INTERNATIONAL MONETARY FUND

IMF Country Report No. 16/234

PERU

July 2016

2016 ARTICLE IV CONSULTATION—PRESS RELEASE; AND STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2016 Article IV consultation with Peru, the following documents have been released and are included in this package:

- A **Press Release**.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis, following discussions that ended May 6, 2016, with the officials of Peru on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 3, 2016.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below have been or will be separately released.

Selected Issues

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July 20, 2016

International Monetary Fund
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IMF Executive Board Concludes 2016 Article IV Consultation with Peru

On June 20, 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Peru, and considered and endorsed the staff appraisal without a meeting.[2]

As a result of prudent macroeconomic management, Peru has successfully navigated the commodity cycle and the 2008–09 global financial crisis, and still leads growth among large Latin American economies. Thus, the new government, which takes office on July 28, 2016, will inherit an economy with a solid foundation, good institutional frameworks in place, and structural reforms in train.

However, important challenges now loom, as metal prices have entered into a slump since their 2011 peak, hurting exports, investment, and fiscal revenues. Following a sharp and unexpected drop in 2014, growth picked up in 2015, reaching 3.3 percent largely owing to higher metals production and fishing, and a partial recovery in services and commerce. Despite a widening negative output gap, inflation increased by more than 1 percentage point to 4.4 percent, y-o-y, in December 2015, reflecting food supply shocks, regulatory adjustments to energy prices, and a pass-through from currency depreciation. The external current account reached a deficit of 4.4 percent in 2015 despite the sol depreciation.

Monetary and exchange rate policies remained attentive to rapidly changing conditions. The central bank has raised the policy rate since September 2015 by a full percentage point to 4.25 percent aiming at re-anchoring inflation expectations, which has added to tighter external financial conditions. The sol was allowed to depreciate 14 percent with respect to the U.S. dollar, while volatility was contained. The authorities have eased the adjustment to commodity price shocks through an expansionary fiscal policy in 2015, but with mixed results, as capital spending continues to suffer delays.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

Peru is positioned to grow faster in the next two years, as mining production reaches full capacity and large infrastructure projects advance. Inflation is expected to decline. Risks to the outlook are balanced, and downside risks are mostly on the external side. Upside risks on the domestic front are a pick-up in sub-national investment and possible larger-than-projected increases in confidence and investment after the presidential election.

Executive Board Assessment

After decelerating sharply in 2014, economic activity recovered last year despite a volatile external environment. The recovery largely reflected additional mining production capacity coming on stream, although non-mining activity has also accelerated modestly more recently. An expected increase in mining exports, together with some rebound in public investment, will impart a strong positive impetus on growth going forward, which should spillover to non-commodity sectors. Thus, despite sluggish external conditions, activity is expected to accelerate further in 2016 and 2017, while inflation continues to decline.

Risks to the outlook are balanced. External pressures have carried over from last year and comprise possibly weaker-than-projected growth in China (and, hence, softer metal prices), possible adverse spillovers from other countries in the region (though these should be relatively small), sharp asset price adjustments in advanced and emerging economies, and an even stronger dollar. The response to shocks should be through further exchange rate flexibility and easing liquidity conditions to support credit activity. Upside domestic risks include stronger-than-expected improvements in business confidence (especially if the incoming government announces decisive productivity-enhancing reforms) and a more effective execution of the existing pipeline of infrastructure projects, which could lift growth further in 2016–17 and beyond.

Monetary and exchange rate policies should remain attentive to rapidly changing conditions. Following monetary tightening, the BCRP should now maintain a wait-and-see stance—given declining inflation and medium-term inflation expectations, the fact that it is too soon to evaluate the effect of past monetary tightening on economic activity and inflation, and the usual uncertainties surrounding the exact cyclical position of an economy. This said, a possibly steeper interest rate path in the United States than currently priced by the financial market could trigger the need for further monetary tightening in Peru. Greater exchange rate flexibility in 2015 was a welcome development with no noticeable impact on firms' and banks' balance sheets; the latter remain healthy and profitable. Further decline in credit de-dollarization has been achieved not least due to the measures introduced by the BCRP. Further exchange rate flexibility would support the development of hedging instruments to reduce currency risk and help accelerate the de-dollarization process. Recent measures to deepen Peru's equity market are also welcome.

A gradual fiscal consolidation in the next few years is advisable to maintain healthy debt dynamics and to protect fiscal buffers. With the output gap closing around end 2017, there is no case for loosening fiscal policy. A gradual fiscal consolidation would be important for ensuring the sustainability of pensions, and defending against natural disasters and realization of contingent liabilities. To accommodate higher-than-projected public capital spending, it will be critical to create adequate fiscal space through containing current spending that is not complementary to capital expansion and structural reforms (including in health and education), and raising the low revenue collection through streamlining administration, reducing informality and exemptions, and protecting Peru's tax base from possible international profit shifting by multinational corporations. Reducing bottlenecks to public investment and improving management would go a long way toward enabling full execution of budgeted spending and would support private investment.

With the end of commodity-driven growth, the agenda for growth-spurring structural reforms has become a higher priority, including for further poverty reduction. Investments in capital and labor will be needed to boost potential growth, which is otherwise estimated to be 3.5 percent in the absence of continued reforms. Long-standing challenges include reducing informality, which should be in part addressed through labor market reforms aiming at lowering the costs of hiring and firing workers, and spurring investment in non-extractive industries, including through improving competitiveness and infrastructure. Peru's current decentralization framework should be improved, as it constrains full execution of planned capital expansion and better allocation of resources. While Peru has achieved one of the highest rates of education coverage in Latin America, the low quality of education remains a crucial challenge, and the ongoing reforms will need to continue. Efforts to raise financial inclusion are commendable, especially through the launch of the broad-based National Financial Inclusion Strategy and the private sector-led e-money platform. Free trade agreements also provide an opportunity for boosting and diversifying long-term growth.

Staff would like to relay their appreciation to the outgoing administration for the constructive dialogue and look forward to working with the new government.

Peru: Selected Economic Indicators

	2011	2012	2013	2014	2015	Projections 2016	2017
Social Indicators							
Life expectancy at birth (years)	73.8	74.0	74.2	74.4	74.6	…	…
Infant mortality (per thousand live births)	16.0	17.0	16.0	17.0	17.6	…	…
Adult literacy rate	92.9	93.8	93.8	93.7	…	…	…
Poverty rate (total) 1/	27.8	25.8	23.9	22.7	21.8	…	…
Unemployment rate	7.7	6.8	5.9	5.9	6.5	…	…
	(Annual percentage change; unless otherwise indicated)						
Production and prices							
Real GDP	6.5	6.0	5.9	2.4	3.3	3.7	4.1
Real domestic demand	7.7	7.2	7.3	2.2	2.9	2.4	3.3
Consumer Prices (end of period)	4.7	2.6	2.9	3.2	4.4	3.2	2.5
Consumer Prices (period average)	3.4	3.7	2.8	3.2	3.5	3.8	2.5
External sector							
Exports	29.5	2.2	-9.6	-7.8	-13.4	-1.0	7.1
Imports	28.9	10.4	3.3	-3.1	-8.9	-4.5	3.9
Terms of trade (deterioration -)	7.3	-2.6	-5.2	-5.4	-6.3	-1.7	-0.1
Real effective exchange rate (depreciation -)	-1.4	8.1	-0.2	-1.6	0.8	…	…
Money and credit 1/ 2/							
Broad money	15.1	12.5	15.3	9.5	11.6	13.7	14.0
Net credit to the private sector	21.6	13.3	18.3	13.2	14.0	13.7	14.0
	(In percent of GDP; unless otherwise indicated)						
Public sector							
NFPS Revenue	27.2	27.7	27.8	27.7	24.6	24.3	24.8
NFPS Primary Expenditure	24.0	24.3	25.8	26.8	25.7	25.1	25.1
NFPS Primary Balance	3.2	3.4	2.0	0.8	-1.1	-0.9	-0.2
NFPS Overall Balance	2.0	2.3	0.9	-0.3	-2.1	-2.1	-1.6
External Sector							
External current account balance	-1.9	-2.7	-4.2	-4.0	-4.4	-3.9	-3.5
Gross reserves							
In millions of U.S. dollars	48,859	64,049	65,710	62,353	61,537	62,230	62,930
Percent of short-term external debt 3/	559	494	539	508	554	559	601
Percent of foreign currency deposits at banks	228	300	274	258	224	222	209
Debt							
Total external debt	25.6	27.3	27.2	29.7	33.7	37.7	36.5
NFPS Gross debt (including Repaymetn Certificates)	23.0	21.2	20.3	20.7	24.0	25.9	25.8
External	11.4	9.8	8.8	8.7	11.1	12.4	12.1
Domestic	11.6	11.4	11.5	12.0	12.9	13.5	13.7
Savings and investment							
Gross domestic investment	25.7	26.0	27.9	26.4	26.0	24.6	24.2
Public sector 4/	4.8	5.4	5.8	5.8	5.0	4.7	4.9
Private sector	19.1	20.3	20.7	20.1	19.3	18.3	18.3
National savings	23.9	23.4	23.7	22.3	21.6	20.7	20.7
Public sector 5/	7.5	8.1	7.0	5.9	3.7	3.4	4.1
Private sector	16.4	15.3	16.6	16.4	17.9	17.4	16.7
Memorandum items							
Nominal GDP (S/. billions)	469.9	507.7	546.0	576.0	612.0	647.2	688.3
GDP per capita (in US$)	5,731	6,396	6,629	6,586	6,168	5,548	5,811

Sources: National Authorities; UNDP Human Development Indicators; and Fund staff estimates/projections.
1/ Corresponds to depository corporations.
2/ Foreign currency stocks are valued at end-of-period exchange rates.
3/ Short-term debt is defined on a residual maturity basis, and includes amortization of medium- and long-term debt.
4/ Includes Repayment Certificates (CRPAOs).
5/ Excludes privatization receipts.

