

Trade Policy Review Body

TRADE POLICY REVIEW

HONDURAS

Report by the Secretariat

This report, prepared for the Trade Policy Review of Honduras, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from the Government of Honduras on its trade policies and practices.

Any technical questions may be addressed to Mr Raymundo Valdes (tel. 022.739.5346, Mr Angelo Silvy (tel. 022.739.5249, or Mr Karsten Steinfatt (tel. 022.739.6759).

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SUMMARY OBSERVATIONS

INTRODUCTION

Honduras has taken important steps to liberalize both its trade and investment regimes, and thus become increasingly integrated into the global economy. Applied MFN tariffs have been lowered to an average of 6 per cent, and limited use is made of non-tariff trade measures. New laws have been passed in areas such as foreign investment, customs procedures, government procurement, and several service activities, although their implementation is yet to be completed in some cases. The anti-export bias still present in the trade regime has been in part counteracted through the use of free-trade zones (FTZs). These have been key generators of employment and investment but their long-term rationale may need reconsideration in the light of Honduras' modest rates of overall economic growth.

The rapid growth of FTZ production has transformed manufactures into a key export, but market and product diversification for merchandise exports remains limited. Remittances from Hondurans living abroad make a vital contribution to external balances. Relations with the United States are paramount on both accounts. Honduras' increasing participation in preferential agreements may help diversify its economic links, but its weak institutional capacity makes it exceptionally difficult to negotiate and implement effectively multiple agreements. Honduras thus has much to gain by seeking to strengthen the multilateral trading system, and by expanding its multilateral commitments to lock in its own reforms and thus shore up its efforts to improve the living standards of the Honduran population.

ECONOMIC ENVIRONMENT

In recent years, Honduras' economy has been growing steadily but at a slow pace, although available data may underestimate the actual level of economic activity. Average

GDP growth over the 1995-2002 period was 3.1 per cent, barely higher than the rate of population growth. Honduras' per capita GDP, at some US\$900, thus remains one of the lowest in Latin America. Although development indicators have improved during the last decade, it is estimated that some two thirds of the population still live in poverty.

Honduras has followed programmes of structural reform and monetary discipline to try to accelerate economic growth. As a result, inflation has fallen but competitiveness has been undermined by a real currency appreciation. On the fiscal side, measures have been introduced to curtail the Central Government deficit which, however, remains relatively high. Structural reform has been slow in addressing the inefficiencies in State-owned enterprises, the regulatory weakness in financial services, and the low level of competition in certain domestic markets.

International trade plays a crucial role in the Honduran economy. The share in GDP of trade in goods and services was 95 per cent in 2002. Exports are dominated by products from the maquila industry, in particular clothing, and by agricultural products such as coffee, shrimps, and bananas. The United States is by far Honduras' main trading partner, including in maquila products.

Honduras' external current account traditionally posts a deficit, due mainly to a high merchandise trade deficit. Remittances from workers living abroad, mainly in the United States, and external aid play important roles in financing the current account deficit. Foreign direct investment has increased in importance, having reached an accumulated total of close to US\$1.7 billion in 2001. The United States is the largest investor, but FDI inflows from countries in Central America and Mexico are also important. Honduras has benefited from the Highly-Indebted Poor Countries programme and from the renegotiation of its debt in the Paris Club under the Naples terms.

TRADE AND INVESTMENT POLICIES

Honduras joined the GATT in 1994 and became a WTO Member in 1995. It grants at least MFN treatment to all its trading partners. To facilitate the implementation of multilateral agreements, Honduras has adapted several domestic statutes. As a developing country, Honduras has made use of the transition periods provided for in the different WTO Agreements.

Honduras has made numerous notifications to the WTO, but as of March 2003 several were pending in areas such as customs valuation, import licensing, quantitative restrictions, technical barriers to trade, trade-related investment measures, and services. Honduras participated in the WTO negotiations on financial services in the framework of the GATS; the Fifth Protocol was ratified in 1999. Honduras did not participate in the WTO negotiations on telecommunications, nor does it participate in the Information Technology Agreement.

Important steps have been taken to liberalize Honduras' legal and investment framework. However, some reforms have not been fully implemented. Honduras has stepped up its efforts to fight corruption and to strengthen its institutional capacity, which are both important initiatives to promote trade and investment.

Honduras has given growing importance to its participation in preferential agreements. It has been a member of the Central American Common Market since 1961. Although most intra-regional trade is now duty-free, a few exceptions persist; market access is also hindered by technical barriers to trade, and sanitary and phytosanitary requirements. As a member of the Central American Common Market, Honduras has signed or is negotiating free-trade agreements with Canada, Chile, Dominican Republic, Mexico, Panama and the United States. The latter is seen as crucial and Honduras has given priority to its

successful negotiation. In addition, Honduras participates in the negotiations on a Free Trade Area of the Americas.

As is the case for many other countries following similar strategies, Honduras' growing network of preferential agreements raises concerns about the transparency of the trade regime, and possible trade and investment diversion. The burden of negotiating and administering such agreements is of special concern in the case of Honduras, given its limited institutional capacity.

