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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT

FOR A PROPOSED LOAN

IN THE AMOUNT OF US\$1.25 BILLION

TO

THE REPUBLIC OF PERU

FOR THE

BOOSTING HUMAN CAPITAL AND PRODUCTIVITY

DEVELOPMENT POLICY FINANCING WITH A DEFERRED DRAWDOWN OPTION

January 16, 2016

Macroeconomics and Fiscal Management Global Practice
Bolivia, Chile, Ecuador, Peru and Venezuela Country Management Unit
Latin America and the Caribbean Region

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REPUBLIC OF PERU—GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange rate effective as of January 13, 2016)

Currency Unit = Peruvian Sol (PEN)

US\$1 = 3.43 PEN

ABBREVIATIONS AND ACRONYMS

AEO	Authorized Economic Operators
BCRP	Peruvian Central Bank (Banco Central de Reserva del Perú)
BOP	Balance of Payments
CGR	General Comptroller's Office (<i>Contraloría General de la República</i>)
CPS	Country Partnership Strategy
DDO	Deferred Drawdown Option
DIGEIE	General Directorate for School Infrastructure
DIGESU	General Directorate of University Education within MINEDU
DPF	Development Policy Financing
DRE	Regional Education Directorate (<i>Dirección Regional de Educación</i>)
FDI	Foreign Direct Investment
FTAs	Free Trade Agreements
FY	Fiscal Year
GDP	Gross Domestic Product
GIZ	German Corporation for International Cooperation (<i>Deutsche Gesellschaft für Internationale Zusammenarbeit</i>)
GFS	Government Finance Statistics
GRS	Grievance Redress Service
IBRD	International Bank for Reconstruction and Development
IMF	International Monetary Fund
INACAL	National Quality Institute (<i>Instituto Nacional de Calidad</i>)
INDECOPI	National Competition and Consumer Protection Agency (<i>Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual</i>)
LAC	Latin America and the Caribbean
MEF	Ministry of Economy and Finance
MINEDU	Ministry of Education
OECD	Organization for Economic Cooperation and Development
OSCE	Peruvian Public Procurement Agency (<i>Organismo Supervisor de las Contrataciones del Estado</i>)
PEFA	Public Expenditure and Financial Accountability assessment
PFM	Public Financial Management
PISA	Programme for International Student Assessment
PRONIED	National Program for School Infrastructure
PSIA	Poverty and Social Impact Analysis
SECO	Swiss State Secretariat for Economic Affairs
SEDLAC	Socio-Economic Database for Latin America and the Caribbean
SIAF	Integrated Financial Management System
SUNARP	National Superintendence of Public Registry (<i>Superintendencia Nacional de los</i>

Registros Públicos)

SUNEDU	National Superintendence of University Education
TSA	Treasury Single Account
TUPA	Administrative Procedure Text (<i>Texto Unico de Procedimientos Administrativos</i>)
UGEL	Local Education Management Unit (<i>Unidad de Gestión Educativa Local</i>)
UIT	Unit Tax (<i>Unidad Impositiva Tributaria</i>)
VAT	Value Added Tax
WBG	World Bank Group
WCO	World Custom Organization
WDI	World Development Indicator
WTO	World Trade Organization

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REPUBLIC OF PERU
BOOSTING HUMAN CAPITAL AND PRODUCTIVITY
DEVELOPMENT POLICY FINANCING WITH A DEFERRED DRAWDOWN OPTION

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LOAN AND PROGRAM SUMMARY

REPUBLIC OF PERU

BOOSTING HUMAN CAPITAL AND PRODUCTIVITY

DEVELOPMENT POLICY FINANCING WITH A DEFERRED DRAWDOWN OPTION

Borrower:	Republic of Peru
Implementing Agency:	Ministry of Economy and Finance (MEF)
Financing Data:	<p>IBRD Loan Amount: US\$ 1.25 billion. Terms: Flexible Loan at 6 Month Libor plus variable spread, with a maturity of 14 years and 13.5-year grace, with bullet repayment of principal. Front end fee: 0.25 percent of loan amount to be financed from own resources. Stand-by fee: 0.50 percent on the Unwithdrawn Loan balance</p>
Operation Type:	Development Policy Financing with a Deferred Drawdown Option (DPF-DDO)
Main Policy Pillars and Program Development Objective(s):	The objectives of the DPF-DDO are to support Peru's efforts to boost human capital and productivity by: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade.
Result Indicators	<p>The PDOs and program supported have the following result indicators:</p> <ul style="list-style-type: none"> • <i>Increase the share of programmed merit-based promotions and appointments for teachers and school principals within the Teaching Career outside Lima and Callao from 60% in 2014 to 75% in 2017.</i> • <i>Increase the number of secondary schools that implement the new school-day model from 0 in 2014 to 1500 in 2017; and include learning outcomes in the stated targets of the performance-based financial incentive mechanism for subnational entities; baseline: 0% in 2014, target: 100% in 2017.</i> • <i>Increase private sector investment in the construction and/or maintenance of public schools from 0 in 2014 to US\$150 million in 2017.</i> • <i>The number of universities and university programs under revision to be licensed increases from 0 in 2014 to 20 in 2017.</i> • <i>Number of new firms incorporated online in the System of Online Registration (Sistema de Intermediación Digital-SID); 0 before October 2014; 5,000 by 2017.</i> • <i>Number of bureaucratic barriers voluntarily removed from the legal framework by entities of the Public Administration due to an action of INDECOPI; 91 in 2013; 1,000 between 2014 and 2017.</i> • <i>Reduction in the average amount of monthly withholdings (which would increase liquidity for firms) due to the system by US\$70 million from 2014 to 2017.</i> • <i>Increase in the average recovery rate of creditors on insolvencies from 28.5% in 2014 to 36% in 2018.</i> • <i>The time to import declines by 10% in 2017 compared to 2014.</i> • <i>Increase in the number of Conformity Assessment Bodies for products, processes, and management systems by 20% from 2014 to 2017 (baseline: 115 in 2014, target: 140 in 2017).</i>
Overall risk rating:	Moderate
Operation ID:	P156858

IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO THE REPUBLIC OF PERU

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed Boosting Human Capital and Productivity Development Policy Financing with a Deferred Drawdown Option (DPF-DDO) aims to support Peru's efforts to foster productivity growth under a more challenging external environment.** Lower export demand, including from China, worsening terms of trade, and the prospects of higher borrowing costs are affecting a large number of emerging economies. In this context, a larger portion of economic growth in Peru will have to come from further productivity gains. The proposed DPF-DDO supports measures targeting key productivity constraints by enabling the improvement of the quality of human capital, fostering competition pressures, and facilitating trade. Given the Presidential elections in mid-2016¹, the proposed operation is a stand-alone DPF-DDO. Nevertheless, the reforms supported are the first installment of widely backed medium term reform programs—the National Competitiveness Plan 2014-18 and the National Education Project to 2021. This DPF-DDO will also help to maintain the dialogue with the next government, facilitating the implementation of the reform agenda. The proposed amount for the DPF-DDO is US\$ 1.25 billion.

2. **Sound macroeconomic and structural policies over the last 20 years, also supported by favorable external conditions over the last decade, rendered significant growth and poverty reduction.** Peru grew at an average of 4.5 percent per year during 1990–2013 (compared to regional and global growth of around 3 percent). Under a more favorable external environment for its commodities, Peru grew at an even faster average rate—above 6 percent per year—during the last decade. Growth helped Peru to reduce poverty from 55 to 24 percent of the population between 2001 and 2013, faster than other countries with similar income levels (Figure 1). Growth was also widely shared: between 2004 and 2013, real income per capita of the bottom 40 percent grew at an average rate of 6.8 percent, faster than the national average (Figure 2). Growth was the main driver of poverty reduction and inequality primarily through improved labor incomes rather than redistribution policies, and in the context of a smaller size of the state relative to other higher middle income countries.

3. **Peru continues to have a sound macroeconomic policy framework.** Throughout the period of high growth and unlike many countries, Peru saved the commodities' windfall, leaving itself with significant savings to continue to afford needed investments and strong macroeconomic buffers to face more challenging times. Indeed, domestic savings increased from just above 10 percent of GDP in the early 1990s to 24 percent in 2014, with public sector savings playing a key role over the last 10 years. Growth slowed to 2.4 percent in 2014. The recovery is expected to be gradual since Peru's growth potential in the following years is likely to be lower compared to that of the last decade under the assumption of a non-temporary price adjustment on the country's main exports. The current account is hovering around 4 percent of GDP and remains mostly covered by FDI and portfolio investments. Foreign exchange reserves stood at 32 percent of GDP or 20 months of imports by the end of December 2015. Monetary policy has been prudent and the Central Bank

¹ The first round of the Presidential election is planned for April 2016 and the second round, if needed, would take place in June 2016.

adheres to a well-established inflation targeting regime. The strong macroeconomic buffers have allowed the country to undertake a moderate and temporary fiscal impulse with the aim to smooth the economic transition to the less favorable external environment, without compromising macroeconomic stability. A gradual fiscal policy tightening is expected to begin in 2017—the fiscal deficit is projected to peak at 3 percent of GDP in 2016 and come down to 2.5 percent in 2017. Public debt has remained relatively low at 20 percent of GDP and net public debt was 3 percent of GDP in June 2015 (one of the lowest in the world).

4. **Under a less favorable external environment, growth will have to rely much more on productivity.** While growth requires a number of important ingredients, increasing productivity will be a critical one in Peru. Productivity contributed to about a third of the country’s growth over the last years, but there is still a large productivity gap with high-income countries. Peru’s growth dividend from closing that gap is significant and this can be supported through deeper and sustained reforms targeting key determinants of productivity growth in Peru: human capital, competition, and trade.

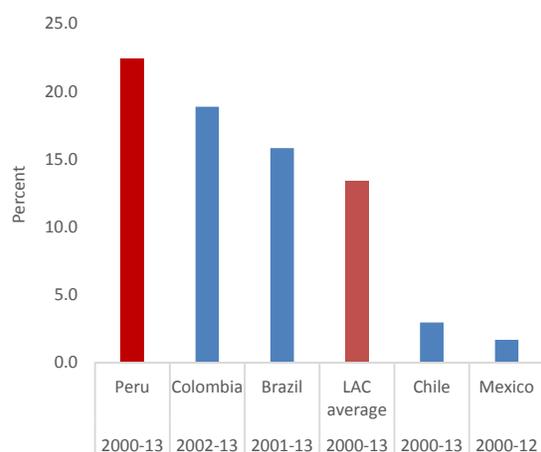
5. **Against this background, the authorities have started a new wave of reforms supported by two parallel DPF-DDOs.** This operation supports the objectives of the authorities’ reform agenda to boost firms’ human capital and productivity focusing on: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade. Among other important factors limiting growth are the country’s infrastructure gaps and managing the available resources for public investments adequately. A parallel and complementary DPF-DDO, would support measures to improve the management and reporting of public expenditures in subnational governments and to improve the legal and institutional framework for public-private partnerships (PPPs). The objectives of these DPF-DDOs are fully aligned with key parts of the Country Partnership Strategy (CPS).

6. **From a financing perspective, the proposed DPF-DDO is an important element of the authorities’ medium term financial plan and a buffer to negative shocks.** The proposed operation supports the authorities’ medium term financing plan, debt maturity, and cost strategy. The authorities see the DPF-DDO as a very useful alternative, particularly as borrowing costs for emerging economies may increase in the context of the tapering of monetary policy in the United States. They also value the hedging feature of the DDO, particularly in times of volatility in international capital markets. This type of financing may also help as a buffer for other shocks if they materialize beyond expectations. For example, the climatic phenomenon El Niño may have a strong adverse effect on the country’s infrastructure and on economic sectors such as agriculture and fisheries. In the context of strong institutions for macroeconomic management authorities in one government use disbursements out of DDOs, but leave new contingent financing options to future governments, as demonstrated in with the use of resources in the previous DPF-DDOs of 2008-09.

7. **A DPF-DDO is also important for policy and institutional reform continuity.** The authorities value the technical support of the World Bank’s policy-based financing. This support is embedded in the proposed DPF-DDO design, preparation, and supervision. With a Presidential election in mid-2016, this instrument also signals an ongoing commitment to policy reforms. That is, by focusing on policy changes with long-term impact, which are also anchored in the widely

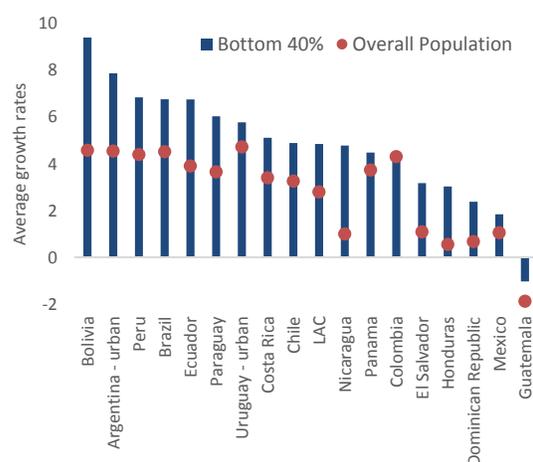
backed medium-term reform programs of the country that go well beyond 2016, this operation supports policy and implementation continuity beyond the financing option for the incoming administration.

Figure 1. Growth has been pro poor
(poverty reduction in percent)



Source: World Bank staff calculations based on data from the National Institute of Statistics and Information, Economic Commission for Latin America & the Caribbean.

Figure 2. Growth has been broadly shared
(average annual per capita income growth)



Source: World Bank staff calculations based on SEDLAC and WDI. Note: From 2004-13 for Peru.

2. MACROECONOMIC POLICY FRAMEWORK

2.1 RECENT ECONOMIC DEVELOPMENTS

8. **Peru’s growth over the past decade was one of the fastest in the Latin America and Caribbean region (LAC), but its pace has recently slowed.** Between 2004 and 2013, GDP grew at an average annual rate of 6.2 percent on the back of prudent macroeconomic policies, structural reforms, large foreign direct investments, and a favorable external environment. Growth slowed in 2014 to 2.4 percent—still faster than the average for the LAC region (which advanced only 0.8 percent). Public investment in real terms contracted by 2.0 percent in 2014; the main driver was slow execution rates of subnational governments despite an increase in central government’s public investment due to construction and improvement of roads across the country. A weak external environment with declining commodity prices and the economic slowdown of key trading partners (especially China) led to a contraction of private investments and exports. At the same time, and like in other mineral exporting countries, the economy suffered from the postponement of large mining projects. Performance of the fishing sector was affected by weather related events.

9. **The current account deficit narrowed slightly in 2014, and remained chiefly financed by foreign direct investment (FDI).** The current account deficit improved marginally from 4.2 percent of GDP to 4.0 percent in 2014 (Table 1), owing to a decline in the outflow of foreign firms’ profits which outweighed the impact of the fall in commodity prices. Copper and gold are the two most important commodities in Peru and accounted for about 35 percent of total exports in 2014. Copper prices have been declining since 2011. But overall commodity exports represent only about

13 percent of GDP. Net FDI reached 3.8 percent of GDP, down from 4.5 percent of GDP in 2013, mainly due to a slowdown in the extractive industry investments. The terms of trade deterioration of 2013-14 is expected to continue in 2015. International reserves fell slightly from US\$65.7 to US\$62.3 billion between 2013 and 2014. But they remain at comfortable levels, accounting for 32 percent of GDP or 20 months of imports by the end of December 2015.

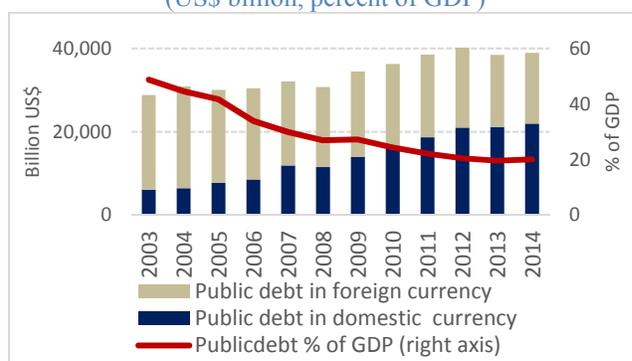
10. **Inflation expectations remain well-anchored.** Average inflation, measured by the consumer price index, amounted to 3.2 percent in 2014, only marginally above the upper level of the target band. In an effort to mitigate the slowdown, the Peruvian Central Bank (*Banco Central de Reserva del Perú*, BCRP) reduced its policy rate from 4 to 3.5 percent in 2014 and further to 3.25 percent in January 2015. It also eased reserve requirements to free up 4.9 billion of *Soles*. The reduction in the policy rate has recently been reversed—the BCRP increased the policy rate to 3.5 percent in September 2015 and to 4 percent in January 2016 to temper inflationary expectations. The BCRP also allowed the currency to depreciate, especially during the last months of 2014. The *Soles* depreciated by 6.3 percent in 2014 and by 14.5 percent in 2015, after lifting temporary interventions to smooth out the rate of depreciation. Additional de-dollarization measures were initiated in the last quarter of 2014, particularly higher reserve requirements for foreign currency deposits and Repo operations in local currency to support credit growth in *Soles*. The dollarization ratio of private sector credit fell from 38 to 31 percent between November 2014 and November 2015. Growth of private sector credit slowed to an annualized rate of 10.4 percent in November 2015, compared to 10.6 percent in November 2014. Furthermore, between November 2014 and 2015, credit in local currency surged by 29.2 percent while credit in foreign currency shrank by 19.4 percent, the lowest rate recorded so far.

11. **The banking sector remains profitable, well-capitalized, and resilient to external shocks.** The ratio of regulatory capital to risk-weighted assets remained stable at 14.3 percent as of November 2015. The banking system's return on equity remained among the highest in the region and reached 22 percent in November 2015. The non-performing loans (NPLs) ratio for the banking sector is low, but increased slightly from 2.5 to 2.6 percent between November 2014 and 2015. The ratio of provisions to overdue loans remains high at 160 percent in November 2015. For the financial system as a whole—including banks, municipal credit unions, and other lending institutions (excluding cooperatives)—the NPLs ratio slightly increased from 2.9 percent in November 2014 to 3.0 percent in November 2015.

12. **The overall fiscal balance turned from a surplus in 2013 into a small deficit in 2014.** The overall balance of the general government fell from 0.7 percent of GDP in 2013 to -0.3 percent of GDP in 2014 as a result of the economic slowdown and a moderate fiscal impulse that started in late 2014. The fiscal impulse for 2014/15 consists of a gradual reduction in income tax rates and higher current expenditures (mainly salaries). The fiscal cost of these measures is estimated at 0.25 percent of GDP in 2014 and 1.6 percent of GDP in 2015. In 2015, the general government deficit is expected to increase primarily because of the continued gradual reduction in income tax rates while overall spending is expected to stay at a comparable level, as percent of GDP, to 2014. The expected fiscal deficit for the general government in 2015 is projected to be around 2.4 percent of GDP.

13. Public debt levels remain low owing to sound macroeconomic policy management in recent years. In 2014, Peru’s total public debt stood at US\$39 billion, or 20.1 percent of GDP, down from 42 percent in December 2005 (Figure 3), one of the lowest in Latin America (Figure 4). The reduction in public debt followed a decade of high real GDP growth accompanied by overall fiscal surpluses. There has also been a significant change in the debt structure: domestic currency denominated debt now represents more than half of the total public debt while it was close to eight percent a decade earlier. The average maturity of debt also increased from 8 to 12 years between 2001 and 2014. Markets have recognized Peru’s prudent macroeconomic policies by continuously upgrading its sovereign debt ratings. Moody’s upgraded Peru’s sovereign rating in July 2014 from Baa2 to A3, with a stable outlook, reflecting, in addition to a sound macroeconomic management, a good record in implementing structural reforms in pension systems, health care, education, and public private partnerships for infrastructure investments.