INTERNATIONAL MONETARY FUND

PERU

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION

June 3, 2016

KEY ISSUES

Context: Even though economic conditions in Latin America remain fragile, the new Peruvian government, which takes office on July 28, 2016, will inherit an economy with a solid foundation. Over the last five years, and despite a downward trend in metal prices, sizable fiscal and monetary buffers have been built and carefully managed, Peru's investment grade rating has been consolidated, economic diversification fostered, private investment crowded in through partnerships in infrastructure projects, and reforms initiated in civil service, education, and health care. Targeted social assistance programs also went a long way in reducing poverty further.

Recent developments: Like the rest of the region, Peru has been affected by the end of the commodity cycle. Following a sharp, unexpected drop in 2014, growth picked up in 2015 largely due to higher metals production and fishing. The recovery spilled over to Q1 2016, and Peru remains one of the fastest growing economies in Latin America.

Outlook and risks: Unlike most of its peers, Peru is expected to grow faster in the next two years, assuming expanded mining production remains as competitive as currently, and large infrastructure projects advance. Risks to the outlook are balanced with downside risks mostly on the external side. Upside risks on the domestic front are a pick-up in sub-national investment and a perceived investor-friendly outcome of the presidential elections (which reduces the risk of eroding Peru's prudent fiscal framework) implying possible larger-than-projected increases in confidence and investment.

Policy advice: The current policy mix is broadly adequate. A wait-and-see monetary stance should be maintained at present given lagged effects from previous monetary tightening and declining inflation. Greater exchange rate flexibility is welcome in helping adjustment and should be continued. The progress in credit de-dollarization is laudable and further steps in this direction should increase the effectiveness of monetary policy and reduce financial vulnerabilities. The consolidation strategy, which is guided by the current fiscal framework, is appropriate; larger spending on public infrastructure and social projects should be accommodated through raising tax revenue without compromising Peru's positive debt dynamics. The continuation of ongoing reforms and a strong push for reforms in the labor market, fiscal decentralization, and public investment management are crucial to boost potential growth.

Approved By
A. Cheasty and S. Barnett (SPR)

Discussions took place in Lima during April 25–May 6, 2016. Mission team: M. Estevão (Head), F. Roch, and S. Vtyurina (all WHD), G. Everaert (SPR), Y. Mooi (MCM), and R. Schatan (FAD Expert). A. Santos (Senior Resident Representative) assisted the mission. Mr. Hendrick (OED) also participated in the discussions. The mission held discussions with the Minister of Economy and Finance, Alonso Segura, the President of the Central Reserve Bank of Peru, Julio Velarde, the Minister of Education, Jaime Saavedra, the Governor of the Province of Arequipa Yamila Osorio Delgado, other senior government officials, and representatives of the private sector and civil society. The mission's findings will also be relayed to the new economic team during a short staff visit on June 13–14.

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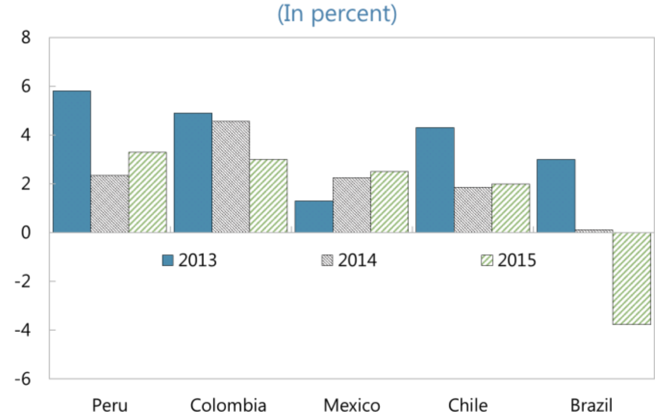
CONTEXT

1. As a result of prudent macroeconomic management, Peru has successfully navigated the commodity cycle and the 2008–09 global financial crisis, and still leads growth among large Latin American countries. However, important challenges now loom as metal prices have dropped markedly since their 2011 peak, hurting exports, investment, and fiscal revenues. Like other emerging markets, Peru experienced capital outflows as global portfolios rebalanced and investment appetite dropped. The sol has depreciated 31 percent with respect to the U.S. dollar since its peak in January 2013, but only 3.8 percent in nominal effective terms over the same period, and Peru's current account deficit widened. While supportive policies over the past three years have softened the adjustment, growth averaged about 2¾ percent over 2014–15 compared to $6^{1/5}$ percent over the previous decade. Following the runoff in the presidential elections (June 5), a new government will assume office (July 28), providing an opportune time for setting a medium-term agenda that builds on past achievements to raise potential growth and further reduce poverty.

Selected Latin American Countries: Growth Rates
(In percent)



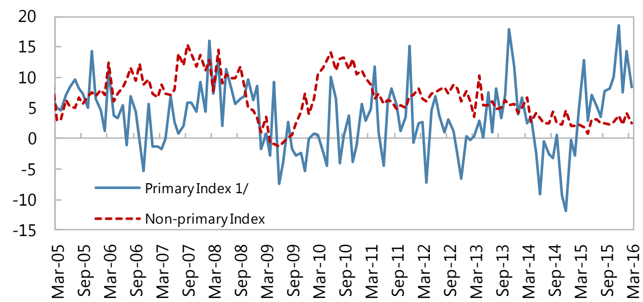
Sources: National Authorities; and Fund staff estimates.

RECENT DEVELOPMENTS

2. After decelerating sharply in 2014, economic activity recovered somewhat in 2015.[1] Growth reached 3.3 percent in 2015, led by mining and fisheries and a partial recovery in services and commerce, while the unemployment rate increased to 6.5 percent, reflecting lagged effects from the sharp downturn in 2014. From an aggregate demand perspective, private and public consumption supported growth in 2015, together with inventory accumulation. The inventory build-up, which more than explains the growth increase in 2015, is due to the year-end surge in mining output which was exported during the first quarter of 2016. Gross private and public fixed investment was a drag on overall activity. The external current account reached a deficit of 4.4 percent in 2015, mostly owing to large declines in metal prices while non-commodity exports did not pick up despite the sol depreciation. The current account deficit was partially financed by borrowing and foreign direct investment, while other capital flows remained subdued.

[1] See the accompanying *Selected Issues Paper*, Chapter 1, for a comparison of recent adjustment to shocks in Chile, Colombia, and Peru.

Peru: Real GDP Decomposition
(In percent, year-over-year changes)



Sources: National authorities; and Fund staff calculations.
1/ Primary includes Agriculture, fishing, mining and hydrocarbons, and manufacturing process for primary resources.

