

Energy Sector Structural Adjustment

Report No: ; Type: Report/Evaluation Memorandum; Country: Honduras; Region: Latin America And Caribbean; Sector: Oil & Gas Adjustment; Major Sector: Oil & Gas; Project ID: P007384

The Honduras Energy Sector Adjustment Program, supported by IDA credit of US\$50.6 million equivalent under Credit 2306-HO and IDA reflows of US\$65.9 million equivalent under related Credits 2306-1-HO and 2306-2-HO, was approved in FY92 and closed on March 31, 1996, after a delay of 27 months. The Inter-American Development Bank (IDB) provided parallel financing of US\$105 million equivalent for disbursement in three tranches, of which US\$50 million was for adjustment and US\$55 million was disbursed for investment in power system distribution. The IDB also provided an additional tranche in the amount of US\$20 million. The Implementation Completion Report (ICR) was prepared by the Latin American and Caribbean Regional Office, and includes an evaluation report on the program by the Borrower.

The main objectives of the reform program under this adjustment loan were to: (a) establish a comprehensive energy policy and strategy, and a sound energy framework; (b) strengthen the efficiency, planning and financial soundness of the national power company (ENEE); (c) improve electricity pricing and resource allocation in the sector; (d) promote petroleum exploration and production; (d) liberalize petroleum products trade; and (f) encourage greater private sector participation in the development of the energy sector. These objectives were to be achieved through implementation of the following elements: (i) sectoral institutional reform and strengthening; (ii) electricity pricing based on sound economic criteria and financial improvement targets; (iii) clearer government policy-making and supervisory responsibilities and performance accountability on the part of ENEE; (iv) a Management and Operational Restructuring Program (MORP) to improve ENEE's performance and a Financial Rehabilitation Plan (FRP) to restore ENEE's financial soundness; and (v) petroleum liberalization program.

The sectoral adjustment program designed for implementation under this credit has been partially executed. For the power subsector, a framework was adopted establishing the organizational structure and functions of its institutions, plus rules for access to the grid, load dispatch, installation of new capacity, and privatization of the distribution system. A National Electric Regulatory Commission (CNEE) was established to advise the Government, set rules for expansion plans, calculate tariffs and oversee the performance of the subsector. Tariffs have been designed on the basis of economic principles and by 1996 ENEE's tariffs averaged 90% of long run marginal costs. Private sector participation in the power subsector is now allowed, and there are some agreements in place for private power projects. Liberalization of the petroleum subsector has been initiated, with entry of the private sector in the importation of crude and petroleum products, and elimination of guaranteed margins for refining, trading, transportation and retail trade in these products. However, the reform process became slow, uncertain, and spotty at times during program implementation. Notable shortfalls in accomplishments, or pending actions, in the reform process are as follows: (a) ENEE has not achieved operational and financial targets and there are issues on the autonomy of the subsector which need to be resolved; (b) liberalization of the petroleum and gas subsector is yet to be completed, especially on the pending issue of participation of the private sector in exploration and production, and price controls for gasoline, diesel, kerosene and LPG for domestic use.

OED agrees with the ratings in the ICR. Outcome is rated as marginally satisfactory, sustainability as uncertain, and institutional development impact as modest. OED agrees with the ICR's rating of Bank performance as satisfactory, with some qualifications. As stated by the ICR, the design of the conditionalities during identification was deficient, and the appraisal was completed before satisfactory agreements with the Borrower had been reached on some key issues. In particular, lack of agreement on institutional reform of the energy sector and operational autonomy for ENEE led to problems during implementation.

The main lesson from this sector adjustment program, which was so critical to macro-economic health, is that before approval and disbursement of the credit/loan, it is vital to obtain all necessary agreements on issues, goals and required actions during implementation.

The ICR is satisfactory and provides a good account and analysis of the implementation history.

OED will audit this project.