Figure 3. Public debt
(US\$ billion, percent of GDP)



Source: MEF, BCRP and World Bank staff estimates.

Figure 4. Public debt in LAC in 2014
(Percent of GDP)

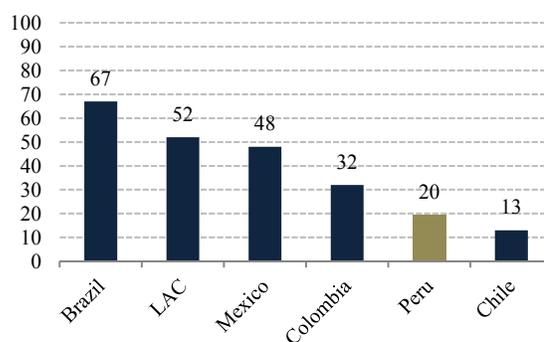


Table 1. Peru: Key Macroeconomic Indicators, 2011-2017

	2011	2012	2013	2014	2015	2016	2017
Real sector	Annual percentage change, unless otherwise indicated						
GDP (nominal--local currency)	469,854	508,326	545,554	575,250	593,901	628,066	666,637
Real GDP	6.5	6.0	5.8	2.4	2.7	3.3	4.5
Per Capita GDP (In US\$ Atlas Method)	5,378	5,634	5,891	5,962	6,052	6,182	6,390
Contributions:							
Consumption	4.2	4.6	4.0	3.6	2.9	2.3	2.5
Investment	3.3	2.8	3.0	-1.4	-0.5	1.4	1.8
Net exports	-1.1	-1.4	-1.2	0.2	0.2	-0.4	0.1
Imports	11.6	11.3	2.9	-1.5	-1.8	2.7	3.1
Exports	6.9	5.8	-1.3	-1.0	-0.9	1.0	3.9
Unemployment rate (ILO definition)	3.9	3.6	3.9				
GDP deflator	5.2	2.1	1.5	3.0	0.6	2.4	1.6
CPI (average)	3.4	3.7	2.8	3.2	3.8	3.5	2.8
Fiscal Accounts	Percent of GDP, unless otherwise indicated						
Expenditures	19.8	20.3	21.6	22.6	22.6	23.3	22.5
Revenues	21.8	22.4	22.3	22.3	20.2	20.3	20.0
General Government Balance 1/	2.0	2.1	0.7	-0.3	-2.4	-3.0	-2.5
Selected Monetary Accounts	Annual percentage change, unless otherwise indicated						
Base Money	15.1	12.2	14.8	8.8			
Credit to non-government	21.6	13.3	18.4	13.5			
Interest (key policy interest rate)	4.25	4.25	4	3.5	3.5		
Balance of Payments	Percent of GDP, unless otherwise indicated						
Current Account Balance	-1.9	-2.7	-4.2	-4.0	-4.3	-4.2	-3.3
Imports	25.6	25.2	24.7	23.9	20.5	20.6	20.3
Exports	29.7	27.2	24.1	22.4	18.2	17.4	17.0
Foreign Direct Investment	4.4	6.1	4.5	3.8	4.1	3.9	3.7
Gross Reserves (in US\$, eop)	48,859	64,043	65,711	62,353			
In months of next years' imports	15.8	18.7	18.7	18.3			
As % of short-term external debt	7.7	7.2	10.2	8.9			
External Debt	28.2	30.8	30.1	31.8			
Terms of Trade (percentage change)	6.9	-2.0	-5.7	-4.6	-5.8	-3.9	-1.8
Exchange Rate (average)	2.8	2.6	2.7	2.8			
Other memo items	Percent of GDP, unless otherwise indicated						
GDP nominal (in million US\$)	170,564	192,680	201,849	202,597	185,594	184,725	196,070
Non-Financial Public Sector (NFPS) balance	2.0	2.3	0.9	-0.3	-2.7	-3.0	-2.6
Gross Public Debt	22.1	20.4	19.6	20.1	22.9	24.8	25.5
Net Public Debt	8.6	5.0	3.7	4.0	3.0		
Gross NFPS financing needs (in million US\$)	-1,993	-2,788	1,288	3,895	7,750	7,396	7,624
External	1,024	967	967	382	2,718	5,743	2,339
Internal	-3,017	-3,755	321	3,513	5,032	1,653	5,285

Source: Government of Peru data and World Bank staff calculations and projections.

Table 2. Peru: Key Fiscal Indicators, 2011-2015
(Percent of GDP)

	2011	2012	2013	2014	2015	2016	2017
Overall Balance	2.0	2.1	0.7	-0.3	-2.4	-3.0	-2.5
Primary balance	3.2	3.1	1.8	0.8	-1.4	-1.8	-1.3
Total Revenues (and grants)	21.8	22.4	22.3	22.3	20.2	20.3	20.0
Tax revenues	16.4	16.9	16.8	17.0	15.2	15.3	14.9
Taxes on goods and services	7.5	7.5	7.7	7.8	7.3	7.6	7.5
Direct Taxes	7.2	7.3	6.7	7.0	5.8	5.6	5.4
Taxes on international trade	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Other taxes	1.5	1.8	2.1	1.9	1.8	1.8	1.8
Non-tax revenues	3.4	3.4	3.2	3.1	2.8	3.0	3.0
Social insurance contributions	1.9	2.0	2.1	2.2	1.9	1.9	2.0
Capital revenues	0.1	0.1	0.2	0.1	0.2	0.1	0.1
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Expenditures	19.8	20.3	21.6	22.6	22.6	23.3	22.5
Current expenditures	14.6	14.7	15.5	16.7	16.8	17.1	16.4
Wages and compensation	4.9	5.0	5.4	5.9	6.2	6.4	6.3
Goods and services	5.1	5.6	5.8	6.1	6.2	6.3	5.9
Interest payments	1.2	1.1	1.1	1.1	1.0	1.2	1.2
Current transfers	3.5	3.0	3.2	3.6	3.4	3.2	2.9
Capital expenditures	5.2	5.7	6.1	6.0	5.8	6.2	6.1
Capital investments	4.9	5.4	5.6	5.5	5.3	5.8	5.7
Capital transfers	0.3	0.3	0.5	0.5	0.5	0.5	0.4
Non-financial Public Sector financing requirements	-1.3	-1.4	0.7	1.8	4.0	3.8	3.7
Amortization	0.7	0.9	1.6	1.5	1.4	0.8	1.1
Non-Financial Public Sector balance 1/	2.0	2.3	0.9	-0.3	-2.7	-3.0	-2.6

Source: Multiannual Macroeconomic Framework for 2016-18 from MEF and Government of Peru data.

1/ The general government balance includes the central and local governments' balances but excludes public enterprises. The Non-Financial Public Sector balance includes the general government balance and the balance of non-financial public enterprises.

Table 3. Peru: Balance of Payments Financing Requirements and Sources, 2011-2017

	2013	2014	2015	2016	2017
BOP financing requirements and Sources					
Financing requirements (US\$ million)	-16,369	-15,296	-13,842	-14,119	-14,437
Current account deficit	-8,474	-8,031	-8,025	-7,834	-6,440
Long term debt amortization (excl. IMF)	-5,731	-5,287	-6,020	-6,285	-7,997
Other short term capital outflows	-2,164	-1,978	203	0	0
Financing Sources (US\$ million)	16,369	15,290	13,842	14,119	14,437
FDI and portfolio investments (net)	13,883	6,005	3,805	4,522	5,141
Capital grants	0	0	0	0	0
Long term debt disbursements (excl. IMF)	5,388	7,103	8,517	9,202	9,273
Change in reserves	-2,907	2,171	1,508	384	11
IMF credit (net)	0	0	0	0	0

Source: Government of Peru and Central Bank data, and Bank staff calculations and projections.

2.2 MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

14. **Economic growth is projected to be slightly above its 2014 level and to recover gradually in 2016-17.** The recovery path is based on the assumption of a non-temporary price adjustment on the country's main exports and as a consequence a reduced growth potential over the projection period compared to that of the last decade.² Investment continues to be low in 2015 due to sluggish private investments. Total investment is projected to rebound somewhat in 2016 on the back of an increase in public investments and a stabilization of private investment, including the start of several large public-private partnership infrastructure projects. Over the past few years, the government has signed on 10 new projects, equivalent to US\$14.3 billion. The large public investments will support growth in 2016 despite stagnating exports and a slowdown of public consumption. Exports are projected to remain low in 2016 but would start to rebound in 2017 when the fishery sector is expected to recover and several mining projects are expected to have entered into production (e.g., Antamina, Toromocho, Inmaculada, Invicta, Constancia, Shahuindo, Las Bambas, and Cerro Verde). But the positive outlook is subject to downside risks due to global export demand, financial conditions, and uncertainty regarding the execution rates of the large infrastructure investment projects.

15. **The current account deficit is projected to hover at around 4-4.5 percent of GDP in 2015 and 2016 and to narrow thereafter.** This deficit is projected to be financed by FDI inflows and government's long term borrowing. The decline in exports due to falling commodity prices in 2015 is partly counterbalanced by the depreciation of the currency. Moreover, prices of imports also fell netting out the decline in exports—import prices fell by 9 percent relative to a 13 percent price decline of exports. The current account deficit is projected to be around 4.3 percent of GDP in 2015. It is projected to remain at that level (4.2 percent of GDP) in 2016 as global demand for commodities is expected to remain weak and the climatic phenomenon “El Niño” is expected to continue to reduce the exports of the fishery sector in 2016. But it would recover starting in 2017 on the back of a gradual export recovery.

16. **Inflation is expected to remain well-anchored.** Despite edging slightly above the upper target band in 2014 (3.2 percent), inflation projections between 2015 and 2018 are between 3 and 4 percent. The *Sol's* depreciation may affect inflation for tradable goods in 2015, but the effect will be compensated for by decreasing commodity prices. The inflation rate is expected to increase somewhat to 3.8 percent in 2015, slightly above the higher level of the band fixed by the Central Bank, and then start to decline again. Monetary policies are expected to continue to support price stability.

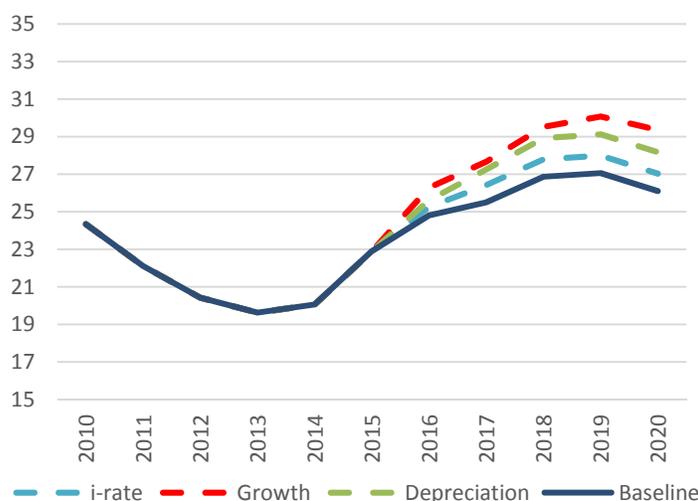
17. **The general government deficit is expected to peak at 3.0 percent of GDP in 2016 and decline thereafter.** The large fiscal buffers accumulated over the past decade have allowed for a moderate and temporary fiscal impulse smoothing the economic transition to the less favorable external environment. The fiscal impulse started in late 2014 and is projected to continue into 2016. The projected increase in the fiscal deficit by 0.6 percentage points of GDP in 2016 (compared to 2015) is expected to be driven primarily by public investments (and a marginal carry over effect of the wage increase of late 2014). But a gradual fiscal policy tightening is expected to start in 2017. The fiscal deficit is projected to decline to 2.5 percent of GDP in 2017, primarily driven by

² Early 2015 World Bank and IMF estimates suggest that potential output growth amounts to 4.5 percent of GDP.

expenditure retrenchment. While the government is projected to maintain the level of capital expenditures in 2017, it will reduce the share of current expenditures in GDP (Table 2). The deficit is expected to gradually decline to 1 percent of GDP by 2020 in structural terms. Fiscal policies are expected to uphold the Fiscal Responsibility and Transparency Law³ which limits government debt to 30 percent of GDP. The government is expected to continue to implement a prudent medium term fiscal framework, including strengthening the control over subnational expenditures. Peru’s Medium-Term Fiscal Framework projects gross financing needs to be US\$22 billion from 2016-18, three-fourths of which are planned to be funded externally.

18. **Peru’s low public debt levels are resilient to adverse economic shocks.** In the baseline scenario (Table 1),⁴ total public debt is expected to increase until 2019 as a result of the fiscal deficits, and to start declining thereafter (Figure 5). The debt analysis indicates resilience to different economic shock scenarios. A real interest rates increase of 2 percentage points for two consecutive years would raise the debt to-GDP ratio—it would peak at 28 percent in 2019 and start declining thereafter (Figure 5). The debt-to-GDP ratio is projected to rise to 28.2 percent in 2020 in a scenario of a real depreciation of 30 percent for two consecutive years and to 29.4 percent in a scenario of a one-time growth shock (reducing economic growth to 0 percent in 2016).

Figure 3. Debt Sustainability Analysis
(Debt as percentage of GDP under different scenarios)



Source: MEF, BCRP, and World Bank staff calculations.

19. **The risks to the economic outlook stem from external conditions and domestic factors and other exogenous shocks.** Growth rates are vulnerable to further shocks in mineral prices, a further slowdown in external demand for Peruvian exports, and unexpected global volatility and higher borrowing costs transmitted through financial channels. Volatility in mining prices

³ The guidance also includes the following elements: (1) the non-financial level of spending must be consistent with the structural balance target; and (2) the growth rate of wage and pensions spending cannot exceed the nominal growth rate of potential GDP.

⁴ The real interest rate in the baseline scenario is the average nominal interest rate on public debt minus the projected inflation rate (see Table 1).

represent an important risk for the overall economic outlook. Copper and gold are the two most important commodities in Peru and accounted for about 35 percent of total exports in 2014. But these external risks have a limited potential fiscal impact. Revenues from commodities account for a relatively small portion of central government budget—11.7 percent of total revenues or 2.3 percent of GDP in 2014. A further 10 percent decline in copper prices is estimated to worsen the fiscal balance, *ceteris paribus*, by 0.3 percentage points of GDP. On the other hand, any further decline in oil prices is beneficial for growth and the fiscal accounts since Peru is a net oil importer. Domestic sources of risk include the pace of implementation of the public investment program and a possible deterioration of investors' confidence associated with the elections in mid-2016. Additionally, the climatic phenomenon El Niño may have a strong adverse impact over the next 12 months hampering the exports of the agriculture and fisheries sectors in 2016.

20. Ample macroeconomic buffers, access to international financial markets, and a strong track record in macroeconomic management place Peru in a strong position to mitigate the potential impact of adverse economic shocks. Peru has full access to international capital markets. The net public debt is about 3 percent of GDP in June 2015—one of the lowest in the world. Furthermore, the Fiscal Stabilization Fund provides an additional buffer in case of continued negative external shocks, although the resources in this Fund can only be used for gross financing needs if specific criteria are met. The Fiscal Stabilization Fund's resources increased from US\$100 million in December 2000 to US\$9.1 billion in December 2014 (4.5 percent of GDP). The government's sound macroeconomic management also provides a buffer against negative external shocks in the short term. The government's strategic debt management approach has resulted in low levels of public debt, high average maturity rates (12 years), and a low exposure to foreign currency risks. An effective asset management policy has resulted in high international reserves and ample fiscal buffers. Prudential regulations in the financial sector have further reinforced macroeconomic policies. Peru's macroeconomic policy framework is sustainable over the medium term and hence adequate for the proposed operation.

2.3 IMF RELATIONS

21. The government maintains an ongoing dialogue with the International Monetary Fund (IMF) on macroeconomic policy in Peru. On May 20, 2015, the IMF's Executive Board concluded the Article IV consultation and highlighted that, in spite of downside risks on the horizon, the existence of ample buffers places Peru in a comfortable position to respond to future shocks. The IMF Assessment Letter from December 7, 2015, is presented in Annex 3.

3. THE GOVERNMENT'S PROGRAM

22. The government's long term development plan is captured in the Bicentennial Plan: Peru to 2021.⁵ The Plan was published in March 2011 and presents long term objectives along six strategic axes: (i) citizen's rights and dignity; (ii) opportunities and access to basic services; (iii) state and governance; (iv) economic growth, competitiveness, and employment; (v) regional development and infrastructure; and (vi) natural resources and environment. This operation supports key reforms under the strategic axes (ii) and (iv) of the Bicentennial Plan (the parallel and

⁵ http://www.mef.gob.pe/contenidos/acerc_mins/doc_gestion/PlanBicentenarioversionfinal.pdf

complementary DPF-DDO supports key reforms under the strategic axes (iii) and (v)).

23. **The short and medium term reforms and objectives of this plan under the strategic axes (ii) and (iv) are further detailed and reflected in the National Education Project to 2021⁶ and the National Competitiveness Agenda.⁷**

24. **The National Education Project to 2021 includes measures supported under one of the pillars of this DPF-DDO. Its relevant strategic objectives are:**

- Strategic objective 1 seeks to ensure that schools meet the essential conditions for learning by providing basic inputs and services and adequate infrastructure nationwide.
- Strategic objective 2 aims at improving the students' acquisition of basic skills oriented to personal and professional development, drawing upon an extended school-day, the use of information technologies, and educational support programs.
- Strategic objective 3 seeks to strengthen the vocation service for teachers and to link promotions to professional achievement and work environment in the context of a merit-based Teaching-Career.
- Strategic objective 4 aims to modernize the management of the education system, including the provision of incentives for subnational entities that are responsible for key decisions such as hiring teachers and appointing directors.
- Strategic objective 5 aims at improving the service supply of universities and other tertiary educational institutions and to consolidate the functioning of the national system of accreditation and certification of the quality for university education.

25. **The National Competitiveness Agenda includes key measures supported by the DPF-DDO. Specifically, the relevant strategic areas of action are:**

- *Entrepreneurship Development (Area 1)*: under which the government aims at increasing the ability of Peruvian enterprises to enhance their productivity in local and international markets. Specific achievements under this area include reforms in the area of the quality of infrastructure, among others.
- *Internationalization (Area 3)*: under which the government aims at enhancing firms' competitiveness by easing customs processes, enhancing export and investment promotion, and strengthening regional support systems for exporting SMEs.
- *Information and communication system (Area 4)*: under which the government aims at, among others, improve the use of information technology in the government—including an online business registration at the national and subnational level, electronic tax receipts, and the launch of an electronic notification system for judicial processes.
- *Human Capital (Area 6)*: under which the government aims at enhancing the skills of the workforce by improving the quality of tertiary education and the learning supplies and facilities for students through the use of information technologies and the acquisition of

⁶ <http://www.minedu.gob.pe/DeInteres/xtras/PEN-2021.pdf>

⁷ <http://www.cnc.gob.pe/web/pagina.php?pID=647>

skills related to employability.