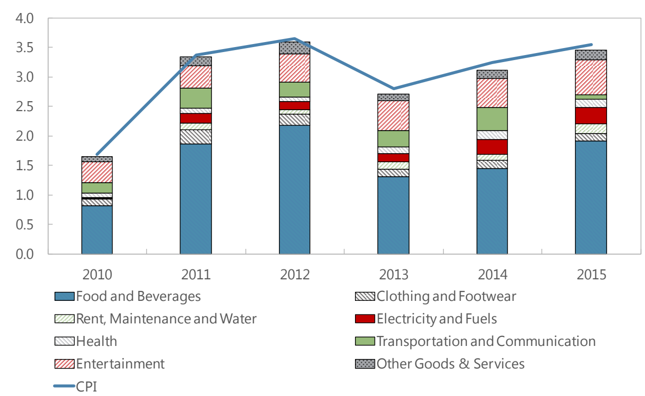
Peru: Real Aggregate Demand Growth
(Contribution to growth rates, y-o-y, percent)

	2014 Year	2015 Year	2016 Q1	2016 Proj. Year
Domestic Demand	**2.3**	**3.0**	**2.0**	**2.3**
Private Consumption	2.5	2.1	2.3	2.3
Domestic Investment	-1.4	-0.3	-1.7	-0.3
Private	-0.5	-0.9	-1.0	-0.4
Public	-0.1	-0.4	0.9	0.2
Change in Inventories 1/	-0.8	1.1	-1.6	-0.1
Public Spending	1.0	0.7	2.2	0.3
External Demand	**0.1**	**0.3**	**2.5**	**1.4**
Exports	-0.2	0.9	1.9	1.6
Imports	0.3	-0.6	0.6	-0.1
Gross Domestic Product	**2.4**	**3.3**	**4.4**	**3.7**

Sources: National authorities; and Fund staff estimates.
1/ While inventories are projected to unwind through Q3 2016, for the year total it is implied that a similar accumulation of mining inventories will take place by year-end as last year.

3. **Rising inflation pushed the central bank (BCRP) into tightening the monetary stance in 2015.** Despite a widening negative output gap, inflation increased by more than 1 percentage point to 4.4 percent, y-o-y, in December 2015, reflecting food supply shocks, regulatory adjustments to energy prices, and a pass-through from currency depreciation.[2] The BCRP has raised the policy rate since September 2015 by a full percentage point to 4¼ percent aiming at re-anchoring inflation expectations, which has added to tighter external financial conditions (Box 1).

Peru: Contributions to CPI Inflation
(Average, in percent)

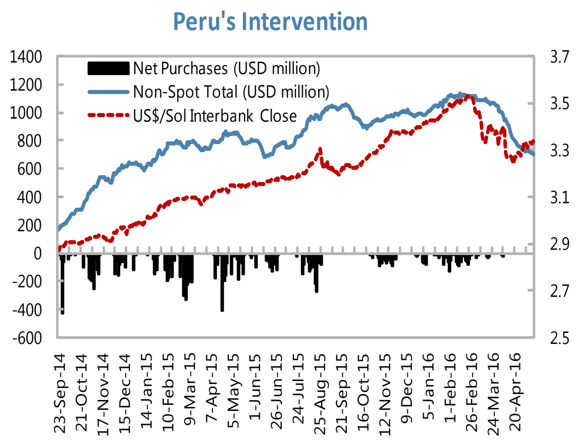


Source: National authorities; and Fund staff calculations.

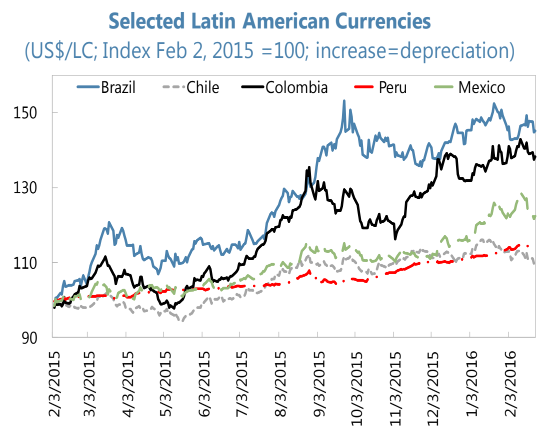
4. **Over 2015, the sol depreciated amid the BCRP's FX intervention.** The sol depreciated 14 percent with respect to the U.S. dollar, much more than in 2014 but less than other LA5 currencies, implying a flatter path for the sol in real effective terms. Overall, the external position was assessed as moderately weaker than fundamentals with a positive real effective exchange rate

[2] Effective May 1, 2016, the energy regulator announced cuts in electricity prices, which are indexed to the U.S. dollar, for residential and commercial consumers.

(REER) gap and a current account deficit wider than its norm (Annex II). Net spot market sales were significant, amounting to US$8 billion or about 4 percent of GDP; FX swaps and FX-linked certificates of deposit accounted for US$3.2 billion or about 2 percent of GDP; however, intervention slowed by year-end and more recently has focused on managing appreciation pressures. Net international reserves (NIR) remained high, at US$61.5 billion (308 percent of the Assessing Reserve Adequacy (ARA) metric, or 263 percent after augmenting the ARA for commodity buffers). While a significant part of NIR consists of domestic FX liabilities, these are mostly of maturities of 2 years and longer, and do not constitute a short-term risk to reserves (Annex II). After adjusting for these liabilities, NIR still remained within the adequacy range.



Source: Central Reserve Bank of Peru.



Sources: Bloomberg, and Fund staff calculations.

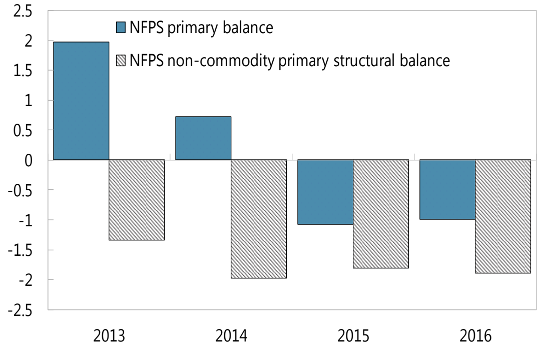
5. Following a string of surpluses since 2009, the non-financial public sector (NFPS) deficit rose to about 2 percent of GDP in 2015. Government revenues fell by about 2 percent of GDP. A loss of income from reduced tax rates accounted for about ⅓ of the total; the rest was explained by a structural drop in commodity prices, one-off extraordinary revenues collected in 2014, and higher tax reimbursements on overestimated pre-payments, especially by commodity producing companies. Under-execution of capital spending, especially at sub-national levels of government, undermined the authorities' targeted fiscal impulse. Overall, fiscal policy remained broadly neutral in structural terms, and is estimated to have contributed *negatively* to economic activity in 2015 since multipliers on investment spending (which fell) are greater than tax and current-spending multipliers.[3] Gross public debt increased to about 24 percent of GDP, including pre-financing operations,[4] with net debt (gross debt excluding government deposits at the central bank and in private banks) increasing to 7 percent of GDP.[5]

[3] Staff estimates of fiscal multipliers in the accompanying *Selected Issues Paper,* Chapter 2, while to be interpreted with the usual caution, indicate that capital spending multipliers have a larger effect on growth both during cyclical upturns and downturns (0.5–1.1) and over different horizons than tax measures and current spending increases. Weighting revenue and spending impulses by their respective multipliers, the impact of the fiscal impulse on the economy in 2015 was a *negative* 0.3 percent.

[4] After a decade absence in European markets, Peru issued a 1.1 billion euro bond with 11-year maturity, yielding 2.75 percent, to pre-finance the 2017 needs.

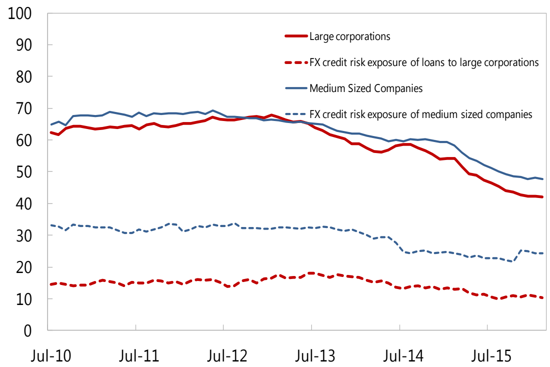
[5] In June 2015, the authorities also published for the first time the stock of contingent liabilities (as required by the fiscal rules framework adopted in 2014).

Peru: Fiscal Outcomes
(In percent of GDP)



Sources: National authorities; and Fund staff calculations.

Corporate Sector's Dollarization and FX Credit Exposure
(Share of total loans)



Source: National authorities.