MARKET ACCESS IN GOODS

Since the early 1990s, Honduras has made significant strides towards liberalizing its market access regime for goods. The simple average applied MFN tariff fell to 6 per cent in 2003, from around 17 per cent in 1993. The tariff structure shows clear escalation; a more uniform tariff structure would promote economic efficiency. All tariffs are ad valorem and bound at a ceiling rate of 35 per cent or lower, except for a few products with ceiling rates of up to 60 per cent. For a handful of products, applied tariffs may exceed bound levels. Lower bindings would further improve market access predictability.

As part of a price band system, imports of maize, some of its products, and sorghum are subject to tariffs that vary in inverse proportion to world prices. Domestic processors may import certain grains at preferential duties provided they also purchase the local production. Imports of certain goods needed for the development of FTZs, and tourist and mining operations are exempt from tariffs.

Internal taxes are generally applied in a non-discriminatory manner. Domestically grown flowers are exempt from sales tax. Apparently, sales taxes applied to imported cigarettes and certain beverages are calculated on the basis of the price of the corresponding domestically produced goods.

Steps have been taken to expedite customs procedures through the adoption of an automated system. Honduras has applied the WTO Customs Valuation Agreement since February 2000 and ceased using minimum values at the beginning of 2003.

Honduras has never applied anti-dumping or countervailing duties, nor has it implemented safeguard measures.

The use of non-tariff barriers appears to be limited. However, transparency needs to be improved, as none of the technical regulations currently in force has been notified to the WTO. Two WTO Members have raised concerns about Honduras' sanitary and phytosanitary measures, but no formal complaints have been lodged.

OTHER MEASURES AFFECTING TRADE

Honduras' last remaining export tax was eliminated in 2000 and no export quotas are in force. Export prohibitions reflect international commitments and security considerations, except in the case of wood from certain forests, which cannot be exported unless incorporated into furniture or furniture parts.

Honduras assists its exports through two, largely equivalent, FTZ regimes. Both exempt eligible firms from import duties and other taxes, including income tax. Another scheme, known as the Temporary Import Regime, is more limited and allows eligible firms to import free of duty and other charges inputs and machinery for the production of export goods. Honduras reserved its right to use the special procedure agreed to by the WTO Ministerial Conference at Doha to request an extension of the transition period to phase out export subsidy programmes.

Honduras is not a party to the Plurilateral Agreement on Government Procurement. A new law adopted in 2001 is likely to diminish discretion in this area and increase competition and transparency, but much will depend on the establishment of an

institutional structure to implement the law. The law establishes a margin of preference for domestic producers and products, and limits the extent to which foreign-based firms can participate in public procurement.

Honduras has no general competition policy legislation, and certain legal provisions currently in force might encourage anti-competitive behaviour. The State plays a key role in certain sectors, such as telecommunications and electricity, and controls the prices of a limited number of products.

The TRIPS Agreement came into force in Honduras on 1 January 2000. Honduras has stepped up action to improve IPR protection, including through new legislation on copyright and industrial property; this has been notified to the WTO and reviewed by the TRIPS Council.

SECTORAL POLICIES

Agriculture accounts for almost one quarter of GDP and is a crucial source of jobs, employing some 38 per cent of the working population. Production is concentrated on a few products, with bananas, coffee, maize, and sugar cane representing almost half of agricultural value added. No legal constraints exist on the production or marketing of agricultural products. In the wake of natural disasters and adverse international market conditions, most notably for coffee, the sector has benefited from official financial assistance, including debt forgiveness. In late 2002, the Government launched the Agricultural RoundTable, a consultation mechanism between the public and private sectors to design a comprehensive agricultural policy to confront the sector's long-standing problems.

The contribution of manufacturing to GDP is around 15 per cent. Two sectors account for the bulk of manufacturing value added: food, beverages, and tobacco; and textiles and clothing. The latter has grown rapidly and is mostly located in FTZs, whose importance as

generators of employment and foreign exchange continues to increase. In time, however, and because of their distorting effects, it may become necessary to reassess the net economic benefits of these schemes.

The services sector is of considerable importance for Honduras, contributing over half of GDP. Honduras has made efforts to reform some essential service sectors in the past few years, in particular electricity and telecommunications, but results have been modest. Although new legislation has been adopted to enhance competition in both sectors, attempts to privatize have not been successful, and State-owned monopolies remain dominant. The banking sector experienced serious difficulties in past years, leading to the enactment of new and stricter

regulations. Despite the changes, however, the sector remains institutionally weak.

In the WTO, Honduras has bound commitments with respect to four broad service categories. It has included a number of horizontal limitations to foreign investment in its Schedules of Specific Commitments. The reforms undertaken in its regulatory system in recent years go way beyond its WTO commitments. The legal regime could thus be strengthened and its predictability enhanced by binding multilaterally this autonomous liberalization. This could also help attract more FDI and contribute to the modernization of sectors vital for the development of the country.