- *Business climate (Area 7)*: under which the government aims at simplifying all national and subnational procedures for firms' entry, operation, and exit. Actions supported range from strengthening online business registration processes, introducing a single-window electronic process for environmental impact assessments and tourism services, improving processes related to technical inspections for construction permits, among others.

4. THE PROPOSED OPERATION

4.1 LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

26. **The DPF-DDO supports the Peruvian government's National Competitiveness Agenda 2014-2018 and the National Education Project to 2021.** Although a portion of Peru's growth is already driven by improvements in productivity, in the next stage of convergence, and under the new external conditions, a larger contribution to economic growth will have to come from increasing productivity. There is evidence that low educational quality compared to countries at the same level of income reduces the adoption of more efficient technologies and workers' productivity and contributes to the high prevalence of less productive informal jobs; that markets distortions tend to misallocate labor and capital to less productive workplaces; that small and medium size firms in Peru grow very slowly compared to firms in countries at the same level of income; and that Peruvian firms trade relatively little despite a liberalized trade regime.⁸ The National Competitiveness Agenda and the National Education Project to 2021 start a new wave of reforms to deal with these issues. The DPF-DDO is structured around three pillars: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade.

27. **These pillars complement each other reinforcing the impact of the reform program.** Reducing the regulatory burden for firms and enhancing private sector competition are key to unleash private sector productivity growth in Peru. Pillar 1 aims to enhance the education policy framework to enable better quality of skills, which enable people to find a job in the more productive formal sector, addresses firms' shortage of skilled workers, and raises the probability of firms to adopt more efficient technologies. Pillar 2 supports the churning of firms that is essential to boost the country's overall productivity, by facilitating firm entry, reducing the costs of operation to facilitate firms' growth, enhancing competition forcing firms to raise their cost effectiveness or to innovate, and enabling faster firm exit so that resources can be reallocated to other productive activities in the economy. Pillar 3 adds further enabling conditions for firms to trade more easily and meet quality standards in global markets. The exposure to world markets provides additional competitive pressure forcing firms to enhance their cost effectiveness and technology adoption, boosting the productivity of the domestic economy.

28. **The DPF-DDO incorporates a number of lessons learned from the Bank's previous DPO engagements in Peru and other upper middle-income countries.** It builds on three lessons that are essential to achieve the results of this operation: (i) strong government ownership; (ii)

⁸ See "Peru – Building on Success; Boosting Productivity for Faster Growth", Flagship report launched in October 2015 during the Annual Meetings of the World Bank Group and the IMF.

significant new supportive policy initiatives that are directed to high-priority issues; and (iii) a solid track record of Bank engagement. The government requested the DPF-DDO to support reforms in high-priority areas for their objectives and with longstanding Bank engagement (including through in-depth analytical work such as the recently launched report “Peru – Building on Success; Boosting Productivity for Faster Growth”. The DPF-DDO would further help the government to signal commitment to critical reforms. Moreover, creditworthy emerging countries like Peru benefit most from programs that permit adequate flexibility to account for rapid responses to changing circumstances. In this context, the contingent financing embedded in this DPF-DDO would help support the authorities financing plans for the next years.

4.2 PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

PRIOR ACTIONS AND RESULTS

Enhancing the education policy framework to enable better quality of skills

Prior Action #1: *Increase in the teaching quality of education in economically disadvantaged areas by introducing a balanced and equitable system for recruiting and promoting qualified teachers and principals within the merit-based Teaching Career System.*

29. **Rationale.** Enhancing the quality of education and thus the human capital of the future workforce can raise Peru’s productivity. It will provide workers with the skills necessary to find a job in the more productive formal sector, address firms’ shortage of skilled workers, and raise their ability to adapt new technologies or/and management practices. There are large spatial differences in learning outcomes in Peru reducing the average quality of education and human capital in the country. Peru has one of the lowest PISA scores in English and Mathematics, in large parts due to differences in the quality of education across school provinces and districts. In fact, Peru has the largest gaps in student learning outcomes among countries participating in the PISA study.⁹ To increase the average quality of education, Law 29944 (Teacher Reform) of 2012 reformed the existing teacher law to enable the implementation of a merit-based system for hiring and promotions throughout the career for all tenured teachers. This law encouraged and rewarded high performance and sought to attract more qualified applicants, raising the quality of teaching. Still, it did not directly address the large spatial inequalities in the country that stem from the difficulties of attracting qualified teachers and principals to schools in poorer areas of the country, particularly outside Lima and Callao. For example, 70-90 percent of the teachers in rural areas are contract teachers that are not yet included in the Teaching Career system.¹⁰ Schools in disadvantaged areas also lack qualified school management and are often governed by teachers acting as interim school principals.

30. **Substance of the action.** In 2015, the reform introduced incentives to attract qualified teachers and school principals to disadvantaged regions, directly targeting schooling quality where it is needed the most. The new policy aims to ensure that the performance-based teacher career introduced in the 2012 Teacher Reform contributes to higher teacher quality in all regions, also

⁹ OECD (2014) *PISA 2012 Results: What Students Know and Can Do – Student Performance in Mathematics, Reading and Science* (Volume I, Revised edition, February 2014), PISA, OECD Publishing.

¹⁰ Kudo and Székely, 2015.

benefitting schools in disadvantaged areas which now will have a chance to recruit, promote, and retain qualified teachers and principals within the Teaching Career system. This measure has a high potential impact on Peru's average level of schooling quality. The Ministry of Education (MINEDU) introduced an algorithm-based system for determining the location of new tenure positions and promotion slots that would be opened to public competition through the Teaching Career evaluation system. This system allocates quotas to each region for entry-level and mid-level positions outside of Lima and Callao, encouraging qualified teachers to take up higher level positions in more disadvantaged regions. The design of the evaluation instruments and training program for school principals is being supported through the World Bank Basic Education project.

31. **Expected results.** The reforms are expected to increase the share of programmed merit-based promotions and appointments for teachers and school principals within the Teaching Career outside Lima and Callao from 60% in 2014 to 75% in 2017. In the medium- to long-term, it reduces spatial inequalities in the quality of schooling, raising also the average quality in the country.

Prior Action #2: *Improvement of school graduates' learning outcomes by: (i) introducing an extended school-day model for secondary education that strengthens the teaching of Math, Science, English language, and soft skills; and (ii) creating performance-based financial incentives for subnational government institutions that manage schools (UGEL and DRE) to improve the learning environment in schools.*

32. **Rationale.** Low educational quality leads to skill shortages and mismatches in the private sector inhibiting productivity growth. The results of the Program for International Student Assessment (PISA) suggest that Peru's quality of education is deficient across the board. It is lower than in most comparator countries with comparable income levels. Between 2000 and 2009, net enrollment rates in secondary education increased from 69 to 78 percent and students showed substantial improvements in average reading scores. But despite the progress, only one of four 15-year-olds has recently reached a proficiency in mathematics which would allow them to begin demonstrating the skills that enable them to participate effectively and productively in life.¹¹ This compares to an OECD average of 77 percent. Moreover, only one of three students in secondary education reaches the basic PISA level of reading comprehension (compared to 83 percent in OECD countries).¹² Increasing teaching hours tends to improve student achievements, in particular in the poorest and most disadvantaged school districts.¹³ More importantly, the extra hours are used to teach skills in Math, English, and soft skills targeting the areas with low PISA test scores as well as the skills demanded by the private sector. The recent introduction of a comprehensive system to evaluate the teachers further ensures that the extra hours improve the quality of education.

33. Tightly connected to quality shortcomings discussed above, are also the significant delays in hiring personnel and distributing learning materials in the beginning of the school year. These functions do not depend only on the Ministry of Education, but also on the regional (DRE) and

¹¹ Castro and Yamada. 2012. "Convexification" and "Deconvexification" of the Peruvian Wage Profile: A Tale of Declining Education Quality. Universidad del Pacifico.

¹² OECD (2014) PISA 2012 Results: What Students Know and Can Do – Student Performance in Mathematics, Reading and Science (Volume I, Revised edition, February 2014), PISA, OECD Publishing.

¹³ <http://blogs.worldbank.org/latinamerica/is-the-school-day-too-short-in-latin-america>

local (UGEL) education management units, which report to regional governments. This shared responsibility entails complex administrative processes that often delay the hiring process and distribution of materials to schools, hampering education quality. For instance, only 53 percent of the public schools received learning materials on time for the start of the school year in 2014. The low number is explained by large spatial discrepancies: 97 percent of schools received the materials on time in Lima and Callao compared to only one-third of schools in rural areas.¹⁴

34. **Substance of the action.** The extended school-day reform increases the weekly teaching by 10 hours. The extra teaching hours will be spent on teaching Math, English, Labor Education, Science and Technology, communication and citizenship skills. The extension of the school day is supported by improvements in school management and organization through the hiring of additional staff for administrative, pedagogical, technological, psychological, and logistical support (RM No. 451-2014-MINEDU; RM No. 174-2015-MINEDU). The program also includes additional resources and support for teachers and students. The program further provides additional computer equipment and improves school facilities. To target the delays in hiring and distribution of learning materials and equipment highlighted above, the policy supported introduces financial incentives provided to DRE and UGEL directly targeting a source of those administrative delays. Under the new policy, DRE and UGEL receive additional funds if they hire teachers and principals, distribute learning materials to schools, and enroll students in the school system on time for the start of a new school year in March of each year. Later in the year, they receive additional funding if they meet teacher attendance targets in their corresponding regions (No. 019-2014-MINEDU, No. 591-2014-MINEDU).

35. **Expected results.** The reform is expected to increase the number of secondary schools that implement the new school-day model from 0 in 2014 to 1,500 in 2017; and include learning outcomes in the stated targets of the performance-based financial incentive mechanism for subnational entities: baseline: 0% in 2014, target: 100% in 2017. In total, there exist about 8,000 secondary schools but not all of them meet the immediate requirements to introduce the extended-day model due, for example, to infrastructure constraints. Thus, the expansion of the model is planned in phases, starting with those schools that can readily implement the model. In the medium- to long term, the reform is expected to enhance the quality of secondary schooling, in particular in rural areas, reducing the large spatial differences in educational quality in Peru.

Prior Action #3: *Creation of the General Directorate for School Infrastructure within the Ministry of Education, to foster the participation of the private sector in school infrastructure upgrading, and to separate the functions of policy formulation and planning from construction.*

36. **Rationale.** The basic education infrastructure gap in Peru is large, particularly in rural areas where over 900 thousand students do not have access to proper education facilities (defined as those without basic services and insufficient room for learning activities). The 2013 Education Infrastructure Census revealed that 69 percent of school buildings would not stand an earthquake of great magnitude, 75 percent operate without proper ownership titles, and 34 percent do not have any access to water or sanitation. In addition, complementary reforms targeting the quality of education, such as the extended-school day program, require additional infrastructure investments

¹⁴ Kudo and Székely (2015) based on the National Education Survey.

to proceed as planned. The cost of closing the infrastructure gap is estimated at 100 billion *Soles*. The closure of this gap is delayed by the low current execution rates due to weak planning, coordination, and execution capacity and due to limited financing available. The previous institutional arrangements for public investment projects had overlapping mandates between the three levels of government in attracting private sector investments/financing and in planning the portfolio of infrastructure projects. The lack of a clear separation of responsibilities led to a de facto absence of private sector investments and participation in the sector despite a number of policies in the broader framework that allow for that participation.

37. **Substance of the action.** The reform improves the division of labor across all three levels of the government in promoting private sector participation and in planning school infrastructure investment projects, which is an important precondition to accelerate the closure of the school infrastructure gap in Peru. Until January 2015, the functions of planning and policy for basic education infrastructure were part of the National Program for School Infrastructure (PRONIED). However, PRONIED was only responsible for schools that were not designed and constructed by subnational governments (which is the larger share). As a consequence, the central government could not control the planning and policy of all basic education infrastructure in the country, including the promotion of private sector participation. Supreme Decree No. 001-2015-MINEDU separates the planning and policy functions of basic education infrastructure from the construction of the schools. This measure also facilitates investments by the private sector since it can match private interest with upgrading needs across the country and facilitates the process to bring-in the private sector through a number of mechanisms as described below. In particular, a new General Directorate for School Infrastructure (DIGEIE), under the reform supported, is tasked with the following planning and policy functions for all basic education infrastructure: (i) leading the process of identification, prioritization, promotion, and development of a portfolio of projects through public-private partnership investment programs, tax deductions for school infrastructure works, and other mechanisms that involves the participation of the private sector in the construction, operation, and management of public schools; (ii) formalizing ownership titles and keeping an updated public registry of school facilities and infrastructure needs; and (iii) issuing guidelines and regulations relevant to school infrastructure (e.g., design frameworks, maintenance and operation standards, roles and responsibilities across different government levels). The reform facilitates planning, coordination, sustainability, and private sector participation of school infrastructure investments.

38. **Expected results.** The reform is expected to increase private sector investment in the construction and/or maintenance of public schools from 0 in 2014 to US\$150 million in 2017. The reform will also accelerate the implementation of the complementary education reforms such as the extended school-day program (also supported by this operation).

Prior Action #4: *Improvement of the framework of university education by creating the National Superintendence of University Education (SUNEDU) and the General Directorate of University Education (DIGESU) within MINEDU to guarantee that university programs and institutions meet quality standards and to lead the implementation of the university reform.*

39. **Rationale.** In Peru, firms with a higher share of workers with higher education are more likely to adopt more efficient foreign technologies and management practices. Moreover, higher

education is one of the factors that enables graduates to find a job in the formal sector and workers to transition from informal to formal work.¹⁵ About 80 percent of Peruvian workers are employed in the informal sector even though the formal sector is four times more productive. Informal workers have on average 4 years less of education than formal workers—9.2 years versus 13.4. But a low average quality and large quality differences across higher education institutions are a major obstacle to the creation of human capital. Peru has a small group of prestigious institutions of relatively good quality, but there is substantial variation in the program quality and relevance among all institutions.¹⁶ Key determinants of low quality include outdated programs, weak institutional capacity, insufficient teaching equipment and laboratories, and the low qualification of professors—only 7 percent have a PhD and only 40 percent have a post-graduate degree. As a result, an estimated one-third of higher education graduates are not employed in their line of specialization. The creation of a higher education quality assurance system is a critical mechanism to address these weaknesses. Such a system would raise both, minimum standards and overall quality, by introducing self and external evaluations, promoting quality enhancements based on these evaluations, and providing a system of quality accreditation.

40. **Substance of the action.** The reform supported introduces independent quality control mechanisms for granting licenses to university programs and institutions as part of the higher education quality assurance system. The government enacted Law 30220 with the purpose of better regulating the university sector, accelerating the process of quality assurance¹⁷, and giving the Ministry of Education (MINEDU) a clear role and responsibility in higher education. The creation of the Superintendence for Higher Education (SUNEDU) by Decree No. 012-2014-MINEDU facilitates the process of quality assurance and supervision through the issuance of quality licenses (operation permits), the supervision of basic quality standards, and a more efficient use of public resources spent on higher education. SUNEDU further has the mandate to define new guidelines and binding quality standards for the licensing of universities. These apply to all existing and new higher education programs and institutions. The creation of the General Directorate of University Education within MINEDU (DIGESU) by Decree No. 001-2015-MINEDU facilitates the implementation of Law 30220, establishes the leadership of MINEDU in higher education, and ensures an efficient coordination with and supervision of the higher education sector.

41. **Expected results.** The New University Law (Law 30220) and the creation of the SUNEDU are expected to increase the number of universities and university programs under revision to be licensed from 0 in 2014 to 20 in 2016. This will increase the quality of higher education in Peru addressing skill shortages and facilitating the transition towards higher value added formal sector employment in the medium- to long-term.

¹⁵ See “Peru – Building on Success; Boosting Productivity for Faster Growth”, Flagship report for the 2015 Annual Meetings of the World Bank Group and the IMF.

¹⁶ Castro, Juan F., Gustavo Yamada, and Omar Arias. 2010. “Analysis of School Trajectories, Career Choice, and Insertion into the Peruvian Labor Market”. World Bank, mimeo.

¹⁷ The process was initiated earlier through a public investment project, the Project for Quality Improvement of Higher Education (PROCALIDAD) and jointly financed by the Peruvian government and the World Bank. The project aimed to support and strengthen the National System for Evaluation, Accreditation and Certification of the Quality of Education (SINEACE) and higher education institutions. The creation of SUNEDU and DIGESU, which is part of the reforms supported in this DPF-DDO, is an important new milestone in the reform process to improve the quality of higher education in Peru as it introduces a regulatory and supervision mechanism guaranteeing that the university programs and institutions meet quality standards and implement the broader university reform agenda.

Facilitating the entry, operation, and exit of firms

Prior Action #5: *Facilitation of business entry of firms by: (i) integrating online registration procedures into the system of public registries under the management of the National Superintendence of Public Registries (SUNARP); (ii) creating financial incentives for large municipalities to deliver operating licenses faster than required by law No. 28976 of February 4, 2007; and (iii) introducing a more effective risk-based classification system for technical safety inspections for new firms.*

42. **Rationale.** Facilitating business entry is a key determinant for productivity growth. It promotes the entry of innovative firms and (the threat of entry) puts competitive pressure on incumbent firms to increase their cost effectiveness and innovate. The number of licenses procedures and the time required to obtain these influences the decision of potential entrepreneurs to enter the formal sector. In Peru, 20 percent of firms report business licensing and permits as a major constraint to growth which is considerably higher than the average share of 5 percent in OECD countries. The process to comply with legal procedures to start a business in Peru required 26 days in 2014 which was significantly higher than the median number of 14 days across all countries (Doing Business, 2015). The main regulatory burden is the time spent to obtain an operating license from the municipality where the firm will be located which alone consumed on average 15 days. Part of the time is consumed by technical safety inspections as the law requires all new firms to be inspected by provincial and district governments. A risk-based classification for safety inspections would further reduce the cost for firms to enter the formal sector.

43. **Substance of the action.** Online registrations were previously managed by the Prime Minister's Office. After this reform, they are now integrated into the overall system of public registries managed by the National Superintendence of Public Registries (SUNARP). SUNARP is the most effective institution to manage online registrations as it has extensive back-office functions, including direct connections with the country's tax and customs administration. Its integrated system makes the most extensive use of electronic signatures. Furthermore, SUNARP has a growing network of front-office functions in the form of the notaries that voluntarily become portals of SUNARP's systems. The legal change also provides financial incentives for larger municipalities if they issue operating licenses within a period of 10 days. Moreover, the risk-based classification system for safety inspections would replace the existing system whereby inspected firms were selected exclusively on the basis of their location and size, especially when firms are initially registered. Municipalities often have low supervision capacities to identify higher-risk firms so that the selection can be arbitrary and left to the discretion of local public officials. The new risk-based approach preselects only firms that present major safety risks because of their activities and other relevant firm characteristics. The reforms directly target efficiencies of municipalities which consume more than half of the time for firms to enter the market.