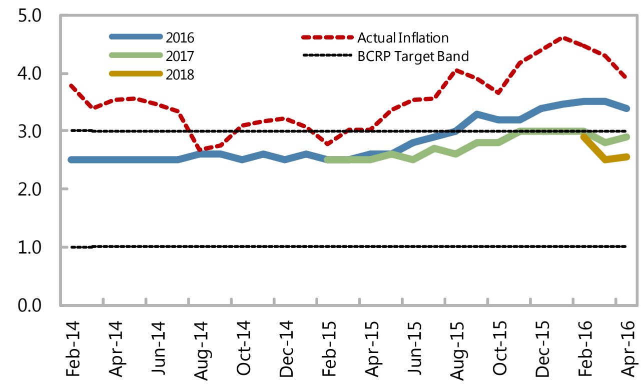
6. **The banking sector reported strong results in 2015** (Annex III). In an effort to reduce dollarization and encourage financial intermediation in local currency, the BCRP reduced the average reserve requirement rate on local currency deposits from 20 percent to 6.5 percent from May 2013 through June 2015. Private sector credit grew robustly at 9½ percent (y-o-y, in FX adjusted terms), also reflecting a shift of corporate borrowing towards the domestic market. Net profits increased 32 percent, the highest rate since 2008, while credit risk indicators stabilized. Direct exposure to the commodity sector remains limited, and banks are solid, profitable, and liquid. As a result of amplified de-dollarization measures introduced in late-2014, the share of FX loans in total loans dropped to 27.4 percent in January 2016 from 38.2 percent in December 2014. Expectations of further currency depreciation boosted dollar deposits in commercial banks in 2015 to about 45 percent of total deposits from 40 percent in 2014. The BCRP has been offering FX repos with maturities of 2 to 5 years to close banks' open balance-sheet positions in U.S. dollars and support the creation of credit in local currency.

OUTLOOK AND RISKS

7. **The recovery is off to a good start in the first quarter of 2016.** Led by the jump in exports (which absorbed the excess of mining inventories accumulated in end-2015), a pick-up in private consumption, and a strong rebound in public spending (including investment), GDP grew 4.4 percent, y-o-y, in the first quarter of 2016, with final domestic demand (domestic demand excluding inventory accumulation) accelerating to 3.6 percent, y-o-y, from 3.3 percent, y-o-y, in the fourth quarter of 2015. Inflation has declined since end 2015 (3.9 percent, y-o-y, in April 2016) and inflation expectations have fallen within the BCRP's target range at the 2017 and 2018 horizons. Credit growth remained stable (8.3 percent in April, y-o-y), investment sentiment is recovering following the first round of the presidential election on April 10, and the sol has appreciated since mid-February 2016.

8. While short to medium-term growth prospects for many South American countries are weak, higher mining exports and some rebound in public investment should impart a strong impetus to growth in Peru. With marginal costs of producing copper in Peru well below current metal prices, large mining companies are bringing additional mining capacity on stream following the completion of expansion projects and new mines, often at the expense of cutting production elsewhere in the world. After under-executing capital spending in 2015, government investment has picked up in 2016Q1 with prospects of further expansion during the year. As business confidence continues to recover, the incipient recovery seen in several non-commodity producing sectors in 2015Q4 and 2016Q1 is expected to continue and staff projects a 3¾ percent growth in 2016 and 4.1 percent growth in 2017. By 2017, mining production is expected to double from its 2014 level, with smaller increases thereafter owing to stalling new mining investment. The authorities project slightly higher growth than the staff's forecast for 2016 and 2017 on the assumption of stronger investment. Inflation should converge to the target band by early-2017 as the fallout from *El Niño* wears off, the pace of currency depreciation slows in 2016, and the full effect of past monetary tightening is felt.

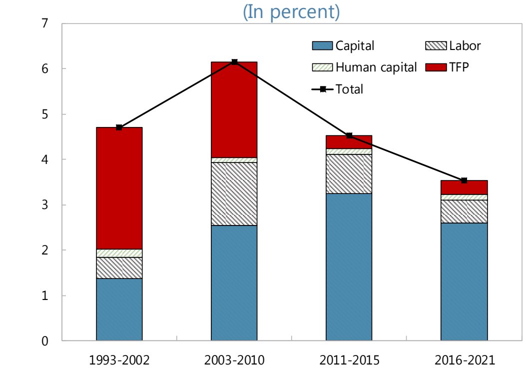
Actual and Expected Inflation
(By Economic Analysts, in percent, year over year)



Source: Central Reserve Bank of Peru.

9. Peru's medium-term fundamentals remain strong but its potential growth has been revised downwards. A one percentage-point downward revision to 3½ percent annual growth from 2018 onwards mostly reflects lower projections for private investment in the metals and hydrocarbon sectors, small increases in copper production after 2017, downward revisions to global growth, and the baseline assumption of a *status quo* in structural reforms.[6] The authorities envisage the implementation of structural reforms and higher rates of growth in private non-commodity investment and public capital spending execution, resulting in potential growth estimates ranging from 4.0 to 4.5 percent. From a growth decomposition perspective, the staff forecast

Peru: Contributions to Potential Growth 1/
(In percent)



Sources: National authorities; and Fund staff calculations.
1/ Based on production function approach.

[6] *Cerro Verde*, *Las Bambas* and *Antamina* mines are expected to be the world's second, fourth and fifth largest copper mines by 2017. Falling copper prices are seen as unlikely to cause production cuts as copper's marginal production cost for Peru's large mines is about US$1.2–1.5 per pound, which is still significantly below the international price of about US$2¼. And, to recover mega investments, new or amplified mines will need to produce, even at the currently reduced margins. In contrast, low oil prices are no longer enough to cover production costs in Peru and oil production has decelerated steadily.

assumes a continuation of the relatively low total factor productivity (TFP) growth seen on average from 2011 to 2015. This is consistent with the historical relationship between commodity prices and TFP growth. As additional mining capacity feeds into higher exports over the medium term, the current account deficit is projected to approach the norm of 2 percent of GDP by 2021 under current policies (Annex II). The authorities saw the exchange rate to be currently in line with fundamentals, noting that EBA models do not fully account for future copper expansion. The staff's baseline fiscal scenario is in line with the current authorities' projections envisaging consolidation driven by their fiscal rule. Despite policy tightening, monetary aggregates should grow more than nominal GDP due to financial deepening.

10. Downside risks are similar to those in last year's assessment. The authorities and the staff agree that the main external risks to growth are: (i) structurally weak growth and disorderly rebalancing (towards services production) in China, affecting metal prices; (ii) a stronger-than-expected dollar; and (iii) sharp asset price adjustments and decompression of credit spreads (Box 2). The spillovers from the crisis in Brazil have been negligible, with exports to Brazil accounting for only 3 percent of total, and markets seeing the crisis as an idiosyncratic event and not a representation of broader problems in emerging market economies. There is some upside domestic risk to staff's near-term forecast from further strengthening of non-primary sectors' growth, already observed in Q1 2016, a possibly stronger pickup in sub-national investment, improvement in TFP, and the widely-perceived investor-friendly outcome of the presidential elections leading to larger-than-projected increases in confidence and investment.

POLICY DISCUSSIONS

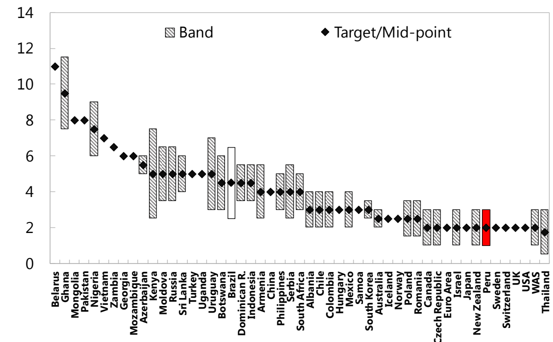
A. Holding Tight

11. The recent monetary tightening appropriately aimed at re-anchoring inflationary expectations. Under the authorities' and staff's baseline scenarios, Peru's small output gap would be closed around end-2017. Observed and expected inflation outside the target band could be reasons for tightening the monetary stance further. However, the declines in year-on-year inflation since end-2015 and softer medium-term inflation expectations corroborate the BCRP's current wait-and-see approach. The authorities reaffirmed their view (and staff agreed) that future policy moves should be guided by the drivers of future inflation, such as movements in inflation expectations, and take into account the lags with which changes in the monetary policy stance affect the economy. The authorities and staff exchanged views on the estimates of the exchange rate pass-through to prices (Box 3), which fall into the range of 0.1−0.2 for 1 percent depreciation depending on the methodology. The authorities and staff concurred that the pass through is high for some non-tradable goods that are directly priced in U.S. dollars. Staff stressed the importance of continued BCRP guidance so that temporary inflation shocks do not contaminate inflation expectations. Staff remarked that a possibly steeper path of interest rate hikes in the United States than currently priced in by financial markets could trigger the need for further rate increases in Peru to address the inflationary impact of a weaker sol. And there could be some pressure from the recent 13 percent increase in the national minimum wage; however, as discussed with the BCRP, the pass-through of minimum wage increases to consumer price inflation is uncertain. Staff expects inflation to be within the authorities' target range in the medium term.

