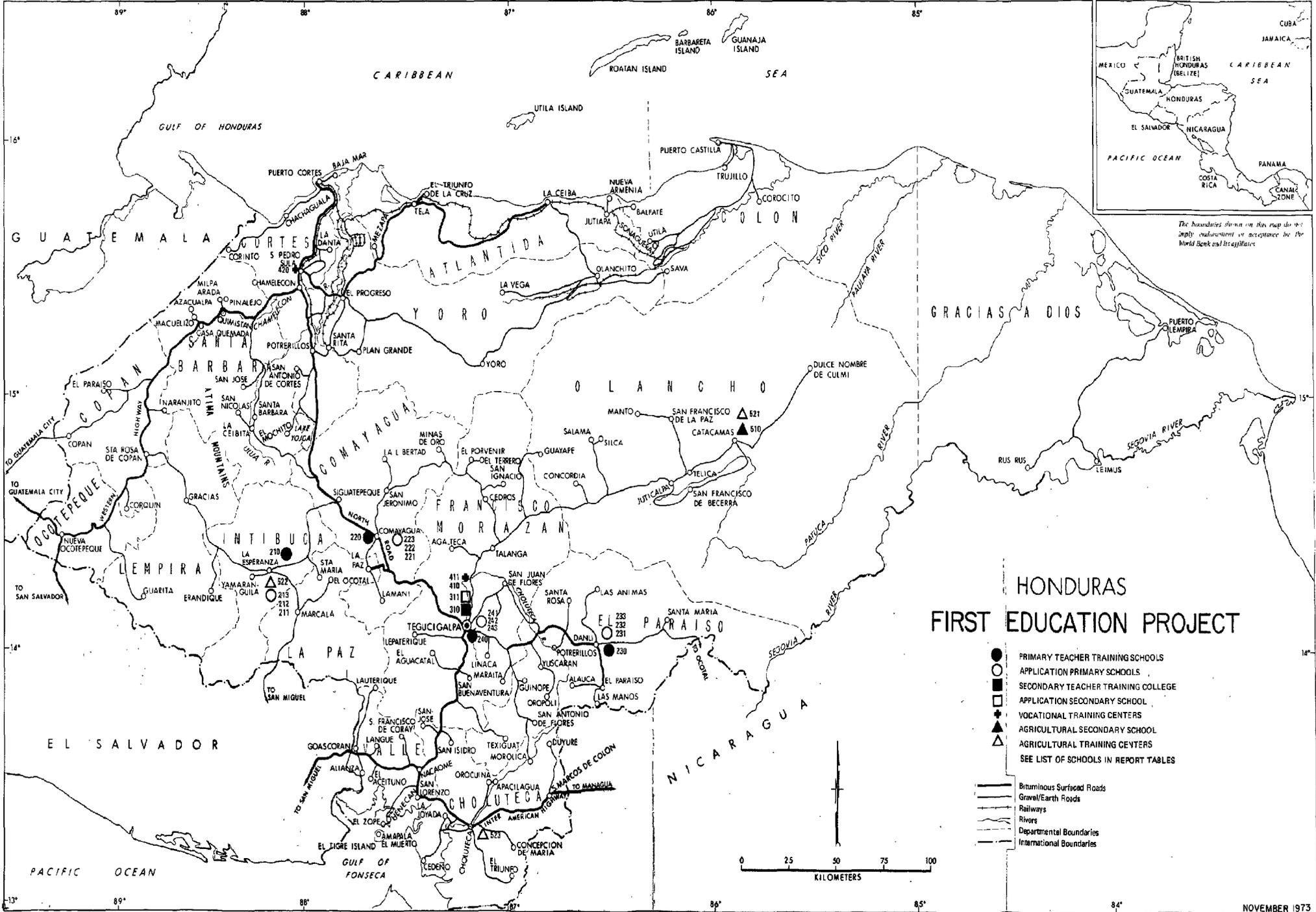
PROCUREMENT ARRANGEMENTS:  
(continued)

Contracts for civil works would also be awarded on the basis of international competitive bidding, except for the twelve rural primary application schools. Because of their small size and dispersed location, contracts for the latter are not likely to attract foreign companies and would be advertized locally only. Architectural and engineering design work not done by the Ministry of Education's architectural unit would be contracted to consulting firms under terms and conditions satisfactory to the Bank and IDA.

APPRAISAL REPORT:

Report No. 196a-HO dated December 7, 1973.





The boundaries shown on this map do not imply endorsement or acceptance by the World Bank and its affiliates.

## HONDURAS FIRST EDUCATION PROJECT