44. **Expected results.** The new System of Online Registration became effective on October 1, 2014. The reforms are expected to increase the number of new firms incorporated online in the System of Online Registration (*Sistema de Intermediación Digital-SID*); 0 before October 2014; 5,000 by 2017. For example, improving the effectiveness of online registration systems has been shown to promote firm entry into the formal sector (World Development Report, 2016). In the long

term, the reduction in time and cost for firms to obtain an operating license from municipalities, including the more effective risk-based classification system for technical safety inspections for new firms, encourages firm entry. The increase is expected to be more pronounced in service sectors where the regulatory burden on startups was higher and problems of factor misallocation seem to be more acute.¹⁸

Prior Action #6: *Limit the discretion of all government bodies to impose regulations and administrative procedures outside the national legal framework, by strengthening INDECOPI's power to sanction non-compliance with the legal framework.*

45. **Rationale.** Many regulatory improvements to enhance competition and consequently the productivity of firms have been enacted, but significant challenges remain in the implementation of the legal framework, particularly at the subnational level. Often, municipalities, control important aspects of the regulatory environment and impose most of the bureaucratic barriers for local businesses. In 2013, three-quarters of the complaints about bureaucratic barriers outside of the legal framework originated from actions of local governments and decentralized public entities. The number of complaints increased dramatically in 2014.¹⁹ Local bureaucratic barriers enhance the discretion of (local) public officials to discriminate between firms in the implementation of rules and regulations which stifles competition, discourages firms' growth, and reduces firms' incentives to raise their cost effectiveness and innovate to break away from potential competitors. The majority of these barriers restrict competition in backbone service sectors that facilitate local market efficiency and access such as transport, telecommunication, retail, construction, or tourism.

46. **Substance of the action.** Enhancing INDECOPI's power is critical to promote competition and remove local regulatory barriers. Previously, the scope of INDECOPI's decision to act upon a particular complaint was very limited. Moreover, firms could not refer to previous rulings and had to submit their own, new complaint to INDECOPI even for administrative actions that had already been declared illegal or unreasonable based on a previous complaint of another firm. A new law in 2013 empowered INDECOPI to directly sanction responsible public officials in fast-track procedures and to act upon complaints by firms about procedures that had already been declared illegal or irrational in a precedent.²⁰ But so far these legal changes only applied to a limited number of administrative procedures. Law 30230 of 2014 supported by this operation substantially expanded the set of bureaucratic barriers that INDECOPI can directly sanction in fast-track procedures to include any rules, procedures, and illegal fees that are governed by public bodies at any government level, the *Texto Unico de Procedimientos Administrativos* (TUPA). The Legislative Decree No. 1212 of 2015 further broadens the mandate to sanction *de facto* practices by officials. Moreover, it introduces that public entities are required to repay any fees collected in the past from undue bureaucratic barriers and that they must inform all citizens within 5 days about any act that has been declared an undue bureaucratic barrier. The reform constitutes an important step to reduce the discretion of (local) public officials to discriminate between firms in the

¹⁸ See "Peru – Building on Success; Boosting Productivity for Faster Growth", Flagship report for the 2015 Annual Meetings.

¹⁹ See Licetti, Martha, Donato de Rosa and Tanja Goodwin (2015). "Peru—Tackling regulatory barriers to competition and local economy development". World Bank mimeo.

²⁰ This precedent case has to have been initiated by the Commission and not by complaint and it has to have been confirmed by the Tribunal and published.

implementation of rules and regulations.

47. **Expected results.** The reform supported creates strong incentives for all public bodies at any government level to voluntarily align their administrative procedures with regulatory best practices, which foresees no undue barriers to market access. As a result, the number of bureaucratic barriers voluntarily removed from the legal framework by entities of the Public Administration due to an action of INDECOPI is expected to increase from 91 in 2013 to 1,000 between 2014 and 2017. Rather than creating an additional legal and institutional framework, it substantially strengthens the implementation and enforcement of the existing framework building on the existing experiences of its application in practice. The alignment of administrative procedures with regulatory best practices in local government bodies will make policy implementation more consistent and predictable across the country. It will level the playing field among firms and facilitate firm entry, intensifying domestic market competition.

Prior Action #7: *Simplification of the withholding regime for VAT payments to reduce operating costs for firms.*

48. **Rationale.** Cumbersome tax regulations are one of the regulatory burdens limiting private sector competition and contributing on the misallocation of resources among firms in Peru, whereby additional capital and labor is not necessarily utilized by more productive firms over time.²¹ Tax rates, and the overall tax burden, are not high. But the National Tax Administration Supervisory Authority (SUNAT) has been lagging behind the overall modernization process in Peru’s government institutions raising the bureaucratic costs for firms to pay taxes.

49. Firms in Peru are required to comply with cumbersome withholding regimes for VAT payments which were initially introduced to reduce tax evasion. The withholding regimes for VAT payments impose additional operative costs on firms. They can also stifle competition. The regimes impose liquidity constraints on smaller firms supplying or consuming goods and services to/from these firms. And firms complying with the regimes are disadvantaged relative to competition from the informal sector or competitors supplying goods or services to firms not subject to these regimes. The idea behind these mechanisms is that designated firms—typically formal and larger firms—make their transactions (with smaller firms) visible, enforcing their VAT payment. Effectively, the tax regimes force larger firms to act as tax agents. Countries that had used these regimes at early stages of VAT implementation had raised tax collection. But the success of these regimes also implies that they must be dismantled over time to allow more standard international VAT collection procedures to become the norm, particularly as the authorities’ implementation capacity strengthens, and given the system’s shortcomings in terms of burden on businesses. There are three different withholding regimes depending on whether SUNAT trusted the “buyer,” the “seller” or neither of them:

- First, the “Perception” Regime is a mechanism whereby the seller collects prior to the delivery of the goods a portion of the VAT due to be subsequently incurred by its customers (buyers) on their sales transactions. The seller is required to deliver the collected amount to SUNAT. The reform reduces the goods and services subject to the perception regime

²¹ See “Peru – Building on Success; Boosting Productivity for Faster Growth”, Flagship report for the 2015 Annual Meetings of the World Bank Group and the IMF.

from 41 to 12. Prior to the changes 41 goods or services were subject to this regime, including, for instance, beverages, beer, wheat, and liquefied propane gas.

- Second, the “Withholding” Regime reverses the approach: the “buyer” retains a portion of the VAT payments it would have otherwise left with the seller and forward it directly to SUNAT. Up to 1500 firms are used under this scheme, mainly large firms, to collect VAT on SUNAT’s behalf from small sellers.
- Third, the so called “Detraction” Regime—System of Payment of Tax Obligations with the Central Government—which is a mechanism whereby the buyer or user of certain goods or services deposits into the National Bank (*Banco de la Nación*) a defined portion of the VAT that the latter must pay for the transaction subject to this tax. The funds are deposited in an account on behalf of the seller or provider of the service and must use those funds to pay tax obligations. While the practice started as a way to formalize the former socially owned sugar cooperatives (by now all privatized), it was applied to a vast set of sectors starting in 2012. Prior to the changes, 39 goods or services were subject to this regime, including for instance sugar cane, asparagus, cotton, and fish oil.

50. **Substance of the action.** The new law reduces the number of goods and services subject to the detraction regime from 39 to 26 (excluded goods are sugar cane, asparagus, cotton, and fish oil). At the same time, the reform reduced detraction rates for an additional 16 of the 26 goods and services. It further reduces the goods and services subject to the perception regime from 41 to 12. With these measures, the government of Peru has taken an important first steps towards introducing regular channels for VAT compliance.

51. **Expected results.** The simplification of VAT withholding regimes is expected to reduce the average amount of monthly withholdings (which would increase liquidity for firms) due to the system by US\$70 million from 2014 to 2017. This reduces the operative costs of firms, increases their liquidity available for investments, and enhances competition. The simplifications will not reduce VAT revenues if tax authorities use the historical transaction information stored in the accounts at the Bank Nacional or SUNAT effectively for tax auditing.²²

Prior Action #8: *Facilitation of business exit of firms by: (i) introducing electronic auctions for asset foreclosures in order to reduce costs and risks of insolvency; (ii) creating the Registry for Judicial Delinquent Debtors, simplifying the legal framework for insolvency; and (iii) modifying the general law of the insolvency system in terms of quality and registry of administrators and liquidators, simplification of administrative procedures under responsibility of INDECOPI, and the system of offenses and penalties.*

52. **Rationale.** High costs of insolvencies due to cumbersome bankruptcy regimes reduce the value of asset recovery and delay the exit of the least productive firms, reducing the amount of resources that can be reallocated to more productive ventures—that is, from firms that are exiting to firms that are entering or growing. This contributes to the inefficiencies in the allocation of human and physical capital across firms in Peru. Facilitating the process and reducing the costs of insolvencies are thus an integral part of Peru’s Competitiveness Agenda to increase innovation and firm productivity. It further complements the reforms that facilitate business entry and makes them

²² The Peruvian Central Bank has nevertheless estimated that the reforms can potentially reduce VAT revenues by up to 800 million Soles (about USD 250 million).

more effective.

53. **Substance of the action.** The government enacted Law 30229 to facilitate the process of exit and increase the recovery rate of firms' assets in case of insolvencies. Previously, the process of selling the assets of insolvent firms was largely non-transparent and there were limited publishing requirements leaving substantial room for discretion and lack of transparency in the way the assets were sold. As a result, Peru has a low rate of asset recovery, measuring the share of value secured creditors recover from an insolvent firm at the end of insolvency proceedings (Doing Business, 2015). Only 28.5 percent of asset values were on average recovered in 2014, well below the OECD average (72 percent) and the average across Latin American countries (36 percent). The new Law 30201 further creates this registry for delinquent debt that is public and free of charge and managed by the judiciary. Before the reform, debtors sentenced to repayment by the judiciary had to automatically initiate an insolvency proceeding, administered by the competition agency (INDECOPI). After the reform, the debt record remains in the public registry as long as the debt is not repaid which imposes a cost to the debtor reducing her credit worthiness. Furthermore, sanctions can be imposed on delinquent debtors that do not register their assets involved in the insolvency proceeding and those assets cannot be sold anymore.

54. Moreover, Legislative Decree 1189 improves the insolvency regime in three important dimensions. First, it establishes more stringent requirements to bodies that act as administrators or liquidators, ensuring their quality, credibility, and probity. Second, it defines new fines and penalties and strengthens the existing ones for those who fail to comply with the dissemination of information and required procedures. Third, it streamlines insolvency procedures by reducing the administrative burden to comply with a number of requirements. For instance, it separates the procedures for businesses disputes from non-business disputes which are to be resolved by the judiciary. These reforms provide greater security and guarantees for asset management involved in case of insolvencies and streamline the administrative burden to comply with procedures.

55. **Expected results.** The reform is expected to reduce the scope for discretion in handling the asset recovery process of insolvent firms, avoiding fraud, collusion, and price-fixing arrangements in the process. It is also expected to increase the transparency in the management and sales of the assets of insolvent firms. The reform is expected to lead to higher sales prices of insolvent firms' assets for both, creditors and debtors, reducing the cost of insolvencies. As a result, the average recovery rate of creditors on insolvencies will increase from 28.5% in 2014 to 36% in 2017. In the long term, the lower bankruptcy costs are expected to encourage (potential) entrepreneurs to take more risk and enter new markets or adopt new products or processes.

Reducing transaction costs in trade

Prior Action #9: *Improvement of the customs regime through: (i) the modernization of the Custom Law by introducing key elements of the revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures of February 3, 2006 and the Bali WTO Trade Facilitation Agreement of November 27, 2014, particularly improving the Authorized Economic Operators (AEO) regime, and adopting a more targeted system of fines; and (ii) the elimination of all stamp duties for Customs Declaration reducing transaction costs and in alignment with the Bali WTO Trade Facilitation Agreement.*

56. **Rationale.** Peru has signed a large number of FTAs with most major trading partners granting firms based in Peru preferential access to countries that together represent 73 percent of the world's GDP (92 percent of total world trade). At the same time, however, relatively few non-mining firms in Peru export or are integrated in global value chains. Despite its liberalized trade regime, Peru trades much less than other countries at a similar level of income—total exports accounted only for 22 percent of GDP in 2014, including mining exports. The government is thus embarking on a new set of reforms to enhance private sector export competitiveness to harness the opportunities given by the multiple FTAs and the country's liberalized trade regime. An important reform is the modernization of the customs regime which reduces firms' regulatory burden. Both, the World Custom Organization (WCO) and the World Trade Organization (WTO) have developed a number of recommendations to facilitate trade, such as the revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures, which entered into force in 2006, and the Bali WTO Trade Facilitation Agreement, adopted in 2014. Peru had already introduced the Authorized Economic Operators (AEO) regime under which financially solvent firms with a good track-record can apply for advanced customs clearance. But only 21 companies have yet been certified accounting for only 2 percent of total exports two years after introducing the regime. Moreover, an unrefined system of fines and penalties, which had not distinguished between administrative mistakes and intended fraud, has led to excessive costs for some exporters. Moreover, stamp duties involved transaction costs for firms in Peru, spending time for the payment and the corresponding documentations. The elimination of stamp duties thus further reduces transactions costs for firms to trade. The reform is consistent with the Bali WTO Agreement, which recommends a reduction of fees associated with import and export activities.

57. **Substance of the action.** The reforms supported under Legislative Decree 1235 will make the existing AEO regime more effective. It will also improve the system of penalties and fines to better distinguish between mistakes in administrative procedures and intended fraud while further strengthening systems of control against illegal activities. These measures will significantly reduce transaction costs in trade to firms. The new AEO regime also extends the application period for advanced clearances from 15 to 30 days before the arrival of the cargo. The accreditation requirements are simplified by facilitating solvency criteria, exempting accredited AEOs from providing financing guarantees up front, and introducing a single declaration for all shipments in a given period of time—all of which reduce firms' financial and administrative transaction costs. Moreover, the amounts of penalties and fines must now consider the context and be proportional to the offense, in particular distinguishing between intended fraud and administrative mistakes which may be non-punishable. Law 30230 of July 12, 2014 further eliminates all stamp duties which constituted a fixed payment charged for customs transactions. Stamp duties were initially

created to recover the costs of processing the single customs declaration for imports with values exceeding 3 UIT (approximately USD 3,500). Customs administrations are already financed by other tax payments so that the stamp duties represented a redundant transaction cost.

58. **Expected results.** The reforms are expected to reduce the administrative burden for firms to trade. They will decrease the time to import directly and indirectly. For example, the more effective incentive system in the new AEO regime will increase the number of operators to be accredited facilitating imports. It is expected that the time to import declines by 10 percent in 2017 compared to 2014.

Prior Action #10: *Establishment of the National System for Quality and the National Quality Institute (INACAL) to enhance the systems of accreditation, standardization, and metrology, supporting export competitiveness and access to markets.*

59. **Rationale.** Inadequate technical standards and regulations and the lack of internationally recognized quality accreditations undermine the competitiveness of Peruvian exporters and limit the gains from Peru's free trade agreements (FTAs). Until recently, overlapping responsibilities and the lack of clear mandates to issue technical standards or regulations between various institutions and ministries were undermining the development of an effective system of quality accreditations and standards. The competition authority (INDECOPI) was responsible for developing "technical standards", while various central government ministries were responsible for developing technical regulations within their spheres of competence. The lack of an effective national system of quality accreditation and trade facilitation, for instance, resulted in an insufficient number of laboratories and organizations in charge of quality and product accreditation standards. These constraints limit the ability of firms, in particular in the food-processing sector, to harness the full opportunities of Peru's multiple FTAs. The country is now starting the reforms to improve the domestic institutions that facilitate quality inspections and accreditations to help domestic firms comply with internationally recognized product and quality standards.

60. **Substance of the action.** In July 2014, the government launched the National Policy on Quality including measures to enhance the competitiveness, productivity, and trade of goods and services. It included the creation of the National System for Quality and the National Quality Institute (INACAL) by Law 30224. INACAL has a clear mandate as the sole agency issuing technical standards and regulations, establishing testing laboratories, and certifying quality standards. INACAL, which is formally associated with the Ministry of Production, is thus the only government body responsible to regulate accreditation, standardization, and metrology, enabling firms to meet international quality standards. The establishment of INACAL is part of the National Competitiveness Agenda 2014-18.

61. **Expected results.** The reform is expected to increase the number of Conformity Assessment Bodies for products, processes, and management systems by 20 percent from 2014 to 2017 (baseline: 115 in 2014, target: 140 in 2017). Over the long term (beyond the scope of this operation), it would be expected to increase the number of products exported to markets demanding higher quality standards such as the United States and the European Union.

Analytical Underpinnings

62. **The DPF-DDO is underpinned by extensive analytical work** (Table 4), such as the Peru—Building on Success; Boosting Productivity for Faster Growth report launched during the Annual Meetings 2015, a number of background papers prepared for this report, and several analytical advisory services of the World Bank, the Peruvian government or other World Bank’s resources.

Table 4. Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
<ul style="list-style-type: none"> • Prior Action #1: Increase in the teaching quality of education in economically disadvantaged areas by introducing a balanced and equitable system for recruiting and promoting qualified teachers and principals within the merit-based Teaching Career System [Resolution of the General Secretariat No. 813-2014-MINEDU and Vice-Ministerial Resolution No. 021-2015-MINEDU] 	<ul style="list-style-type: none"> • “Giving Peru a Productivity Boost: Towards a System of Continuous Education and Training.” Background report for the Peru flagship. • “XXI century challenges in education in Peru.” Background report for the Peru flagship.
<ul style="list-style-type: none"> • Prior Action #2: Improvement of school graduates’ learning outcomes by: (i) introducing an extended school-day model for secondary education that strengthens the teaching of Math, Science, English language, and soft skills [Ministerial Resolution 451-2014-MINEDU]; and (ii) creating performance-based financial incentives for subnational government institutions that manage schools (UGEL and DRE) to improve the learning environment in schools [Ministerial Resolution 591-2014-MINEDU] 	<ul style="list-style-type: none"> • “Giving Peru a Productivity Boost: Towards a System of Continuous Education and Training.” Background report for the Peru flagship. • “XXI century challenges in education in Peru.” Background report for the Peru flagship.
<ul style="list-style-type: none"> • Prior Action #3: Creation of the General Directorate for School Infrastructure within the Ministry of Education, to foster the participation of the private sector in school infrastructure upgrading, and to separate the functions of policy formulation and planning from construction [Supreme Decree No. 001-2015-MINEDU] 	<ul style="list-style-type: none"> • “XXI century challenges in education in Peru.” Background report for the Peru flagship.
<ul style="list-style-type: none"> • Prior Action #4: Improvement of the framework of university education by creating the National Superintendence of University Education (SUNEDU) and the General Directorate of University Education (DIGESU) within MINEDU to guarantee that university programs and institutions meet quality standards and to lead the implementation of the university reform [Law 30220; Decree No. 012-2014-MINEDU, Supreme Decree No. 001-2015-MINEDU] 	<ul style="list-style-type: none"> • “Innovation and firms’ productivity in Peru”. Background report for the Peru flagship. • “Tertiary education in Peru.” Background report for the Peru flagship. • “Analysis of School Trajectories, Career Choice, and Insertion into the Peruvian Labor Market.” World Bank, 2010.
<ul style="list-style-type: none"> • Prior Action #5: Facilitation of business entry of firms by: (i) integrating online registration procedures into the system of public registries under the management of the National Superintendence of Public Registries (SUNARP) [Supreme Decree No. 007-2014-JUS]; (ii) creating financial incentives for large municipalities to deliver operating licenses faster than required by law No. 28976 of February 4, 2007 [Supreme Decree No. 015-2014-EF]; and (iii) introducing a more effective risk-based classification system for technical safety inspections for new firms [Legislative Decree No. 1200] 	<ul style="list-style-type: none"> • “Peru—Building on Success; Boosting Productivity for Faster Growth”. Flagship report for the 2015 Annual Meetings of the World Bank Group and the IMF • Investment climate and competitiveness in Peru. Background report for the Peru flagship. • IFC Advisory Services on technical safety inspections.
<ul style="list-style-type: none"> • Prior Action #6: Limit the discretion of all government bodies to impose regulations and administrative procedures outside the national legal framework, by strengthening INDECOPI’s power to sanction non-compliance with the legal framework [Law No. 30230 and Legislative Decree 1212] 	<ul style="list-style-type: none"> • “Peru—Tackling regulatory barriers to competition and local economy development”. Background report for the Peru flagship. • World Bank Effectiveness of Competition Policy Advisory Services

Prior Actions	Analytical Underpinnings
<ul style="list-style-type: none"> • Prior Action #7: Simplification of the withholding regime for VAT payments to reduce operating costs for firms [Law No. 30230] 	<ul style="list-style-type: none"> • “Peru—Building on Success; Boosting Productivity for Faster Growth” Flagship report for the 2015 Annual Meetings of the World Bank Group and the IMF
<ul style="list-style-type: none"> • Prior Action #8: Facilitation of business exit of firms by: (i) introducing electronic auctions for asset foreclosures in order to reduce costs and risks of insolvency [Law No. 30229]; (ii) creating the Registry for Judicial Delinquent Debtors, simplifying the legal framework for insolvency [Law No. 30201]; and (iii) modifying the general law of the insolvency system in terms of quality and registry of administrators and liquidators, simplification of administrative procedures under responsibility of INDECOPI, and the system of offenses and penalties [Legislative Decree No. 1189] 	<ul style="list-style-type: none"> • World Bank Strategic Plan for the Judiciary Advisory Services • World Bank Evidence Based Performance Improvement Strategies for the Judicial System Advisory Services
<ul style="list-style-type: none"> • Prior action #9: Improvement of the customs regime through: (i) the modernization of the Custom Law by introducing key elements of the revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures of February 3, 2006 and the Bali WTO Trade Facilitation Agreement of November 27, 2014, particularly improving the Authorized Economic Operators (AEO) regime, and adopting a more targeted system of fines [Legislative Decree No. 1235]; and (ii) the elimination of all stamp duties for Customs Declaration reducing transaction costs and in alignment with the Bali WTO Trade Facilitation Agreement [Law No. 30230] 	<ul style="list-style-type: none"> • World Bank Strengthening Custom Risk Management Advisory Services. • The role of Imports for Exporter Performance in Peru. Background report for the Peru flagship.
<ul style="list-style-type: none"> • Prior Action #10: Establishment of the National System for Quality and the National Quality Institute (INACAL) to enhance the systems of accreditation, standardization, and metrology, supporting export competitiveness and access to markets [Law No. 30224] 	<ul style="list-style-type: none"> • Services Trade Performance and Productivity in Peru: A comparative Analysis. Background report for the Peru flagship. • The role of Imports for Exporter Performance in Peru. Background report for the Peru flagship.