12. Staff raised the possibility that the inflation target band in Peru could be demanding. This is viewed in light of the country's still high exposure to relative price shocks, stage of development, and the average inflation rate of 2¾ percent (close to the top of the targeted range) since the start of the inflation-targeting regime. Clearer indications to the market that the BCRP's "target" is the whole target range rather than the mid-point of the range or any specific numerical point would better align BCRP's communication with its actions. The authorities stated that Peru has been subjected to many supply shocks in the past that did not warrant monetary policy action and that inflation excluding food and fuels (around 2¼ percent over the last decade) has been lower than headline inflation. Their choice of targeting a band range (rather than its midpoint) is understood by market participants. The choice was driven by the level of U.S. inflation, as a higher domestic inflation target would lead to a weaker currency and to lower demand for local currency, increasing dollarization.

Inflation Target Regimes: Cross Country Comparison

(In percent)



Source: IMF country teams.

13. The commendable steady de-dollarization of credit portfolios has helped reduce financial stability risks and improve the transmission of monetary policy to economic activity and inflation. Discussions focused on the next steps for the de-dollarization process, which was accelerated in 2015 owing to the BCRP's measures. The increase in U.S. dollar deposits in 2015 squeezed local currency funding and the BCRP repos provided a mechanism to avoid a credit crunch in local currency for now. Staff inquired whether these repos would be a long-standing feature of Peru's financial sector, with their associated distortions on credit growth and exchange rate risks for the BCRP. The BCRP asserted that its long-run repo operations (using dollar deposits as collateral) are of a transitory nature and will be wound down as domestic currency deposits pick up again and de-dollarization continues.[7] Both the BCRP and bank supervisors (SBS) see the increase in U.S. dollar deposits as a temporary response of economic agents to expectations that the sol would depreciate further during the year. Staff suggested that more stringent prudential requirements could further help make FX deposits less attractive, although directly imposing higher costs on holders of FX deposits could be seen as intruding on Peru's constitutional right to transact in foreign currencies. Staff also reiterated the need to develop other measures that could help de-dollarization, such as creating incentives for diversifying savings and investment instruments (e.g. deepening local-currency bond markets, and allowing retail sales of government bonds),[8] as well as continuing to move in the direction of allowing greater exchange rate flexibility.[9]

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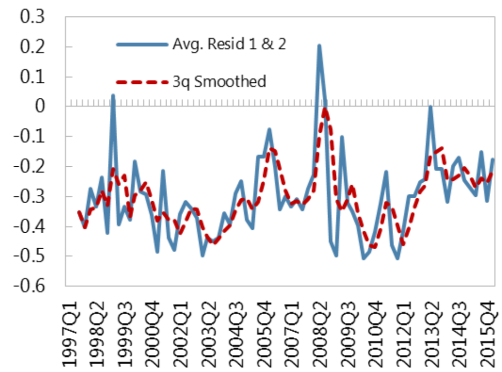
[7] Substitution repos, which carry some FX exposure for the BCRP, constitute 3 percent of the NIR.
[8] Local currency public domestic bonds are likely to become Euro-clearable in 2016, and authorities are working to develop real estate investment trusts (REITs) akin to the Mexican model. Modifications to the Alternative Securities Market scheme could also encourage higher issuances by medium-sized companies.

[9]See the accompanying *Selected Issues Paper*, Chapter 3.

14. Staff welcomed greater exchange rate flexibility but saw room for further flexibility. While continuing to lean against trend currency depreciation, the BCRP has been letting the sol absorb the decline in commodity prices, without a noticeable impact on firms' balance sheets. Exchange rate volatility has been higher than in previous non-crisis periods since 2013 even after controlling for external shocks, but most of the exchange rate depreciation in 2015 was limited to the U.S. dollar. Staff reiterated that, while temporary intervention to reduce excess volatility could be helpful, greater exchange rate flexibility would keep the current account balance closer to equilibrium levels, discourage risk taking, and incentivize the development of FX derivatives to support currency risk hedging. That would help de-dollarization and would limit the need for measures to alleviate banks' balance sheet mismatches. While macro-financial risks from FX lending appear limited—stress test calculations by the SBS suggest that only about 11 percent of FX lending poses risks to banks' capital, which is much below headline dollarization levels—FX leverage by firms and households still requires close monitoring (Annex III).

Residual USD/PEN Volatility 1/

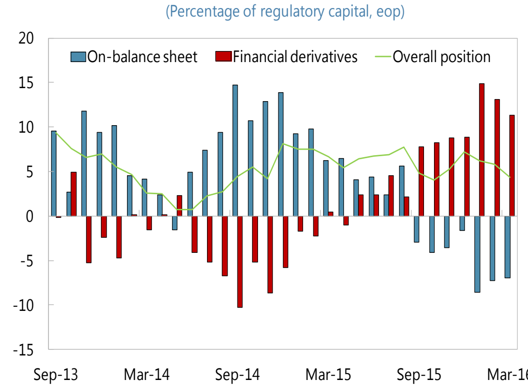


Sources: National authorities; and Fund staff calculations presented in accompanying Selected Issues Paper, Chapter 3.

1/ Adjusted for shocks in the terms of trade and the volatility index (VIX).

Financial System: FX Net Open Position

(Percentage of regulatory capital, eop)



Source: National authorities.

15. Staff supported the authorities' efforts to keep Peru's current classification in the MSCI Emerging Market index. Peru's growth rate and macroeconomic stability continue to stand out when compared to other emerging market economies and the country has been the recipient of significant foreign direct investment in the past decade. Reclassifying Peru into the MSCI frontier market index due to the perception of low liquidity (as has been contemplated by MSCI) would lead to a change in the investor base, but, even if regrettable, authorities believe it would not have significant macro-financial consequences. The Supervisor of the Stock Market (SMV) and the management of the Lima stock exchange (BVL) have been taking important steps to increase market liquidity, including a temporary exemption of the capital gains tax, to which the staff does not object, and providing stronger incentives for market makers and stock lending.

Selected Liquidity Improving Measures

Measure	Details
Exempt sales of shares from capital gains tax	Temporary exemption for 3 years. Applies to transactions with volumes that represent less than 10 percent of the company's total value and with a minimum traded volume of 4 UITs (approximately U.S.$ 4,700). 1/
Strengthen incentives for market makers	Modification of payments in advance tax scheme for market makers, and transaction fees of BVL, Central Register for Securities and Settlements (CAVALI), and SMV exempted until July 31, 2016.
Promote stock lending	Transaction fees of BVL, CAVALI, and SMV exempted for stock lending operations until July 31, 2016. Pension funds allowed to act as stock lenders.
Implement a new trading platform "Millennium"	The platform allows algorithmic trading via Direct Market Access, market making, stock lending, and short selling.

Source: Lima Stock Exchange.
1/ A "tax unit" (UIT) is a figure set annually by the tax authorities to determine applicable rates and deductions.

B. Ensuring Stability and Creating Fiscal Space

16. Projected under-execution of public capital spending suggests a broadly neutral fiscal stance in 2016, although staff stressed the importance of delivering the budgeted spending, excluding the provisions for a stronger *El Niño*. Under the escape clause, the 2016 deficit target was increased to 3 percent of GDP to support the economy and to accommodate provisions for a possibly stronger *El Niño*. As *El Niño* has now been downgraded, the authorities project the deficit not to exceed 2.5 percent of GDP. Staff estimates an even lower deficit (about 2¼ percent of GDP), making the fiscal stance neutral in structural terms. A projected small loss in income tax collection (following further rate cuts spread over 2015–19) is expected to be more than offset by lower current and capital spending, given lower historical execution of investment than budgeted, and the fact that this is a government transition year. Revenues could surprise on the upside if growth rises by more than projected. Staff advises the incoming government to concentrate on delivering the originally budgeted capital spending and resist surpassing the budgeted current outlays, since the economy is recovering, the external current account deficit is still high, and inflation expectations need to remain well-anchored. There was broad agreement with the current authorities that a significant fiscal impulse is not necessary given the economy's ongoing recovery.

17. With the output gap estimated to close around end-2017, staff supported fiscal consolidation starting next year in line with Peru's current fiscal rules. Effective delivery of budgeted capital spending is important to support medium-term growth and social objectives. However, any expansion of the expenditure envelope for infrastructure and social reforms beyond the current framework would require the creation of additional fiscal space through revenue generation, in order to preserve healthy debt dynamics and fiscal buffers. Staff reiterated Fund advice to reach a ½ percent of GDP primary surplus in the medium term. Such a target would stabilize the debt-to-GDP ratio well below 30 percent,[10] and protect the fiscal buffers necessary to shield Peru against natural disasters, commodity price shocks, and the risk of realization of contingent liabilities totaling 8 percent of GDP (including from public-private partnerships). It would also help ensure the sustainability of pensions and Peru's preparedness for longer-term demographic shifts.[11]

18. The newly elected Fiscal Council became operational in January 2016. As required by law, the Council provided a non-binding opinion on the three-year macro fiscal framework released in April 2016, which generally forms the basis for the following year's budget and the medium-term fiscal outlook. In the council's view, the authorities' medium-term estimates of growth in Peru are somewhat optimistic, especially given the difficult external environment. They recommended bigger adjustments in expenditures than projected to ensure fiscal sustainability and the credibility of the fiscal rule.

Peru: Current Fiscal Framework

	NFPS	National Government	Sub-National Governments
Budget Balance	Indicative Structural Deficit Target, up to 1 percent of GDP 1/	…	…
Expenditure	…	Level of primary spending consistent with the structural balance target for the nonfinancial public sector, given spending limits for subnational governments and projections for other entities of the nonfinancial public sector 2/ 3/ The growth rate of wage and pension spending cannot exceed the nominal growth rate of potential GDP	Primary spending growth at time *t* below the average revenue growth rate over the previous four years (from t-6)
Debt	Debt ceiling at 30 percent of GDP	…	Debt/(average of last 4 years revenue) <100 percent
Other	…	New permanent spending requires new permanent revenue sources	Restrictions on external borrowing

1/ The structural price for commodity prices is now estimated using a 15-year moving average, with 11 years backward, the current year, and 3 years forward of projections.
2/ The limit can rise by up to 0.2 percent of GDP in case of budget under-execution in the previous year. If the expected output gap (positive or negative) is larger than 2 percent, the expenditure limit must adjust, counter cyclically, by up to ¼ of the output gap or 0.5 percent of GDP. When new tax measures yield a permanent change in revenue of 0.3 percent of GDP or more, the expenditure limit changes accordingly.
3/ In the first seven months of election years, two additional limits apply: (1) budget execution of national government's primary spending cannot exceed 60 percent of the annual budget and; (2) no measures can be taken that increase future current spending or reduce the fiscal space for the future administration.

19. Peru's tax burden is low and policy efforts should focus on improving revenue collection while avoiding tax rate cuts. Peru has come a long way in improving the efficiency of the tax system but further efforts are needed to reap the full benefits from these reforms. Peru's tax-to-GDP ratio, slightly above 15 percent, remains below the regional average, and is even lower than this average if commodity-related income is stripped out. Staff discussed a number of areas where improvements can be achieved, based on recommendations from the substantial technical assistance provided in this area, and advised against further reductions in tax rates (Annex IV). The

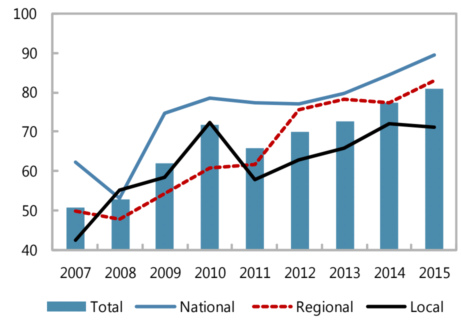
[10] See IMF Country Reports No. 14/21 and 22 for analysis.

[11] In this connection, it will also be important to follow closely the evolution of private savings as a recent law allows retirees to cash in 90 percent of their private pension funds instead of receiving the equivalent monthly pension for the rest of their lives. A fast depletion of these savings poses a social contingent liability to the public accounts.

tax agency (SUNAT) agreed with the proposals, and was receptive to the recommendations in the area of international taxation.[12] SUNAT has its own action plan to raise collections that will need to be supported through the introduction of complementary structural reforms, which would help formalize the economy. While not following through with revenue increases if boosting investment spending further could still keep debt-to-GDP ratios below the fiscal rule's 30 percent (Figure 8), this strategy would carry reputational risks and, if followed, would have to provide a credible medium-term anchor to stabilize debt dynamics.

20. Higher execution rates and efficiency of budgeted public investment are needed to support stronger economic activity. Despite a steady increase in execution rates over the past five years, reaching a record-high 82 percent in 2015, they still average 75 percent. Thus, it would be crucial to streamline a number of authorizations and permits, while still safeguarding the appropriate use of resources. While the public investment management (PIM) system compares favorably with those in neighbor countries and other peers, further strengthening is needed especially since investment efficiency also needs to be improved (Table 6, Box 4). Implementation capacity needs further improvement, especially at the sub-national level, including for project selection and quality assurance for large projects under the System of National Public Investment to ensure adequate returns from public investment, while assessment of small projects could also be centralized. Efforts should commence to prepare the new investment pipeline, so it is ready once current mega-projects (e.g., metro line, gas pipeline, highway, and airport) come to fruition. While investment could be increased through public private partnerships, as has been done in the past, a system of risk evaluation under the current framework should be enhanced to insure against contingent liabilities to the state.

Public Investment Spending
(Percent of budgeted amounts)



Source: Ministry of Economy and Finance.

[12] See the accompanying *Selected Issues Paper*, Chapter 4, and IMF Country Reports No. 15/133 and 134.

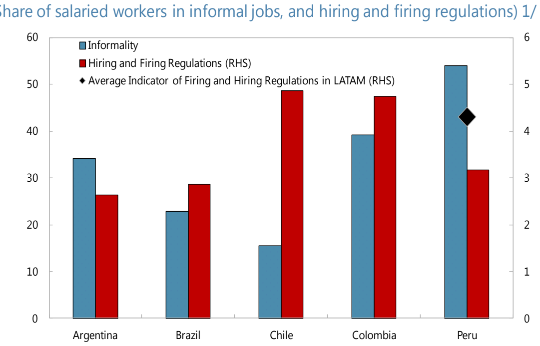
Summary of Recommendations

PIM	Decentralization
Adopt a multi-year budget with the objective of guaranteeing full execution of multi-year investments, including documentation on scheduled commitments, especially in public investment	Revisit the assignment of natural resource revenues through a set of more transparent and equitable transfer mechanisms
Improve cash flow management so as to minimize project implementation delays	Strengthen the efficiency of subnational investment and service delivery through further capacity building initiatives
Design an Information System to integrate the process of planning, budgeting and investment over the project cycle. Monitor all major projects during project implementation for annual project costs, as well as physical progress, and conduct and publish external ex-post audits	Consider merging jurisdictions and reallocate resources away from low-capacity districts to avoid waste and seek efficiency from economies of scale
While information is available on the total cost of each project and the amount invested to date, the national planning system (SNIP) could be updated in a more timely fashion, especially with information on the stage of project execution at the municipal level	Centralize the assessment and selection of investment projects and decentralize their execution

C. More Growth and Less Income Inequality: How to Get There?

Informality and Labor Market Regulations

(Share of salaried workers in informal jobs, and hiring and firing regulations) 1/ 2/

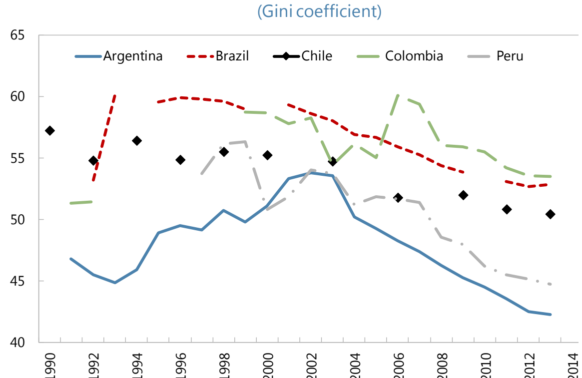


Sources: Socio-Economic Database for Latin America and the Caribbean; and Fraser Institute.
1/ A worker is considered informal if (s)he does not have the right to a pension when retired.
2/ Based on the Global Competitiveness Report question: "The hiring and firing of workers is impeded by regulations (= 1) or flexibly determined by employers (= 7)."

21. The agenda for growth-spurring structural reforms is multi-pronged and should not be postponed. Based on discussions with various stakeholders, staff emphasized the need to (i) reduce informality, including through labor market reforms; (ii) introduce measures to boost investment in non-extractive industries; and (iii) increase competitiveness of Peruvian corporations through reducing red tape and improving infrastructure, while preserving the integrity of the fiscal base. Peru has the highest rate of informal employment among LA5 countries, and strong regulatory constraints that preclude more dynamic job creation in the formal sector. Labor market reforms should introduce more flexibility in hiring and firing decisions. The authorities indicated that the accession process to the OECD could play a key role in triggering reforms, especially in the labor market, and that for the first time since the mid-1990s, there will be a congressional majority that may see such reforms favorably. However, they also saw the current social mood as a risk to a fast pace of reforms. According to many stakeholders, Peru is well placed to reap the full benefits from free trade agreements, including the TPP (through direct access to new markets, higher exports to current trading partners, and innovation and job creation as regulatory systems of TPP nations become compatible); the effect of the TPP on potential growth could be material if accompanied by the supporting domestic reforms mentioned above. Possible revenue losses from the requirement of eliminating 60 percent of nonzero tariffs would be very small and could be offset by correcting weakness in tax collections and closing loopholes.