4.3 LINK TO CPS, OTHER BANK OPERATIONS AND THE WBG STRATEGY

63. **The proposed operation is consistent with the WBG’s CPS for Peru for 2012-2016** (Report No. 66187-PE). The CPS is built around four strategic objectives which are key to improve shared prosperity and reducing poverty in Peru: (i) increasing access and quality of social services for the poor, (ii) connecting the poor to services and markets, (iii) promoting sustainable growth and productivity, and (iv) improving public sector performance for greater inclusion. This operation is well-aligned with the three pillars: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade.

64. **A parallel, and complementary DPF-DDO, would support measures to make public investments more effective and limit the financial risks to the government stemming from PPPs.** Boosting human capital and productivity growth in Peru relies on a number of factors. One of them is addressing the country’s infrastructure gaps which requires managing the limited available resources for public investments adequately.

65. **By focusing on facilitating the entry, operation, and exit of firms, reducing transactions costs in trade, and enhancing the quality of skills, the DPF-DDO complements**

other Bank operations in Peru. The DPF-DDO has been closely coordinated with and complements the following operations, for example, the forthcoming Innovation and Productivity Investment Loan (FY17). Furthermore, the proposed operation complements two current investment operations of the World Bank in education, the Higher Education Quality Improvement (PROCALIDAD) project and the Basic Education project.

4.4 CONSULTATIONS, COLLABORATION WITH DEVELOPMENT PARTNERS

66. **The government has extensively consulted the National Competitiveness Plan and the National Education Project to 2021, which provide the basis for this DPF-DDO.** The National Competitiveness Plan itself is the result of the joint work of the MEF and the private sector, through a well-established partnership in the Competitiveness Council. Further, there has been a strong public engagement through presentations that take place every six months to highlight the results achieved to date. The presentations are widely advertised in public media and generally include more than 1,000 participants from the private sector, trade unions, NGOs, think tanks, universities, and other stakeholders. All relevant documents are available at the Competitiveness Council's website and the MEF's website. The government consultation procedures for new legal initiatives includes a 30-business-day mandatory consultation period.

67. **The IMF also has a number of technical assistance activities in Peru, some of which are connected to the policy program supported by this operation.** For example, 2015 Article IV consultation focused on issues such as securing an economic recovery and unlocking growth potential. It included staff reports on investment dynamics and its determinants, forecasting growth and tax administration issues.

68. **The Swiss and Canadian cooperation agencies, and the Latin American Development Bank (CAF) have worked with the World Bank on reforms supported by the DPF-DDO.** The Swiss Cooperation supports the National Competitiveness Council and the implementation of the ambitious agenda and targets for 2018. The World Bank and the Andean Finance Corporation have worked closely on issues pertaining competition policy.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1 POVERTY AND SOCIAL IMPACT (PSIA)

69. **The poverty and social impacts of policy measures supported under this DPF-DDO are expected to be either positive or poverty-neutral in the short term, and to be positive over the medium term.** The policy areas covered by the operation are: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade. All policies aim to promote private sector-driven growth by facilitating the entry, operations, and exit of firms, enhancing their export competitiveness, and increasing their human capital. The reforms are expected to result in more private sector competition raising firm productivity and inducing stronger economic growth in the medium and long term. The higher growth is expected to be inclusive, with poorer segments of society experiencing a sustainable increase in well-being through better access to services and economic opportunities. The reduction in the administrative burden for formal firms and the higher

quality of secondary and higher education are expected to reduce informality which disproportionately benefits the bottom 40 percent of the income distribution. The impact of each individual reform is expected to have only marginal effects on formalization but taken together, the synergies in the proposed operation can have a noticeable impact.

70. The DPF prior actions in the policy area of facilitating firm entry and exit are likely to support poverty reduction in the medium and long term. The proposed operation increases private sector competition and reduces barriers for otherwise informal firms to enter the formal sector. As a result, the number of newly registered formal sector firms in Peru is expected to increase as soon as overall economic conditions improve. The increase is expected to be more pronounced in service sector where the regulatory burden on startups and informality are higher. These reforms thus favor the creation of more opportunities for workers to enter the formal sector which disproportionately benefits the bottom 40 percent of the income distribution who are more likely to work in the informal sector—90 percent of the poor work in the informal sector compared with 55 percent of the non-poor and 83 percent of the bottom 40 percent of the income distribution work in the informal sector compared with 49 percent of the top 60 percent of the income distribution.

71. The DPF prior actions enhancing competition by limiting the discretion of government bodies to impose illegal regulations and removing cumbersome withholding regimes for VAT payments, are not expected to have an adverse impact on poverty. The proposed operations are not expected to have a direct short term impact on poverty or the bottom 40 percent of the income distribution since they are simplifications that will ease the regulatory burden for formal firms. In the medium term, they are projected to reduce entry barriers for new firms to protected (local) markets which reduces consumer prices benefitting all consumers.

72. The DPF prior actions in the area of trade facilitation reforms have the following poverty and social impacts:

- *The modernization of the Custom Law and the elimination of all stamp duties for customs declaration are expected to have a neutral effect on the incidence of poverty in the short- to medium-term.* The reform encourages firms to trade and to import higher quality foreign intermediate inputs, raising long-term growth and reducing poverty.
- *The establishment of the National System for Quality is poverty neutral in the short term and expected to enhance the income of the bottom 40 percent in the long term.* The reform supports (smaller) firms to achieve internationally recognized quality standards which has the potential to raise exports to large high income countries enabling firms to exploit scale effects. These can create new jobs for workers in sectors such as agribusiness in the medium and long term.

73. The DPF prior actions in the area of education reforms are expected to reduce poverty and raise the income of the bottom 40 percent:

- *The enhancement of the teaching quality in education in economically disadvantaged areas is expected to contribute to the formation of human capital of poorer students from disadvantaged regions reducing poverty.* The reform enhances the access of students in disadvantaged areas to higher quality education, empowering them to find a better job and move out of poverty.

- *The enhancement of the skills of school graduates by introducing an extended secondary school-day model and the financial incentives for UGEL and DRE are expected to reduce poverty and increase the income of the bottom 40 percent.* Improving the quality of high school education is relevant for labor market success of the poor and the bottom 40 as they are less likely to pursue higher studies. Individuals from the lower quintiles of the distribution are more likely to drop-out at high-school. Thus, improving the quality of high school education can potentially be an important factor to prepare individuals for the labor market and has the potential of reducing drop-out rates from high-school, which are especially higher among the lowest quintile.
- *The creation of the General Directorate for School Infrastructure to foster the participation of the private sector in school infrastructure upgrading is expected to be poverty neutral in the short-term and reduce poverty in the long-term.* The reform supports the agenda to improve the quality of schooling, in particular in rural areas, disproportionately benefitting the bottom 40 percent of the income distribution.
- *Improvement of the framework of university education by creating the National Superintendence of University Education (SUNEDU) and the General Directorate of University Education (DIGESU) within MINEDU is expected to have positive impacts on human capital accumulation and earnings of graduates, potentially raising the income of the bottom 40 percent.* The higher quality of higher education will help graduates to find a job in the formal sector, reducing informality which disproportionately benefits the bottom 40 percent of the income distribution.

5.2 ENVIRONMENTAL ASPECTS

74. **The specific policies supported by the DPF-DDO are not likely to have significant effects on Peru’s environmental resources (e.g. forests, water resources, etc.) and natural habitats.** The policy areas covered by the operation are: (i) enhancing the education policy framework to enable better quality of skills, (ii) facilitating the entry, operation, and exit of firms; and (iii) reducing transaction costs in trade. The risk of unanticipated adverse effects to the environment and natural resources is very small. Credible scenarios for any significant, direct or indirect negative impacts appear very unlikely. For the measure related to school infrastructure, the operation supports the strengthening of planning and regulation functions that enable better engagement with the private sector and enhance coordination between the central and local governments in this area. This is an institutional reform measure without a physical footprint directly attached to it. MINEDU and subnational governments have in national policy the controls needed to comply with all country-wide regulations. Peru has adequate environmental controls in place and environmental legislation and regulations are aligned with good international practices.

5.3 PFM, DISBURSEMENT AND AUDITING ASPECTS

75. **Peru’s public financial management (PFM) and public procurement systems are sound.** A joint European Union, Inter-American Development Bank, and World Bank Public Expenditure and Financial Accountability (PEFA) assessment was published in June 2009 and updated in 2015. The report concluded that PFM in Peru has improved since 2009 in several aspects and remains in line with international best practices. The following aspects are important to highlight as regards to Peru’s PFM system:

- The Peruvian central government’s budget has improved its reliability and credibility as a financial tool. Fiscal rules, innovation and monitoring, and transparency tools enhance budget planning and predictability. There is a reduced variance between budget execution and the final budget. Budget formulation continues to follow international best practice.
- Budget classifications are compatible with international practices (IMF GFS, 2001). In addition, more than 50% of budget resources are allocated under programmatic classifications, and predictability of budget resources is working well. There are no significant delays in availability of funds or in payments for legal obligations.
- Budget execution is well documented and the Consolidated Government Financial Statements (*Cuenta General de la República*) are prepared annually within six months from the end of the year and made publicly available in both printed and electronic versions. The budget execution reports are comprehensive, providing information on revenues, expenditures, and financial assets and liabilities.
- Budget execution reports are *audited* within the legally established time periods by the CGR and conducted pursuant to the respective regulations and within the time frames established by law. In addition, legislative scrutiny of the annual budget bill is conducted in accordance with well-established procedures, which are also used in examining the general accounts (*Cuenta General*).

76. **Since 2009, Peru has undertaken critical reforms necessary to improve the management of public finances.** A new budget classification system using a programmatic approach and a new chart of accounts in line with international standards were adopted and are operating in all government ministries and agencies. The implementation of the Treasury Single Account (TSA) at the central government level and sub-national level (regional governments and municipal level) has been implemented and is working in line with international best practice. The Treasury Directorate is working now on the implementation of the TSA for external sources of funds. There has been steady progress in establishing the foundations for performance-based budgeting, with the development of well-defined measures of performance that link priority policies and programs. In 2015, 58% of the budget is allocated under the performance approach through 85 budget programs, 7 percentage point higher than in 2014.

77. **On-going efforts to continue modernizing the budget and improving PFM include:** (i) the design and gradual implementation of a multi-annual budget framework (which include all level of government’s and current and capital expenditure planning, as well debt service payments); and (ii) continued strengthening the Budget Directorate (the implementation of a unit on quality spending in the general directorate of budget have being playing a critical role in the developing of performance instruments as impact evaluations and indicators); and (iii) the design of a new Integrated Financial Management System (SIAF II).

78. **The Bank has conducted analytical work and provided technical assistance on the public procurement system.** The updated 2015 PEFA report concludes that the public procurement system follows international best practices and has improved since 2009. In 2012, the Bank suggested reforms to improve the effectiveness of Peru’s public procurement system in delivering Value for Money, including: (a) onerous requirements for bidders to participate in procurement processes, (b) the use of reference price (bracketing) “valor referencial” for

evaluation purposes, (c) financial costs linked to government contracts, and (d) skill gaps linked to low level of professionalization in procurement professionals. These, among other factors, led to low participation amongst potential bidders as well as a high rate of failure of bidding processes. Also in 2012, the World Bank supported the Peruvian Public Procurement Agency (OSCE) in the design and implementation of a sustainable training program on international best procurement practices and innovative procurement methods, in order to increase the efficiency and economy of the procurement system, particularly for the implementation of infrastructure projects. Bank support also facilitated the 2013 signing of a Technical Cooperation Agreement between OSCE and the Public Procurement Office in Chile (Chile-Compra) aiming at strengthening good practices in public procurement through the exchange of successful experiences between the two countries. In 2014, support was provided by the Bank and other donors (SECO, GIZ) to OSCE in the reform of the procurement law (Law 30225, approved in July 2014). The Law will enter into force once a number of specific regulation (“Reglamento”) are issued.

79. **The control environment for budget support proceeds flow has improved.** A summary of the IMF Safeguards Assessment carried out in 2007 (the latest report) found no significant weaknesses in the Central Bank’s safeguards framework and the updated PEFA highlights the improvements in the internal control environment of the budget process since the last evaluation in 2009. The latest external audit report on the 2013 financial statements of Central Bank did not reveal any significant issue related to the internal control environment; and the IMF latest Article IV Consultation with Peru (concluded on May 20, 2015) noted the Central Bank’s sound management.

80. **The Bank will disburse the loan proceeds into the US dollars Single Treasury Account (Cuenta Única del Tesoro) of the MEF at the Central Bank.** The funds will be available to finance budgeted expenditures and will be fully incorporated into the Borrower’s accounting records and financial statements. The full amount of the loan would be available as a line of credit that can be drawn down subject to satisfactory semiannual review on the maintenance of the program supported and an adequate macroeconomic policy framework in line with OP/BP 8.60.

81. **Given that the control environment into which the DPF-DDO proceeds would flow is adequate, the Bank will not require a dedicated account at the Central Bank for loan proceeds.** As such, no audit will be required for the deposit account.

5.4 MONITORING, EVALUATION AND ACCOUNTABILITY

82. **The Bank will work with MEF and MINEDU to monitor progress of the proposed operation during the course of the program.** For most indicators, monitoring and evaluation will be folded into the National Competitiveness Council regular activities, chaired by the Minister of Economy and Finance. They will be supported by MINEDU for the progress on the indicators of the education reforms. Other ministries and agencies linked to the prior actions and results will monitor and provide budgetary, legislative, and economic data and verify official disclosures, directives, and regulations. The baseline and updated data are provided by the respective specialized agencies and tracked according to the indicators and outcome measures as shown in the policy and results matrix (Annex 1).

83. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, and/or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaints to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given the opportunity to respond. Information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS) can be found at <http://www.worldbank.org/GRS>. Information on how to submit complaints to the World Bank Inspection Panel can be found at visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

84. **This operation entails an overall moderate level of risk.** Reforms are all well entrenched in the institutional framework of the implementing agencies and the performance budgeting framework. Together with continuous World Bank support, this would mitigate risks arising from the forthcoming presidential elections.

85. **Political and governance risks are considered moderate and are associated with election dynamics.** The main internal risk relates to domestic politics (presidential elections April and June, 2nd round) of 2016 and their potential impact on future reforms in these areas. These risks are mitigated as policy continuity is very likely and unrelated to election results, partly because it is entrenched in a technically sound management of the government.

86. **Macroeconomic risks to the results of this operation are considered moderate.** Peru's solid macroeconomic policies and fundamentals allow the government to respond to shocks. The less favorable external environment affects all countries in the LAC region, including Peru. China is also a significant export destination for Peru, and further deterioration of export demand in this country would continue to affect trade balances. While commodities represent 65 percent of total exports, they account for about 13 percent of GDP, and only around 2.3 percent of fiscal revenues in Peru. The climatic phenomenon El Niño may have a strong adverse impact over the next 12 months, particularly affecting the fishery sector and its exports in 2016. Nonetheless, throughout the past period of growth and favorable external conditions, and unlike many countries, Peru saved the commodities windfall, leaving itself with significant savings to continue to afford needed investments and strong macroeconomic buffers. Foreign exchange reserves stood at 32 percent of GDP or 20 months of imports by the end of October 2015. Public debt remained relatively low at 20 percent of GDP and net public debt was 3 percent of GDP in June 2015 (one of the lowest in the world). The Fiscal Stabilization Fund (*Fondo de Estabilización Fiscal*) provides an additional buffer in case of continued negative external shocks (standing at US\$8.6 billion by end 2014 or 4 percent of GDP).

87. **Risks related to institutional capacity for implementation are considered moderate.** While most reforms are well entrenched into Peru's institutional framework, introducing a risk-

based system for technical safety inspections in municipalities, for example, is innovative. It will demand technical capacity and careful follow-up. The World Bank, as well as other key players, will continue to offer technical assistant to help Peru to successfully implement the reform.

88. **Social and environmental risks are considered low.** The specific policies supported by the DPF-DDO are not likely to have significant effects on Peru’s environmental resources and natural habitats. The poverty and social impacts of the supported policy measures are expected to be either positive or poverty-neutral in the short term, and to be positive over the medium term.

89. **Risks related to stakeholders are considered moderate.** The reforms supported are the first installment of a widely backed medium term reform program—the National Competitiveness Plan 2014-18, which has been broadly consulted with all key stakeholders.