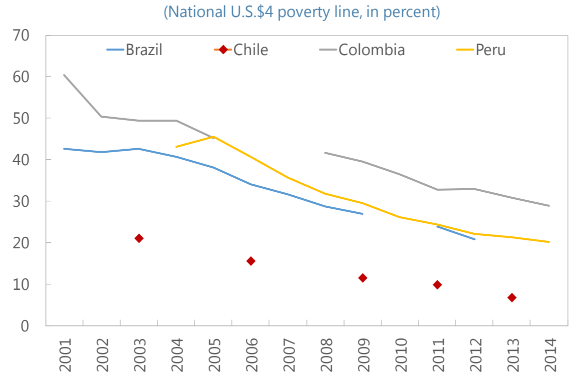
22. Despite significant progress in poverty reduction and inclusion, further efforts are necessary to improve social indicators and, thus, potential growth. Over the past year, the poverty rate fell by ½ percentage point to 21.8 percent. The five main programs of targeted assistance have been delivering important results such as higher student enrollment, reduced malnutrition, and greater integration of women into the labor force, and the authorities' objectives going forward continue to be ambitious. Peru has also achieved one of the highest rates of education coverage in Latin America through radical reforms in the sector. These reforms should continue in full force to further improve the still-low quality of education (measured by student test scores and teachers' proficiency tests), reach higher staffing levels, and address the widespread lack of adequate facilities. The National Financial Inclusion strategy launched in July 2015 sets targets for financial inclusion; and the interoperable mobile money platform—a private sector-led initiative—could help to achieve them (Box, Annex III). Staff commended the authorities for their efforts and agreed that these areas should continue to be an integral part of the next government's development and inclusion strategy.

Inequality in Selected Latin American Countries
(Gini coefficient)



Sources: World Development Indicators.

Poverty Rate
(National U.S.$4 poverty line, in percent)



Sources: World Bank.

STAFF APPRAISAL

23. After decelerating sharply in 2014, economic activity recovered last year despite a volatile external environment. The recovery largely reflected additional mining production capacity coming on stream, although non-mining activity has also accelerated modestly more recently. An expected increase in mining exports, together with some rebound in public investment, will impart a strong positive impetus on growth going forward, which should spillover to non-commodity sectors. Thus, despite sluggish external conditions, activity is expected to accelerate further in 2016 and 2017, while inflation continues to decline.

24. Risks to the outlook are balanced. External pressures have carried over from last year and comprise possibly weaker-than-projected growth in China (and, hence, softer metal prices), possible adverse spillovers from other countries in the region (though these should be relatively small), sharp asset price adjustments in advanced and emerging economies, and an even stronger dollar. The response to shocks should be through further exchange rate flexibility and easing liquidity conditions to support credit activity. Upside domestic risks include stronger-than-expected improvements in business confidence (especially if the incoming government announces decisive productivity-enhancing reforms) and a more effective execution of the existing pipeline of infrastructure projects, which could lift growth further in 2016–17 and beyond.

25. Monetary and exchange rate policies should remain attentive to rapidly changing conditions. Following monetary tightening, the BCRP should now maintain a wait-and-see stance—given declining inflation and medium-term inflation expectations, the fact that it is too soon to evaluate the effect of past monetary tightening on economic activity and inflation, and the usual uncertainties surrounding the exact cyclical position of an economy. This said, a possibly steeper interest rate path in the United States than currently priced by the financial market could trigger the need for further monetary tightening in Peru. Greater exchange rate flexibility in 2015 was a welcome development with no noticeable impact on firms' and banks' balance sheets; the latter remain healthy and profitable. Further decline in credit de-dollarization has been achieved not least due to the measures introduced by the BCRP. Further exchange rate flexibility would support the development of hedging instruments to reduce currency risk and help accelerate the de-dollarization process. Recent measures to deepen Peru's equity market are also welcome.

26. A gradual fiscal consolidation in the next few years is advisable to maintain healthy debt dynamics and to protect fiscal buffers. With the output gap closing around end 2017, there is no case for loosening fiscal policy. A gradual fiscal consolidation would be important for ensuring the sustainability of pensions, and defending against natural disasters and realization of contingent liabilities. To accommodate higher-than-projected public capital spending, it will be critical to create adequate fiscal space through containing current spending that is not complementary to capital expansion and structural reforms (including in health and education), and raising the low revenue collection through streamlining administration, reducing informality and exemptions, and protecting Peru's tax base from possible international profit shifting by multinational corporations. Reducing bottlenecks to public investment and improving management would go a long way toward enabling full execution of budgeted spending and would support private investment.

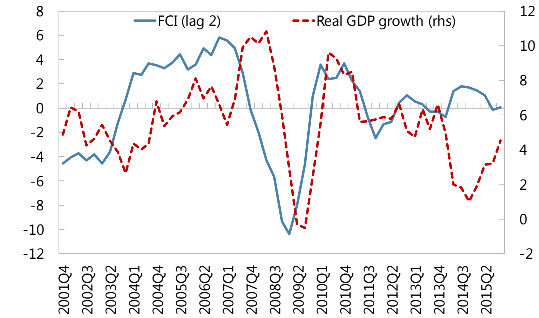
27. With the end of commodity-driven growth, the agenda for growth-spurring structural reforms has become a higher priority, including for further poverty reduction. Investments in capital and labor will be needed to boost potential growth, which is otherwise estimated to be 3½ percent in the absence of continued reforms. Long-standing challenges include reducing informality, which should be in part addressed through labor market reforms aiming at lowering the costs of hiring and firing workers, and spurring investment in non-extractive industries, including through improving competitiveness and infrastructure. Peru's current decentralization framework should be improved, as it constrains full execution of planned capital expansion and better allocation of resources. While Peru has achieved one of the highest rates of education coverage in Latin America, the low quality of education remains a crucial challenge, and the ongoing reforms will need to continue. Efforts to raise financial inclusion are commendable, especially through the launch of the broad-based National Financial Inclusion Strategy and the private sector-led e-money platform. Free trade agreements also provide an opportunity for boosting and diversifying long-term growth.

28. Staff would like to relay their appreciation to the outgoing administration for the constructive dialogue and look forward to working with the new government. It is expected that the next Article IV consultation will take place on a 12-month cycle.

Box 1. Peru: Assessment of Financial Conditions

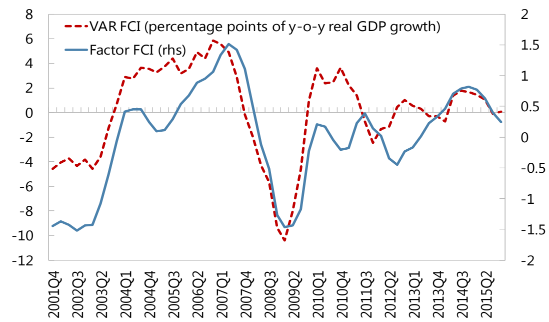
A Financial Conditions Index (FCI) provides a quantitative assessment of overall financial conditions in the economy. The index considers different transmission channels from monetary policy to financial variables (e.g., spreads, exchange rate, asset prices, etc.) that influence the future state of the economy. The FCI can also be used to compare the relative stance of financial conditions in different periods of time.

FCI and GDP Growth
(Percentage points of yy real GDP growth)



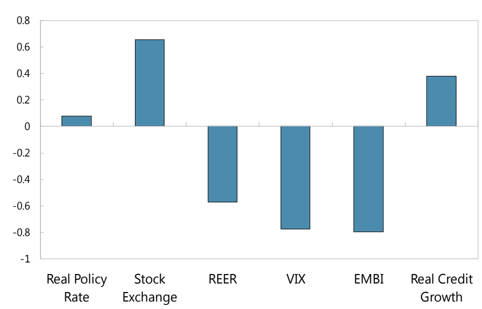
Staff's FCI is constructed using two approaches. In the first approach, the weights of each financial indicator are assigned according to their estimated impact on real GDP growth from a Vector Autoregression (VAR) model. In the second approach, a common factor is estimated from a group of several financial variables and interpreted as the unobserved common component underlying the movements in those variables. The FCIs were constructed using quarterly data from 2001 to 2015, with increases signaling more accommodative financial conditions. An upward movement of the index implies more accommodative overall financial conditions, whereas a decline indicates tighter financial conditions.