90. **All other risks are considered low.**

Table, Systematic Operations Risk-Rating Tool (SORT)

Risk Categories	Rating (H, S, M or L)
1. Political and governance	M
2. Macroeconomic	M
3. Sector strategies and policies	M
4. Technical design of project or program	L
5. Institutional capacity for implementation and Sustainability	M
6. Fiduciary	L
7. Environment and social	L
8. Stakeholders	M
9. Other	L
Overall	M

ANNEX 1: POLICY AND RESULTS MATRIX

DPF Prior Actions	Results
<i>Pillar 1: Enhancing the education policy framework to enable better quality of skills</i>	
Prior Action #1: Increase in the teaching quality of education in economically disadvantaged areas by introducing a balanced and equitable system for recruiting and promoting qualified teachers and principals within the merit-based Teaching Career System [Resolution of the General Secretariat No. 813-2014-MINEDU and Vice-Ministerial Resolution No. 021-2015-MINEDU]	<i>Increase the share of programmed merit-based promotions and appointments for teachers and school principals within the Teaching Career outside Lima and Callao from 60% in 2014 to 75% in 2017. Source: MINEDU</i>
Prior Action #2: Improvement of school graduates' learning outcomes by: (i) introducing an extended school-day model for secondary education that strengthens the teaching of Math, Science, English language, and soft skills [Ministerial Resolution 451-2014-MINEDU]; and (ii) creating performance-based financial incentives for subnational government institutions that manage schools (UGEL and DRE) to improve the learning environment in schools [Ministerial Resolution No. 591-2014-MINEDU]	<i>Increase the number of secondary schools that implement the new school-day model from 0 in 2014 to 1500 in 2017; and include learning outcomes in the stated targets of the performance-based financial incentive mechanism for subnational entities: baseline: 0% in 2014, target: 100% in 2017. Source: MINEDU</i>
Prior Action #3: Creation of the General Directorate for School Infrastructure within the Ministry of Education, to foster the participation of the private sector in school infrastructure upgrading, and to separate the functions of policy formulation and planning from construction [Supreme Decree No. 001-2015-MINEDU]	<i>Increase private sector investment in the construction and/or maintenance of public schools from 0 in 2014 to US\$150 million in 2017. Source: MINEDU</i>
Prior Action #4: Improvement of the framework of university education by creating the National Superintendence of University Education (SUNEDU) and the General Directorate of University Education (DIGESU) within MINEDU to guarantee that university programs and institutions meet quality standards and to lead the implementation of the university reform [Law 30220; Supreme Decree No. 012-2014-MINEDU, Supreme Decree No. 001-2015-MINEDU]	<i>The number of universities and university programs under revision to be licensed increases from 0 in 2014 to 20 in 2017. Source: MINEDU</i>

Pillar 2: Facilitating the entry, operation, and exit of firms

Prior Action #5: Facilitation of business entry of firms by: (i) integrating online registration procedures into the system of public registries under the management of the National Superintendence of Public Registries (SUNARP) [Supreme Decree No. 007-2014-JUS]; (ii) creating financial incentives for large municipalities to deliver operating licenses faster than required by law No. 28976 of February 4, 2007 [Supreme Decree No. 015-2014-EF]; and (iii) introducing a more effective risk-based classification system for technical safety inspections for new firms [Legislative Decree No. 1200]

*Number of new firms incorporated online in the System of Online Registration (Sistema de Intermediación Digital-SID); 0 before October 2014; 5,000 by 2017.
Source: SUNARP*

Prior Action #6: Limit the discretion of all government bodies to impose regulations and administrative procedures outside the national legal framework, by strengthening INDECOPI's power to sanction non-compliance with the legal framework [Law No. 30230 and Legislative Decree No. 1212]

*Number of bureaucratic barriers voluntarily removed from the legal framework by entities of the Public Administration due to an action of INDECOPI; 91 in 2013; 1,000 between 2014 and 2017.
Source: INDECOPI*

Prior action #7: Simplification of the withholding regime for VAT payments to reduce operating costs for firms [Law No. 30230]

*Reduction in the average amount of monthly withholdings (which would increase liquidity for firms) due to the system by US\$70 million from 2014 to 2017.
Source: SUNAT*

Prior action #8: Facilitation of business exit of firms by: (i) introducing electronic auctions for asset foreclosures in order to reduce costs and risks of insolvency [Law No. 30229]; (ii) creating the Registry for Judicial Delinquent Debtors, simplifying the legal framework for insolvency [Law No. 30201]; and (iii) modifying the general law of the insolvency system in terms of quality and registry of administrators and liquidators, simplification of administrative procedures under responsibility of INDECOPI, and the system of offenses and penalties [Legislative Decree No. 1189]

*Increase in the average recovery rate of creditors on insolvencies from 28.5% in 2014 to 36% in 2018.
Source: INDECOPI*

Pillar 3: Reducing transaction costs in trade

<p>Prior action #9: Improvement of the customs regime through: (i) the modernization of the Custom Law by introducing key elements of the revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures of February 3, 2006 and the Bali WTO Trade Facilitation Agreement of November 27, 2014, particularly improving the Authorized Economic Operators (AEO) regime, and adopting a more targeted system of fines [Legislative Decree No. 1235]; and (ii) the elimination of all stamp duties for Customs Declaration reducing transaction costs and in alignment with the Bali WTO Trade Facilitation Agreement [Law No. 30230]</p>	<p><i>The time to import declines by 10% in 2017 compared to 2014.</i> <i>Source: SUNAT</i></p>
<p>Prior action #10: Establishment of the National System for Quality and the National Quality Institute (INACAL) to enhance the systems of accreditation, standardization, and metrology, supporting export competitiveness and access to markets [Law No. 30224]</p>	<p><i>Increase in the number of Conformity Assessment Bodies for products, processes, and management systems by 20% from 2014 to 2017 (baseline: 115 in 2014, target: 140 in 2017).</i> <i>Source: INACAL</i></p>

ANNEX 2: LETTER OF DEVELOPMENT POLICY



PERU

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Despacho
Ministerial

"DECENIO DE LAS PERSONAS CON DISCAPACIDAD EN EL PERÚ"
"AÑO DE LA CONSOLIDACIÓN DEL MAR DE GRAU"

ALONSO SEGURA VASI
MINISTRO

Lima, 12 ENE. 2016

OFICIO N° 042 -2016-EF/10.01

CARTA DE POLITICAS

Señor
Jim Yong Kim
Presidente
Banco Mundial
Av. Álvarez Celedón 185, San Isidro
Lima



Referencia: Programa de Estimulo al Capital Humano y la Productividad

Estimado Señor Kim,

Mediante el presente le manifiesto a usted el compromiso del Gobierno del Presidente Ollanta Humala Tasso, de impulsar medidas de política que permitan el desarrollo y crecimiento del país mediante el incremento de la productividad, basado en la generación del capital humano adecuado que aproveche el conocimiento y tecnologías existentes.

En este marco, se ha venido desarrollando con el Banco Mundial (BM) el "Programa de Estimulo al Capital Humano y la Productividad", el cual incorpora acciones de reforma y compromisos para el año 2015 y comprende una operación bajo la modalidad de desembolso diferido.

A continuación se describe el contexto internacional y el contexto económico del Perú y posteriormente los objetivos del Programa, así como las acciones realizadas en el marco del Programa.

A. Contexto Internacional¹

Los indicadores de la **economía mundial** muestran señales mixtas de recuperación, acompañados de alta volatilidad en los mercados financieros internacionales. Las economías avanzadas como EE.UU. y Zona Euro continúan expandiéndose moderadamente, mientras que las economías emergentes como China y América Latina presentan resultados desalentadores. El PMI² manufacturero global registró 50,9 puntos en diciembre, ligeramente por debajo de noviembre (51,2 puntos) y del promedio julio-noviembre 2015 (51,0 puntos). Las expectativas de crecimiento global están a la baja. En octubre pasado, el Fondo Monetario Internacional (FMI) recortó su proyección de crecimiento mundial para el 2015 a 3,1% (vs. 3,5% esperado en enero 2015), la tasa más baja en seis años, y para el 2016 estima una recuperación de 3,6%.

¹ Información al 04 de enero 2016.

² Índice de Gestores de Compras, se elabora mensualmente, a través de encuestas realizadas a los encargados de registrar las adquisiciones de materias primas de empresas privadas. Mayor a 50 puntos significa expansión.



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En EE.UU., el crecimiento del PBI se moderó de 3,9% en el 2T2015 a 2,0%³ en el 3T2015. Este menor dinamismo, se debe a la contribución negativa de los inventarios privados (-0,59 puntos porcentuales-p.p.), las exportaciones netas (-0,22 p.p.) y la inversión privada (-0,05 p.p.). Sin embargo, el gasto de consumo personal se mantuvo sólido (+2,05 p.p.), en un contexto en el que la tasa de desempleo oficial (U3) y aquella que considera una definición de desempleo más amplia (U6) han alcanzado tasas mínimas desde febrero y mayo 2008 de 5,0% y 9,9% en noviembre 2015, respectivamente. Debido lo anterior, en su reunión del 15-16 de diciembre 2015, la FED elevó la tasa de interés por primera vez en casi una década desde un nivel cercano a cero a un rango entre 0,25% y 0,50%.

La economía de la Zona Euro creció 1,5% en los tres primeros trimestres del 2015, la mayor tasa desde el 2011, mostrándose una recuperación en el empleo y la manufactura, pero que aún se encuentra débil respecto al nivel pre-crisis. La tasa de desempleo se ubicó en 10,7% en octubre, la menor tasa desde noviembre 2011. El PMI manufacturero se elevó a 53,2 puntos en diciembre, el mayor registro en 21 meses. Sin embargo, el índice de precios al consumidor registró una tasa anual de 0,1% en noviembre, muy por debajo de la meta de inflación del Banco Central Europeo-BCE (2,0%). Tomando esto en cuenta, el BCE, en su última reunión de diciembre, redujo su tasa de depósitos en 10 puntos básicos de -0,20% a -0,30% y extendió el plazo de su programa de compra de bonos de € 60 mil millones mensuales hasta marzo 2017 (fecha límite anterior era septiembre de 2016). En octubre, el FMI proyectó un crecimiento de la Zona Euro para el 2015 de 1,5%, superior al registrado en el 2014 (0,9%) y para el 2016 de 1,6%.

En China, la información más reciente confirma un menor dinamismo económico: si bien la economía China creció 7,0% en los tres primeros trimestres del 2015, el sector industrial y construcción -motor de la actividad económica e intensiva en el uso de materias primas- registró un crecimiento solo de 6,2%. Por su parte, los indicadores adelantados muestran que la desaceleración continuaría en los próximos meses: (i) el PMI manufacturero oficial se ubicó por quinto mes consecutivo en zona de contracción, registrando 49,7 puntos en diciembre y (ii) las exportaciones chinas cayeron por quinto mes consecutivo, registrando una caída de -6,8% en noviembre.

Con información al 31 de diciembre, la bolsa de Shanghai ha disminuido -31,5%, desde su nivel "picc" (12 de junio del 2015), luego de subir 135% desde agosto del año anterior. Esto ha generado fuertes dudas sobre la estabilidad del mercado bursátil y preocupaciones sobre el sistema financiero en general. En octubre, el FMI proyectó un crecimiento de China para el 2015 de 6,8%, inferior al registrado en el 2014 (7,3%) y para el 2016 de 6,3%. En este contexto, el gobierno chino, en su décimo tercer plan quinquenal, estableció metas agresivas para el desarrollo y sostener su crecimiento en torno al 6,5%⁴ para los próximos 5 años.

Los países de América Latina y el Caribe continúan mostrando signos de desaceleración económica, en un contexto de menores precios de materias primas, aumento de percepción de riesgo, incremento de costos de financiamiento y salidas de capitales. En el 3T2015, Brasil profundizó su recesión de -4,5%, acumulando seis

³ Tercer estimado oficial para el 3T2015

⁴ Entre las metas: duplicar el PBI y los ingresos residenciales para el 2020, la eliminación de la pobreza y el abandono de la política de un solo hijo.



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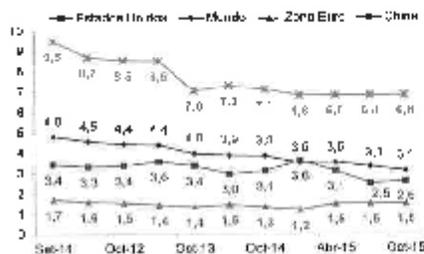
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trimestres de caídas consecutivas; Chile creció 2,2%, igual al registro del 1S2015; México avanzó 2,6%, acelerando ligeramente respecto al 1S -0,1%; Uruguay avanzó apenas 0,6%, luego de registrar su primera contracción en doce años en el trimestre previo (-0,3%), y el PBI de Colombia registró un crecimiento de 3,2%, inferior al 3T2014 (4,2%). En el caso particular de Brasil, dada la contracción económica, la inestabilidad política la baja perspectiva de crecimiento y el elevado déficit fiscal, las agencias calificadoras de riesgo redujeron el rating crediticio soberano, quitándole Standard & Poor's y Fitch la calificación de grado de inversión el 09 de setiembre y el 16 de diciembre de 2015, respectivamente⁵. En octubre, el FMI proyectó para el 2015 una contracción económica para América Latina y el Caribe en -0,3%, la primera caída desde el 2009, y para el 2016 un crecimiento de 0,8%.

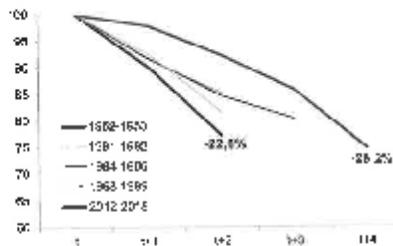
En línea con la menor demanda externa china y la preferencia de los inversionistas por otros activos financieros, las cotizaciones de materias primas cayeron fuertemente, siguiendo su tendencia a la baja desde el año 2011. Cabe destacar, la caída de precios de metales, que enfrenta la economía peruana, es la más larga y profunda de los últimos 65 años. Así, en el 2015⁶, el precio del cobre cayó -19,8%, oro -8,3% y petróleo WTI -47,6%.

Mundo: Proyecciones de crecimiento 2015 del Fondo Monetario Internacional (Var. % anual)



IA6: Brasil, Chile, Colombia, México, Uruguay y Perú.
Fuente: FMI, BCRP.

Episodios de caídas consecutivas del IPX (Índice: Año previo a los episodios de caída=100)



B. Contexto Económico Nacional

La economía peruana creció 2,6% en el periodo enero-octubre 2015; cifra ligeramente superior a lo registrado en el 2014 (2,4%), que estuvo afectado por un escenario internacional complejo y choques de oferta transitorios. Este resultado se sustenta en el mayor avance de los sectores primarios (4,2%) respecto a los sectores no primarios (2,5%).

⁵ El 11 de agosto 2014, Moody's reculó la calificación de deuda en moneda extranjera en una escala de "Baa2" a "Baa3" con perspectiva estable, a un paso de perder la calificación crediticia; y el 09 de diciembre puso esta calificación en revisión. El 9 de setiembre 2015, Standard & Poor's redujo en una escala, de BBB- a BB+, a "grado especulativo" y con perspectiva negativa. El 16 de diciembre 2015, Fitch redujo en una escala a "BB+" pasando a "grado especulativo" y con perspectiva negativa.

⁶ Respecto al 2014.



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- A nivel sectorial, el PBI creció 3,0% en octubre, impulsado por los sectores primarios que en conjunto crecieron 7,0%, la mayor tasa en 6 meses, se destaca el resultado favorable de la minería metálica que volvió a crecer a dos dígitos (15,9%), registrando 8 meses de crecimiento continuo y ratifica el inicio del ciclo de producción minera (cuprífera). Por su parte, los sectores no primarios se expandieron 2,4%, favorecidos por el crecimiento estable de los sectores vinculados al consumo privado (comercio y servicios).
- Cabe indicar que los últimos indicadores dan señales que la recuperación continuará en los próximos meses:
 - De acuerdo al COES⁷, la producción de electricidad creció alrededor de 11,8% en diciembre, el mayor crecimiento en 65 meses. Por el lado de la demanda, la demanda por electricidad de oficinas libres creció 36,6% (empresas mineras 49,5% y empresas manufactureras 13,3%); mientras que el resto de oficios creció 2,4%.
 - Se reduce la probabilidad de un FEN fuerte en el verano 2016. De acuerdo al último comunicado del ENFEN⁸, la probabilidad de que el FEN sea extraordinario (tal cual el FEN 97-98) se mantiene en sólo 5%, la probabilidad de un fenómeno fuerte se redujo a 35% y la probabilidad de un FEN moderado se incrementó a 59%.
 - Según IMARPE, para diciembre, se espera un desembarque de anchoveta de 550 mil TM; que impulsaría el crecimiento del sector fuertemente, dado que el año pasado el nivel de desembarque fue nulo. Al tener en cuenta el desembarque de noviembre, el monto acumulado alcanzaría el 76% de la cuota autorizada (1,11 millones de TM).
 - Según datos de Ferupetro, en diciembre, hidrocarburos caería -5,6%, la menor contracción en 6 meses. El resultado se explica por la menor producción de petróleo que cayó alrededor de -11,8%, por el menor precio internacional del crudo, y LGN -4,8%, la mejor tasa en 6 meses. Por su parte, la producción de Gas Natural creció 1,8%, acumulando tres meses consecutivos de crecimiento continuo.
 - En diciembre 2015, el índice de avance físico de obras registró una caída de -3,7%, la menor caída del año, y por debajo de lo registrado durante enero-noviembre 2015: -19,5%.
 - Según el BCRP, en noviembre, el crédito en soles creció 29,2%. Por otro lado, el crédito en dólares cayó -19,4%, con lo que registra tasas negativas por onceavo mes consecutivo; ante, la caída de créditos a empresas (-19,6%) y familias (-19,5%). El menor avance de los créditos en dólares ha permitido reducir la dolarización de los créditos a 30,8%, -9,7 puntos porcentuales desde inicios del 2014.
 - De acuerdo al INEI, en el trimestre móvil septiembre-noviembre 2015, el empleo en Lima Metropolitana creció 2,2% (vs. 1,8% previo), el mayor registro en 21 períodos. Sin embargo, el empleo asalariado se desaceleró a 0,7% anual (vs. 2,5% previo), la más baja en los últimos cuatro registros. Por su parte, la tasa de

⁷ Comité de Operación Económica del Sistema Interconectado Nacional

⁸ 17 de diciembre.

⁹ Cifras preliminares. Considere estimación de anulaciones de S/ 400 millones.

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desempleo (5,8%) se mantuvo sin cambios respecto al trimestre móvil previo. Respecto al ingreso laboral, este aumentó 4,2%, superior al previo (2,3%) y al promedio de los tres registros anteriores (1,9%).

- o Según el Ministerio de Trabajo y Promoción del Empleo, en octubre 2015, el empleo en empresas de 10 a más trabajadores del ámbito urbano creció 1,4%, su mayor avance en 10 meses. Esta mayor tasa se debe al desenvolvimiento positivo de cuatro de las cinco ramas de actividad económica: transportes, almacenamiento y comunicaciones (4,3%), servicios (2,1%), seguida por, comercio (1,8%) y extractiva (1,2%). Sin embargo, el empleo en la industria manufacturera continúa en terreno negativo (-1,1%) desde hace casi dos años.
- o Sin embargo, aún persiste el deterioro del sector externo debido a la mayor desaceleración de China, LATAM, la Zona Euro, y la caída en los precios internacionales de los metales. Según SUNAT, en noviembre, las exportaciones totales cayeron -14,2%. Este resultado se explicó por la contracción de los precios de exportación (-14,7%), mientras que el volumen creció ligeramente (0,6%). Las exportaciones tradicionales disminuyeron -16,3%, principalmente por menores envíos de productos mineros (-9,7%) como oro (-18,3%), cobre (-7,8%) y zinc (-6,8%). Las exportaciones no tradicionales disminuyeron -10,0% (décima caída consecutiva), ante menores envíos de productos pesqueros (-29,9%), textiles (-25,7%), metal-mecánico (-24,3%), sidero-metalúrgicos (-21,6%) y químicos (-10,2%).
- c Asimismo, según SUNAT, en noviembre, las importaciones de bienes de consumo cayeron -1,4% (segunda caída consecutiva). Este registro negativo se explica principalmente por menores importaciones de bienes duraderos (-6,0%, registra 3 meses de caída consecutiva).

Así, esperamos que la economía crezca alrededor de 3,0% en el 2015 de acuerdo al MIMMR 2016-2018. Según el consenso de mercado, en el 2015, la economía peruana será una de las economías que acelere su ritmo de expansión respecto del 2014. Según el último sondeo de Consensus Forecasts (CF) de diciembre, Perú se aceleraría en 0,4 p.p., de 2,4% en el 2014 a 2,8% en el 2015, seguido por Chile (0,2 p.p., de 1,9% en el 2014 a 2,1%) y México (0,1 p.p., de 2,3% en el 2014 a 2,4%). Caso contrario, Colombia se desaceleraría en -1,7 p.p., de 4,6% en el 2014 a 2,9% en el 2015.

Para el 2016, la proyección de crecimiento del PBI se acelerará a 4,3% sustentado en:

- Una política fiscal moderadamente expansiva, adoptada de forma preventiva a través del Decreto de Urgencia 003-2015, que contempla fortalecer la respuesta del Estado frente al Fenómeno de El Niño, así como maximizar su efecto multiplicador sobre la actividad económica, a través de una mayor inversión pública.
- Incremento significativo en la inversión en infraestructura de envergadura mediante la modalidad de Asociaciones Público Privadas (APP).
- Mayor crecimiento de la minería metálica dado el inicio de la producción de Las Bambas y la Ampliación de Cerro Verde, la mayor producción de proyectos como Toromocho y Constancia, así como por la recuperación de la producción de Antamina.
- Mayor crecimiento esperado de los principales socios comerciales, en especial, de América Latina y el Caribe y EE.UU., que impulsarán la demanda por las exportaciones no tradicionales, las cuales se expandirían 6,7% (2015: -2,3%)¹⁶.

¹⁶ Otras reportadas en el Marco Macroeconómico Multianual 2016-2018 Revisado



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MINISTRO**OFICIO N° 042 -2010-EF/10.01****C. Reformas asociadas al Programa de Estímulo al Capital Humano y la Productividad**

El Gobierno Peruano es consciente que el país tiene retos importantes que enfrentar para reducir brechas de productividad y mejorar su competitividad, principalmente relacionados con la debilidad de la oferta laboral, gestión empresarial, y acceso a mercados.

En el marco de lo anterior, el Gobierno Peruano, con el apoyo del Banco Mundial, ha desarrollado el Programa de Estímulo al Capital Humano y la Productividad (el "Programa"), con el cual se busca apoyar al Gobierno de Perú en sus esfuerzos por impulsar y dar sostenibilidad a las medidas de política que promuevan el desarrollo del capital humano y refuercen las habilidades de la fuerza laboral, así como aquellas que fortalezcan el rol de los mercados y de la competencia a nivel doméstico e internacional.

El Programa apoya la adopción de reformas de política, las cuales están estructuradas en tres pilares: i) Fortalecimiento del marco de política educativa para facilitar una mejor calidad de habilidades; ii) Facilitación de la entrada, operación y disolución de empresas; y iii) Reducción de costos de transacción del comercio internacional.

C.1 Fortalecimiento del marco de política educativa para facilitar una mejor calidad de habilidades

El Gobierno es consciente de que la acumulación de capital humano es un proceso crucial para el crecimiento económico y la competitividad. No obstante, el país tiene el reto de mejorar los indicadores mostrados por las evaluaciones nacionales e internacionales de la calidad educativa a nivel primaria y secundaria. Asimismo, a nivel de educación terciaria, si bien se cuenta con más de tres mil centros de educación superior y técnico-productiva a nivel nacional, de las cuales más de cien de ellas son universidades, todavía no se considera que se haya alcanzado el potencial requerido en términos de calidad para generar empleos adecuados.

En línea con lo anterior, mediante el primer pilar, el Programa contempla el incremento de la calidad de la educación en regiones en desventaja, el reforzamiento de las habilidades de estudiantes escolares, el cierre de la brecha en instalaciones de aprendizaje, y la mejora de la educación universitaria.

En relación a la educación en regiones, el Programa incorpora la introducción de un sistema más balanceado y equitativo para reclutar y promover profesores y directores calificados en el marco de la Reforma de la Carrera Magisterial.

Asimismo, se espera lograr un reforzamiento de las habilidades de los estudiantes escolares, mediante la introducción de la Jornada Escolar



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Completa, con la cual se refuerza la enseñanza de matemáticas, ciencias, inglés y habilidades blandas, y la creación de un sistema de incentivos financieros basados en el desempeño para que las instituciones subnacionales independientes que administran las escuelas (UGEL y DRE) mejoren el ambiente de aprendizaje.

Adicionalmente, el Programa contempla la creación de la Dirección General de Infraestructura Educativa del Ministerio de Educación, con la cual se separa la función de formulación de políticas y la planificación de necesidades de infraestructura de la función de ejecución.

Finalmente, con el objetivo de mejorar la educación universitaria se ha creado la Superintendencia Nacional de Educación Universitaria (SUNEDU) y la Dirección General de Educación Superior Universitaria (DIGESU). De esta manera, se espera garantizar que las universidades y sus programas logren estándares de calidad y, con ello, se logren avances en la implementación de la reforma universitaria.

C.2 Facilitación de la entrada, operación y disolución de empresas

No obstante la estabilidad económica del país, se requiere tomar acciones para facilitar la creación, la operación y el cierre de las empresas. Según el índice de Competitividad Global medido por el Foro Económico Mundial 2014-2015, el Perú se encuentra en el puesto 65 de un total de 144 países, lo cual revela que existen muchas barreras de tipo burocráticas y operativas para la dinamización de los negocios.

Asimismo, el Ministerio de Economía y Finanzas (MEF) ha preparado la nueva Agenda de Competitividad para el período 2014-2018, la cual incorpora metas a corto plazo para la facilitación de negocios, cuyo objetivo es mejorar los procesos y procedimientos vinculados al inicio, operación y cierre de empresas.

En este sentido, con el presente pilar se apoya la facilitación de la creación de empresas, así como la reducción de costos de operación necesarios para promover el crecimiento de dichas empresas, y la facilitación del cierre de empresas con lo cual se facilita que esos recursos sean reasignados más rápidamente en actividades más productivas para la economía.

Para tales efectos, el Programa incorpora la integración de los procedimientos de registro para la constitución de empresas en línea mediante el establecimiento de dicho sistema a cargo de Superintendencia Nacional de Registros Públicos (SUNARP), el cual se espera llegue a operar a nivel nacional. Asimismo, se incluye la creación de incentivos financieros para que los municipios más grandes entreguen licencias de funcionamiento en menores plazos de los requeridos en el marco legal. Adicionalmente, el Programa incluye la implementación de un régimen más efectivo para las inspecciones técnicas de seguridad a través de un sistema de clasificación basado en el riesgo de las nuevas empresas.



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Asimismo, el Programa incorpora el fortalecimiento del Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual (INDECOP) para sancionar el incumplimiento del marco legal por parte de las entidades públicas, con lo cual se espera lograr una reducción de la discrecionalidad de diversas entidades para imponer reglamentos y procedimientos administrativos fuera del marco jurídico nacional.

En relación a la reducción del costo de operación de las empresas, el Programa comprende la simplificación del régimen de percepciones a los pagos del IGV por parte de las empresas. Asimismo, se incluyen mecanismos que faciliten la disolución de empresas, tales como las subastas electrónicas para embargos de activos a fin de reducir costos y riesgos de insolvencia, la creación del Registro Judicial de Deudores Micros que simplifica el marco jurídico de la insolvencia, y la modificación de la Ley General del Sistema Concursal para mejorar la calidad y registro de administradores y liquidadores, la simplificación de procedimientos administrativos bajo responsabilidad de INDECOP) y mejora del sistema de infracciones y sanciones.

C.3 Reducción de costos de transacción del comercio internacional

Desde el punto de vista del comercio internacional, por medio de la Agenda de Competitividad 2014-2018, el Gobierno viene impulsando el acceso de las empresas a los mercados internacionales mediante la facilitación del comercio y el desarrollo de estándares y certificaciones que permitan obtener productos y servicios competitivos, así como el desarrollo de mercados sostenibles, entre otros.

En línea con lo anterior, el Programa incluye medidas vinculadas a la mejora del régimen de aduanas, el apoyo a la competitividad de las exportaciones y el acceso a los mercados.

En relación al régimen de aduanas, el Programa incorpora la modernización de la Ley de Aduanas, en el cual se incluyen elementos del Convenio Revisado de Kioto y el Tratado de Bali, específicamente en aspectos relacionados con el régimen de Operadores Económicos Autorizados (OEA) y la adopción de un sistema de multas más efectivo. Adicionalmente, se incorpora la eliminación de la Tasa de Despacho Aduanero para la declaración de aduanas, reduciendo los costos de transacción en concordancia con el Acuerdo de Bali de la OMC para Facilitación del Comercio.

Adicionalmente, para reforzar la competitividad de las exportaciones, el Programa considera la creación del Sistema Nacional para la Calidad y del Instituto Nacional de Calidad, con lo cual se fortalecen los sistemas de acreditación, normalización y metrología.



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D. Conclusión

Como se desprende de lo descrito, el Gobierno Peruano está comprometido en sentar las bases para lograr mejorar el capital humano y promover la productividad en el país, considerando las diversas etapas de formación de la oferta laboral y el desarrollo empresarial, facilitando su gestión e incrementando la calidad productiva.

El Gobierno se compromete a continuar avanzando en estos ámbitos, para lo cual requiere contar con el apoyo del Banco Mundial en las áreas señaladas.

En virtud de lo manifestado, por medio de la presente el Gobierno Peruano solicita la aprobación del "Programa de Estimulo al Capital Humano y la Productividad" por un monto de US\$ 1 250 millones por parte del Banco Mundial, bajo la modalidad de desembolso diferido.

Sin otro particular, hago propicia la ocasión para reiterarle a usted mi especial consideración.

Atentamente,

Unofficial Translation:

Mr.

Jim Yong Kim

President

World Bank

Av. Álvarez Calderón 185, San Isidro

Lima

Reference: *Boosting Human Capital and Productivity Program*

Dear Mr. Kim,

By means of this letter I wish to convey to you the commitment of the Government of President Ollanta Humala Tasso to promote policy measures that will permit the country's development and growth by increasing productivity, based on the generation of the necessary human capital to tap existing knowledge and technology.

In this context, Peru has been developing with the World Bank the "Boosting Human Capital and Productivity Program," which includes reform actions and commitments for 2015 and involves an operation with a deferred drawdown option.

Below we will describe the international context and Peru's economic context, then the program's objectives, as well as the actions accomplished in the framework of the program.

A. **International context¹**

*Indicators of the **global economy** show mixed signs of recovery, accompanied by high volatility in the international financial markets. The advanced economies such as the United States and the Euro Zone continue to expand moderately, while emerging economies such as China and Latin America show discouraging results. The PMI² of global manufacturing was 50.9 points in December, slightly below November (51.2 points) and the average for July-November 2015 (51.0 points). Expectations are for global growth to decline. In October the International Monetary Fund (IMF) lowered its world growth projection for 2015 to 3.1% (vs. 3.5% expected in January 2015), the lowest rate in six years, and for 2016 recovery is expected to be to 3.6%.*

*In the **United States**, GDP growth declined from 3.9% in the second quarter of 2015 to 2.0%³ in the third quarter of 2015. This sluggishness is due to the negative impact of private inventories (-0.59 percentage points), net exports (-0.22 percentage points) and private investment (-0.05 percentage point). Nevertheless, personal consumer spending remained strong (+2.05 percentage points), in a context in which the official unemployment rate (U3) and the rate that uses a broader definition of unemployment (U6) have been the lowest since February and May 2008, at 5.0% and 9.9% in November 2015, respectively. In view of the foregoing, at its meeting of December 15-16, the FED raised the interest level for the first time in a decade, from a near-zero level to a range of between 0.25% and 0.50%.*

¹ Information as of January 4, 2016.

based on surveys of the persons in charge of procurement of raw materials for private companies. Greater than 50 points shows expansion.

³ Third official estimate for third quarter or 2015

The **Euro Zone** economy grew by 1.5% in the first three quarters of 2015, the most robust growth since 2011, showing recovery in employment and manufacture, although this growth was still weak relative to the pre-crisis level. The unemployment rate was 10.7% in October, the lowest rate since November 2011. The manufacturing PMI grew to 53.2 points in December, the highest recorded performance in twenty-one months. However, the consumer price index registered an annual rate of 0.1% in November, well below the inflation target of the European Central Bank (ECB) (2.0%). Taking this into account, at the ECB's last meeting in December, it reduced its deposit rate by ten basis points from -0.20% to -0.30% and extended the deadline for the monthly 60 billion Euro bond purchase program until March 2017 (the previous deadline had been set at September 2016). In October, the IMF forecast economic growth of the Euro Zone for 2015 at 1.5%, higher than that recorded in 2014 (0.9%), and for 2016 it forecast 1.6%.

In **China**, the latest information confirms slower economic growth: although China's economy grew by 7.0% in the first three quarters of 2015, the industrial and construction sector—the engine of economic activity and an intensive user of raw materials—grew by only 6.2%. The forward indicators show that the slowdown will continue in the upcoming months: (i) the official manufacturing PMI was contracting for the fifth consecutive month, at 49.7 points in December and (ii) Chinese exports fell for the fifth straight month, with a drop of -6.8% in November.

Based on information as of December 31, the Shanghai stock market declined by -31.5% from its “peak” (June 12, 2015), after surging ahead by 135% since August of the previous year. This has triggered serious doubts about the stability of the stock market and worries about the financial system in general. In October the IMF predicted that in 2015 China would have economic growth of 6.8%, lower than that recorded in 2014 (7.3%), and for 2016 it forecast 6.3%. In this context, the Chinese Government's thirteenth five-year plan set aggressive development targets with growth of 6.5%¹ for the next five years.

The countries of **Latin America and the Caribbean** continue to show signs of economic deceleration, in a context of lower prices for raw materials, increased perception of risk, higher financing costs, and capital flight. In the third quarter of 2015, Brazil sank deeper into recession by -4.5%, accumulating six consecutive quarters of decline; Chile grew by 2.2%, similar to the rate posted during the first semester of 2015; Mexico grew by 2.6%, slightly better than the first half of 2015 (0.1%); Uruguay saw growth of merely 0.6% after the economy registered its first contraction in 12 years during the previous quarter (-.3%); and Colombia's GDP grew by 3.2%, lower than that of the third quarter of 2014 (4.2%). In the particular case of Brazil, given the economic contraction, political instability, the low prospects for economic growth, and the high fiscal deficit, rating agencies downgraded the country's sovereign credit rating, and Standard & Poor's and Fitch removed its investment grade rating on September 9 and December 15, 2015, respectively.² In October, the IMF predicted that for 2015 Latin America and the Caribbean will have an economic contraction of -0.3%, the first decline since 2009, and it forecast growth of 0.8% for 2016.

Owing to reduced Chinese external demand and investors' preference for other financial assets, the prices of **raw materials** fell significantly, continuing their downward trend since 2011. It should be noted that the slump in metal prices, which affects Peru's economy, is the longest and deepest in the past 65 years. In 2015³, the copper price fell -19.8%, gold fell -8.3%, and petroleum WTI fell -47.6%.

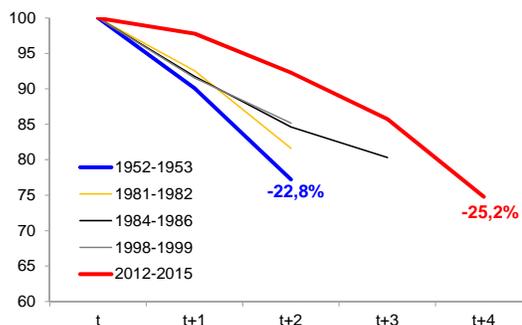
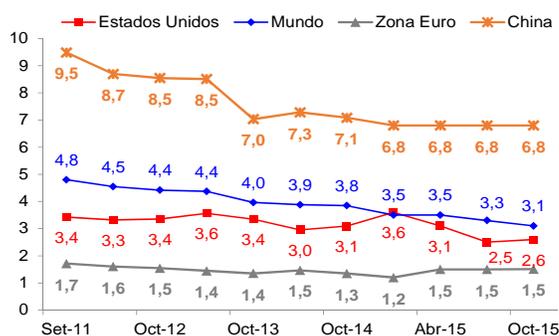
World: Growth Projections for 2015 by the International Monetary Fund (% of annual variation)

Episodes of Consecutive Declines in the IPX (Index: Year before the decline episodes =100)

¹ The goals include: doubling the GDP and residential income for the year 2020, poverty elimination and doing away with the one child policy.

² On August 11, 2015, Moody's dropped the foreign currency debt rating from “Baa2” to “Baa3” with a stable outlook, one step from losing the credit rating, and revised the rating on December 9. On September 9, 2015, Standard & Poor's reduced its rating from BBB- a BB+, a “speculative grade,” with a negative outlook. On December 16, 2015, Fitch lowered its rating to “BB+”, a speculative grade with a negative outlook.

³ With respect to 2014.



LA6: Brazil, Chile, Colombia, Mexico, Uruguay and Peru.
Source: IMF, BCRP.

B. National economic context

Peru's economy grew by 2.6% in the period January-October 2015, a figure slightly above that recorded in 2014 (2.4%), which was affected by a complex international scenario and temporary supply shocks. This result can be attributed to greater growth in the primary sectors (4.2%) over and above the non-primary sectors (2.5%).

- At the sector level, GDP grew by 3.0% in October, driven by primary sectors that together grew by 7.0%, the highest in six months, with the metal mining sector experiencing double-digit growth (15.9%), recording eight months of uninterrupted growth and reflecting the start of the (copper) mining production cycle. Non-primary sectors grew by 2.4%, boosted by the stable growth of the sectors related to private consumption (business and services).
- The latest indicators show signs that the recovery will continue in the coming months:
 - According to the COES,¹ electric power production increased by about 11.8% in December, the highest gain in 65 months. On the demand side, demand by free clients for electric power grew 36.6% (mining companies 49.5% and manufacturing companies 13.3%); while the number of remaining clients grew by 2.4%
 - A strong El Niño phenomenon (FEN) in the summer of 2016 is less likely. According to the latest forecast by the ENFEN² (National Committee for the study of the El Niño phenomenon), there is only a 5% probability of an FEN of extraordinary strength (like that of 97-98) and the likelihood of a strong phenomenon was reduced by 35%, while the probability of a moderate El Niño phenomenon increased to 50%.
 - According to IMARPE, anchovy landings are projected to reach 550,000 MT in December; this should significantly boost the growth of the sector, especially since there were zero landings last year. Taking into account landing figures for November, the accumulated amount should be 76% of the authorized quota (1.11 million MT).
 - According to data from Perupetro, production of hydrocarbons fell -5.6% in December, the least significant reduction in six months. This is due to a fall in oil production of around -11.8% and the drop in the international price of crude and LNG (-4.8%), the most favorable rate in six months. Production of Natural Gas grew 1.8%, amounting to three consecutive months of continuous growth
 - In December 2015, the figure for the progress of implementation of public works was -3.7%³, the smallest decline for the year, and lower than the rate recorded for January- November 2015: -19.6%.
 - According to the BCRP, in November, credit in soles grew 29.2%. However, credit in dollars declined -19.4%, recording negative rates for the eleventh straight month, due to the reduction of credits to

¹ Committee on Economic Operation of the Interconnected National System

² December 17

³ Preliminary Figures. Includes estimates of cancellations in the amount of 400 million soles

- businesses (-19.6%) and to families (-19.5%). The lower advance in dollar credits has made it possible to reduce the dollar portion of the loans to 30.8%, -9.7 percentage points since the start of 2014.
- According to the INEI, in the September-November 2015 moving quarter, employment in Greater Lima grew by 2.2% (vs. 1.8% in the previous period), the most significant increase in 21 periods. However, salaried employment fell to 0.7% on an annualized basis (as against 2.5% for the previous period) the lowest rate for the last four recorded periods. The unemployment rate (5.8%) remained unchanged with respect to the previous moving quarter. Wage income increased by 4.2%, higher than the previous period (2.3%) and the average rate of the three previous periods (1.9%).
 - According to the Ministry of Labor and Promotion of Employment, in October 2015 employment in companies with 10 or more workers in the urban area grew by 1.4%, the biggest advance in ten months. This result is due to the positive performance of four of the five areas of economic activity: transport, storage, and communications (4.3%), services (2.1%), followed by trade (1.6%) and the extractive industries (1.2%). However, employment in the manufacturing industry has been in negative territory (-1.1%) for the last two years.
 - However, deterioration in the external sector persisted owing to the greater deceleration in China, Latin America, the Euro Zone, and the slump in international metal prices. According to SUNAT, total exports in November declined by -14.2%. This result is explained by the contraction of export prices (-14.7%), while the volume of exports increased slightly (0.6%). Traditional exports decreased by -16.3%, mainly because of smaller shipments of mining products (-9.7%) such as gold (-18.3%), copper (-7.8%), and zinc (-6.8%). Non-traditional exports declined by -10.0% (the tenth consecutive decline), because of smaller shipments of fishing products (-29.9%), textiles (-25.7%), metal-mechanics (-24.3%), iron and steel (-21.6%) and chemicals (-10.2%).
 - Furthermore, according to the SUNAT, imports of consumer goods in November decreased by -1.4%, (second consecutive decline). This negative performance is explained mainly by smaller imports of durable goods (-8.0%, with three consecutive months of decline).

We therefore expect the economy to grow by about 3.0% in 2015, according to the MMR 2016-2018. The market consensus is that in 2015 Peru's economy will do better than in 2014. According to the latest survey of Consensus Forecasts (CF) in December, Peru's economy will grow by 0.4%, from 2.4% in 2014 to 2.8% in 2015, followed by Chile (0.2%, from 1.9% in 2014 to 2.1%) and Mexico (0.1%, from 2.3% in 2014 to 2.4%). In the other direction, Colombia would decelerate by -1.7%, from 4.6% in 2014 to 2.9% in 2015.

For 2016, GDP growth is projected to accelerate to 4.3% based on:

- A moderately expansive fiscal policy, adopted as a precautionary measure through Emergency Decree 003-2015, which provides for strengthening the Government's response to the El Niño phenomenon and maximizing its multiplier effect on economic activity through increased public investment.
- Substantially increased investment in large-scale infrastructure through public-private partnerships (PPPs).
- Greater growth in metallic mining given the start of production at Las Bambas and the expansion of Cerro Verde, the greater production of projects such as Toromocho and Constancia, as well as resumption of production at Antamina.
- Greater growth expected among the principal trading partners, particularly in Latin America and the Caribbean, and the United States, which will stimulate demand for non-traditional exports, which are projected to expand by 6.7% (2015: -2.3%).¹

C. **Reforms associated with the Boosting Human Capital and Productivity Program**

The Peruvian Government is aware that the country faces major challenges to reduce the gaps in productivity and improve its competitiveness, especially related to weak labor supply, entrepreneurial management, and market access.

¹ Figures reported in the Multiannual Macroeconomic Framework 2016-2018 Revised.

In this context, the Peruvian Government, with the World Bank's support, has developed the Boosting Human Capital and Productivity Program (the "Program"), which seeks to support the Government of Peru in its efforts to implement and ensure the sustainability of policy measures that promote the development of human capital and strengthen the skills of the labor force, as well as measures that strengthen the role of markets and competition at the domestic and international levels.

The Program supports the adoption of policy reforms that are structured in three pillars: (i) Enhancing the education policy framework to facilitate higher quality skills; (ii) Facilitating the entry, operation, and exit of firms; and (iii) Reducing transaction costs in international trade.

C.1 *Enhancing the education policy framework to facilitate higher quality skills*

The Government is aware that the accumulation of human capital is a critical process for economic growth and competitiveness. However, the country has the challenge of improving the indicators shown by national and international evaluations of educational quality at the primary and secondary levels. With respect to higher education, although the country has more than 3,000 institutions of higher learning and technical-productive education, of which more than 100 are universities, the country has not yet achieved the potential required in terms of quality to generate adequate jobs.

In this regard, through the first pillar the Program will seek to upgrade the quality of education in disadvantaged regions, strengthen students' skills, close the gap in educational institutions, and improve university education.

With respect to education in the regions, the Program incorporates the introduction of a more balanced and equitable system to recruit and promote qualified teachers and principals in the framework of the Reform of the Teaching Profession.

We plan to improve students' skills by introducing an extended school-day model for secondary education that strengthens the teaching of Math, Science, English, and soft skills, and creating performance-based financial incentives for subnational government institutions that manage schools (UGEL and DRE) to improve the learning environment in schools.

We also plan to create the General Directorate for School Infrastructure within the Ministry of Education to separate the functions of policy formulation and planning from construction.

Finally, to improve university education we have created the National Superintendency of University Education (SUNEDU) and the General Directorate of University Education (DIGESU). This is to guarantee that university programs and institutions meet quality standards and thus ensure progress in the implementation of university reform.

C.2 *Facilitating the entry, operation, and exit of firms*

Despite the economic stability of the country, it is necessary to take actions to facilitate the creation, operation and exit of companies. According to the Global Competitiveness Index 2014-2015, measured by the World Economic Forum, Peru ranks 65th out of a total of 144 countries, revealing that there are many bureaucratic and operational barriers that block the dynamism of businesses.

The Ministry of Economy and Finance (MEF) has prepared the new Competitiveness Agenda for the period 2014-2018, which includes short-term business facilitation goals, aimed at improving the processes and procedures related to the startup, operation, and closure of companies.

In this sense, this pillar supports the creation of companies, as well as the reduction in operating costs, which will promote their growth, and the facilitation of business closure, which will enable resources to be reallocated faster into more productive activities.

To this end, the Program incorporates the integration of online registration procedures for the incorporation of companies through the establishment of this system managed by the National Superintendency of Public Registries (SUNARP), which is expected to operate nationwide. It also includes the creation of financial incentives for larger municipalities to deliver operating licenses faster than required by the legal framework. In addition, the Program includes the implementation of a more effective system for technical safety inspections by means of a classification system based on the risk of new companies.

The Program also includes strengthening the National Institute for the Defense of Competition and Protection of Intellectual Property (INDECOPI) to punish violations of the legal framework by public entities, which is expected to discourage the discretion to impose regulations and administrative procedures outside the national legal framework.

In terms of reducing the operation costs of companies, the Program includes the simplification of the system of anticipated VAT payments by companies. It also includes mechanisms to facilitate the dissolution of companies, such as electronic auctions for seized assets to reduce costs and risks of insolvency, the creation of the Judicial Registry for Delinquent Debtors that simplifies the legal framework for insolvency, and amendments to the General Law of Insolvency to improve the quality and registry of administrators and liquidators, simplify administrative procedures under the responsibility of INDECOPI, and improve the system of offenses and penalties.

C.3 Reducing transaction costs in international trade

With respect to international trade, through the Competitiveness Agenda 2014-2018 the Government has been promoting access of companies to international markets through trade facilitation and development of standards and certifications that allow them to offer competitive products and services, as well as the development of sustainable markets, among other measures.

Along this line, the Program also includes measures related to improving the customs regime, supporting export competitiveness and market access.

In relation to the customs regime, the Program includes the modernization of the Customs Law by introducing key elements of the Revised Kyoto Convention and the Bali Treaty, particularly on issues related to the Authorized Economic Agents Regime and the adoption of a more effective system of fines. Additionally, it incorporates the elimination of stamp duties for customs declarations, which will reduce transaction costs, in accordance with the Bali WTO Trade Facilitation Agreement.

In addition, to enhance export competitiveness, the program considers the creation of the National System for Quality and National Quality Institute (INACAL), which will strengthen accreditation, standardization, and metrology systems.

D. Conclusion

As can be seen from the above information, the Peruvian Government is committed to laying the foundation for improving human capital and promoting productivity in the country, considering the various stages of labor supply and business development, facilitating its management and improving the quality of production.

The Government pledges to make further progress in these areas, which will require the support of the World Bank in the indicated areas.

Therefore, by means of this letter the Peruvian Government requests approval of the “Boosting Human Capital and Productivity Program” in the amount of US\$1.25 billion by the World Bank, under the deferred drawdown option.

Please accept, Sir, the renewed assurances of my respectful consideration.

Yours truly,

ANNEX 3: IMF ASSESSMENT LETTER

PERU—ASSESSMENT LETTER FOR THE WORLD BANK

(Documentation to support the proposal on Boosting Human Capital and Productivity Development Policy Financing with a Deferred Drawdown Option and the Public Finance Management Development Policy Financing with a Deferred Drawdown Option)

December 7, 2015

- 1. Peru's good growth performance over the past decade was recognized by the IMF Executive Board at the conclusion of the 2015 Article IV Consultation.** Directors commended Peru's impressive macroeconomic performance, underpinned by strong fundamentals and sound policy management. The country achieved high growth, low inflation and low public debt, and made progress in reducing poverty and improving living standards. Given the current downturn, Directors emphasized the importance of continued implementation of flexible and coordinated policies as well as structural reforms to maintain macroeconomic stability and foster more inclusive long-term growth.
- 2. As in the rest of the region, the pace of economic activity slowed markedly in 2014.** Real GDP grew by 2.4 percent in 2014 (down from 5.5 percent on average over the last 5 years) due to a combination of adverse external and domestic factors. External shocks were compounded by an unexpected drop in sub-national investment and temporary supply disruptions in mining, agriculture and fishing. These developments lingered into this year and staff revised down the growth forecast for 2015 from 3.8 to 2.4 percent in the *October WEO*. Growth is expected to rise above 3 percent in 2016 as new mines come on stream and large infrastructure projects unfold.
- 3. Inflation has been above the 3 percent upper band of the central bank target since end-2014 due to supply shocks and currency depreciation.** The central bank increased the policy rate from 3.25 to 3.5 percent in September, but left it unchanged in two subsequent meetings, to ensure that medium-term inflation expectations remain anchored despite further currency depreciation. While expectations are well anchored, financial market participants expect a return to the target range (1 to 3 percent) only in 2017.
- 4. The authorities have drawn on their large fiscal buffers to provide stimulus to the economy.** After being in balance in 2014, the fiscal position is expected to switch into a deficit of about 2 percent on the back of a significant decline in commodity and tax revenue—due to the reduction in income tax rates as part of the stimulus measures and slow economic growth. The final deficit figure for the year could be lower, however, if sub-national spending continues to underperform. While Peru has ample policy space to undertake countercyclical fiscal policy, allowing such a deficit required an application of an exceptional clause under the new fiscal rule. Gross public debt is expected to grow to 22 percent of GDP in 2015, which is still low by regional standards. While the authorities envisage a fiscal deficit of 3 percent in 2016 due to the effect of lower growth on revenue and provisions for El Niño, which augmented the capital expenditure envelope, staff projects the

deficit to be below 2.5 percent of GDP given persistent difficulties in the execution of public investment.

5. **The external current account deficit has been narrowing, despite further deterioration in the terms of trade.** The current account deficit was around 4 percent of GDP in 2014, and international reserves declined by around US\$3 billion as capital flows were insufficient to cover the deficit. The current account deficit is expected to shrink further in 2015, to below 4 percent, not least due to a sharp reduction in imports and investment income payments; it remains fully financed, mostly by long-term flows. Exchange rate policy has been more flexible over the past two years, although the central bank intervened both in the spot and forward markets to limit excessive volatility. The sol depreciated 13.7 percent (yoy) as of mid-November 2015 and has been trading recently at 9-year lows. The real exchange rate is assessed to be broadly in line with fundamentals and NIR stood at around US\$62 billion (about 30 percent of GDP) in October 2015.

6. **The financial sector remains healthy.** Despite some weaknesses identified in a few small non-bank depository institutions, the overall health of the financial system remains solid. Private credit growth has remained robust (at about 10 percent yoy in September 2015) and credit dollarization has continued to decline in response to measures introduced by the central bank (31.5 percent of total credit in September was in U.S. dollar compared to 39 percent a year earlier). At the beginning of November, the central bank set a new target for financial institutions' de-dollarization process, specifying that by December 2016 they must reduce the stock of U.S. dollar-denominated credit by 20 percent from the levels of September 2013.

7. **The current policy mix is broadly adequate.** Monetary conditions remain appropriately accommodative, but policymakers should remain attentive to inflation expectations. Exchange rate flexibility remains key for cushioning external pressures. Given the continuing difficulties with execution of capital expenditure at the local level, greater spending is encouraged at the central government level, mainly through improving the rates of execution. However, scaling up of public investment should be in line with enhancements in public financial management capacity, also at the sub-national level, in order to ensure high rates of return for investment projects. There is also a need to increase revenue collection to offset the recent erosion of tax revenues due to income tax rate cuts. As the recovery takes hold, a gradual fiscal consolidation will be appropriate. Over the medium term, it would be advisable to target a small structural fiscal surplus of ½ percent of GDP to preserve buffers in light of commodity shocks, natural disaster risks, and contingent liabilities.

8. **Downside risks are manageable given large international reserves and fiscal buffers.** Peru is already facing a significant terms-of-trade shock, with further risks to the downside. The outlook is subject to other important risks, such as a more rapid economic slowdown in China, normalization of monetary policy in the United States, uncertainties

linked to the 2016 presidential elections in Peru, and a possibly more severe El Niño weather phenomenon. The effects of potential shocks should be cushioned by ample fiscal policy space, including the low levels of debt and high savings, together with still high NIR, which are adequate according to the Fund's reserve metrics, and Peru should be using its buffers wisely. Boosting Peru's productive potential and ensuring all-inclusive growth requires steadfast implementation of structural reforms to enhance productivity, investment, human capital, and formal employment.

Peru: Selected Economic Indicators								
(Post-October WEO Projections)								
	Prel.			Proj.				
	2013	2014	2015	2016	2017	2018	2019	2020
Social Indicators								
Life expectancy at birth (years) 1/	74.8	...	...	...	...	...	...	...
Infant mortality (per thousand live births)	12.9	...	...	...	...	...	...	...
Adult literacy rate 1/	93.8	...	...	...	...	...	...	...
Poverty rate (total)	23.9	...	...	...	...	...	...	...
Unemployment rate	5.9	5.9	...	...	...	...	...	...
(Annual percentage change; unless otherwise indicated)								
Production and prices								
Real GDP	5.8	2.4	2.4	3.3	5.5	5.2	4.3	4.0
Real domestic demand	6.9	2.2	2.1	2.0	5.3	4.7	4.1	4.0
Consumer prices (end of period)	2.9	3.2	3.9	3.4	2.5	2.0	2.0	2.0
Consumer prices (period average)	2.8	3.2	3.5	3.0	2.5	2.0	2.0	2.0
External sector								
Exports	-9.6	-7.8	-14.2	2.0	9.9	8.9	6.5	5.4
Imports	2.7	-3.4	-10.5	0.1	8.2	6.4	5.2	4.6
Terms of trade (deterioration -)	-5.7	-5.4	-5.1	-3.1	0.6	0.6	0.4	0.6
Real effective exchange rate (depreciation -)	-0.2	-1.5	...	...	...	...	...	...
Money and credit 2/ 3/								
Broad money	14.8	8.4	13.8	15.1	13.4	13.5	13.5	13.5
Net credit to the private sector	18.4	13.5	13.8	15.1	13.4	13.5	13.5	13.5
(In percent of GDP; unless otherwise indicated)								
Public sector								
NFPS revenue	27.9	27.4	25.4	25.4	25.2	25.3	25.4	25.4
NFPS primary expenditure	25.9	26.6	26.6	26.5	26.0	25.6	25.3	25.2
NFPS primary balance	2.0	0.7	-1.2	-1.2	-0.8	-0.2	0.2	0.2
NFPS overall balance	0.9	-0.3	-2.3	-2.4	-2.0	-1.5	-1.0	-0.9
External Sector								
External current account balance	-4.2	-4.0	-3.7	-3.5	-3.6	-3.5	-3.4	-3.3
Gross reserves								
In millions of U.S. dollars	65,710	62,353	58,853	58,353	58,153	58,053	57,953	58,703
Percent of short-term external debt 4/	539	508	425	484	506	493	450	509
Percent of foreign currency deposits at banks	275	262	260	250	237	225	216	212
Debt								
Total external debt	27.3	29.7	32.0	32.3	30.3	28.3	26.2	24.9
Gross non-financial public sector debt (incl. repayment certificates)	20.3	20.7	22.3	24.4	24.5	24.1	23.5	23.5
External	8.8	8.8	9.3	9.8	9.6	8.9	7.9	7.6
Domestic	11.5	12.0	13.1	14.6	14.9	15.2	15.6	15.9
Savings and investment								
Gross domestic investment	27.8	26.2	25.3	23.9	25.0	25.0	25.0	24.9
Public sector (incl. repayment certificates)	5.8	5.6	5.1	5.0	5.0	5.0	5.1	5.1
Private sector (incl. inventories)	22.0	20.6	20.2	18.9	20.0	20.0	19.9	19.8
National savings	23.6	22.2	21.7	20.4	21.4	21.5	21.7	21.7
Public sector	7.1	5.8	3.3	3.3	3.7	4.3	4.8	5.0
Private sector	16.5	16.4	18.4	17.2	17.7	17.2	16.9	16.7
Memorandum Items								
Nominal GDP (\$/ billions)	545.6	575.2	604.2	634.7	683.8	734.3	781.3	830.2
GDP per capita (in US\$)	6,524	6,449	5,652	5,596	5,937	6,278	6,579	6,883
Sources: National Authorities; UNDP Human Development Indicators; and Fund staff estimates/projections.								
1/ Data for 2012.								
2/ Corresponds to depository corporations.								
3/ Foreign currency stocks are valued at end-of-period exchange rates.								
4/ Short-term debt is defined on a residual maturity basis and includes amortization of medium and long-term debt.								