Financial Conditions Index



The two indices follow a similar trajectory, but the VAR-based FCI has a somewhat higher correlation with two-quarter-ahead, year-over-year, real quarterly GDP growth (0.57). Financial conditions were relatively easy between mid-2014 and mid-2015, mostly owing to the contributions of the real policy rate and external financial conditions. By the end of 2015, the contribution of the FCI to real GDP growth declined but remained marginally positive. Despite increases in the policy interest rate since September 2015, most of the tightening in financial conditions since mid-2015 comes from abroad. As of March 2016, financial conditions are still sligthly supportive of growth until the fall of 2016, contributing 0.3 percentage points to annualized qoq growth.

Factor Loading in FCI



Source: Fund staff calculations.

Box 2. Peru: Risk Assessment Matrix[1]

	Likelihood	*Impact*	*Policy Advice*[2]
		Country-specific risks	
Further improvement in business confidence and a pick-up in public investment execution	H	M (↑) A positive boost to domestic demand through consumption and investment.	Keep up the confidence with the acceleration of structural reforms and capacity building.
Protracted period of weak domestic investment	M	M (↓) Investment could be affected by uncertainties stemming from external conditions, slow structural reforms, and social discontent.	Persevere with structural reforms, especially those aimed at increasing investment potential; and keep up efforts to advance social inclusion.
Fiscal expansion that undermines the fiscal rule	L	M (↓) This would erode important fiscal buffers.	Current spending path should follow the current framework (consolidation), and any increase in productive capital spending should be financed with higher fiscal revenues. Ensure effectiveness of spending by implementing reforms to PIM.
		External risks	
Structurally weak growth in key advanced and emerging economies/Significant China slowdown. Weak domestic demand in China further suppresses commodity prices, roils global financial markets, and reduces global growth (short-term)	H/L	M/M (↓) Continuing slowdown in global demand would lead to a worsening current account deficit and weaker growth, especially through lower exports, both in prices and volume.	Exchange rate flexibility as first line of defense and use of liquidity buffers. Ease monetary and prudential policies. Accelerate structural reforms.
Surge in the U.S. dollar	H	H (↓) Balance sheets will be strained for dollar debtors.	Exchange rate flexibility, while intervening to smooth excessive volatility, developing a market in hedging instruments so agents can internalize risks in the absence of the central bank intervention.
Sharp asset price decline and decompression of credit spreads	M	M (↓) Peru 's risk premia would increase; there could be pressures on the sol and capital outflows. Yields could increase in domestic bond markets together with potential crowding out of companies of domestic private credit. FDI flows could slow down further, which would affect growth outlook as FDI was key to financing large current account deficits and fostering growth.	Exchange rate flexibility and use of liquidity buffers. Persevere with measures to further reduce financial dollarization while improving data collection and analysis of private sector balance sheets. Unwind further macro prudential measures through lowering the ceiling on average reserve requirements on domestic liabilities and reserve requirements on foreign currency liabilities.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

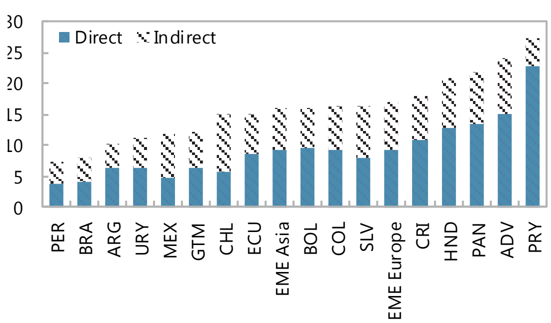
[2] Recommended by staff.

Box 3. Peru: Exchange Rate Pass-Through to Inflation[1]

The BCRP considers that the rising U.S. dollar explained 2/3 of inflation in 2015, with a exchange rate pass-through (ERPT) coefficient of 0.16 percentage point (pp) for a 1-percent depreciation of the sol. IMF staff has followed two research strategies to estimate the extent of ERPT to inflation in Peru.

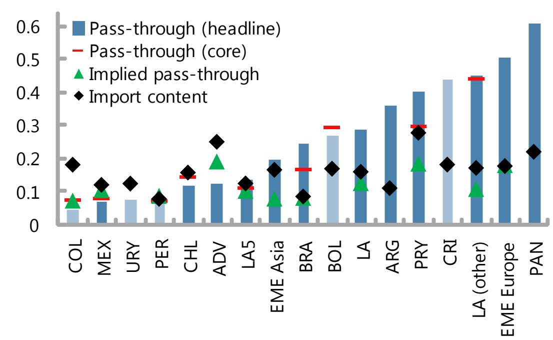
First, staff has analyzed how movements in the nominal effective exchange rate (NEER) would affect inflation in Latin American (LA) countries using a uniform cross-country methodology, as described in the Spring 2016 Regional Economic Outlook for the Americas (REO). This analysis suggests that the ERPT is low in LA. If inflation expectations are well-anchored and the ERPT to import prices is complete, the ERPT to inflation should be close to the import content of consumption, which is relatively low in Latin America. An econometric analysis shows that countries with an inflation targeting (IT) framework and with flexible exchange rates exhibit even lower ERPT. For example, the pass-through for IT emerging countries is 16 percent, while it is 52 percent for non-IT emerging countries. Peru is a case in point, with the lowest import content in the region and a statistically insignificant ERPT. With an ERPT point estimate of only about 0.06, the small NEER depreciation in 2014–2015 would have contributed marginally to the inflation increase.

Import Content of Households' Final Demand
(In percent)



Sources: Eora MRIO; and Fund staff calculations.
Note: The direct import content corresponds to imports of final consumption goods, while the indirect import content accounts for the value of imported inputs used in the production of domestically produced goods that are consumed by domestic households.

ERPT to Headline and Core Prices
(In percent)



Source: IMF staff calculations.
Note: Cumulative exchange rate pass-through to consumer prices two years after a one percent increase in the effective exchange rate. "Implied pass-through" corresponds to the product of the cumulative exchange rate pass-through to import prices after two years and the "import content" of domestic consumption. Solid bars denote statistically significant responses at the 10 percent confidence level.

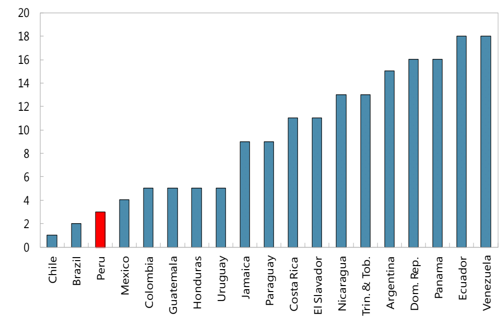
However, many contracts in Peru are set in U.S. dollars and a focus on an aggregate econometric strategy using NEER could miss the effect of movements in the bilateral exchange rate on particular consumer price categories. Estimates of ERPT for large CPI groupings using the most relevant exchange rate definition for each category (for instance, the US$/sol for rent and electricity fares, but the NEER for food products and clothing) show a higher and statistically significant overall ERPT of about 0.1 for the Peruvian economy. Once the larger depreciation of the sol with respect to the U.S. dollar since December 2014 (14 percent) is taken into account, staff estimates that ERPT accounted for about 50 basis points of the year-over-year inflation increase in Peru from December 2014 (3.2 percent) to December 2015 (4.4 percent), still below the authorities' estimates.

[1] See REO Chapter 3 for methodology and calculations.

Box 4. Peru: Public Investment Management (PIM) and Investment Efficiency[1]

Fiscal policy in Peru has played a crucial role in post-1990 stabilization. Deep structural reforms resulted in the creation and strengthening of institutions, including PIM. Private sector investment was crowded-in through the Public-Private Partnership framework, which is now considered to be one of the most developed in Latin America.

Overall PPP Environment
(Rank, 1=highest)

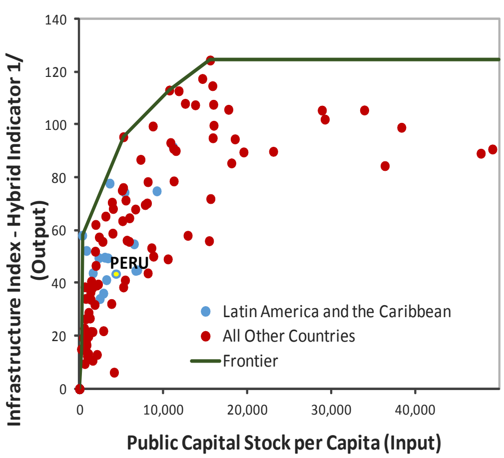


Source: Infrascope 2014 (Economist Intelligence Unit).

Given higher multipliers of capital spending (Chapter 2, accompanying *Selected Issues Paper*), Peru tried to provide an investment-led stimulus when growth slowed. However, efforts were largely derailed by bureaucratic and regulatory hurdles, lingering weaknesses in PIM, and the unfinished decentralization process which hampered spending at the local level.

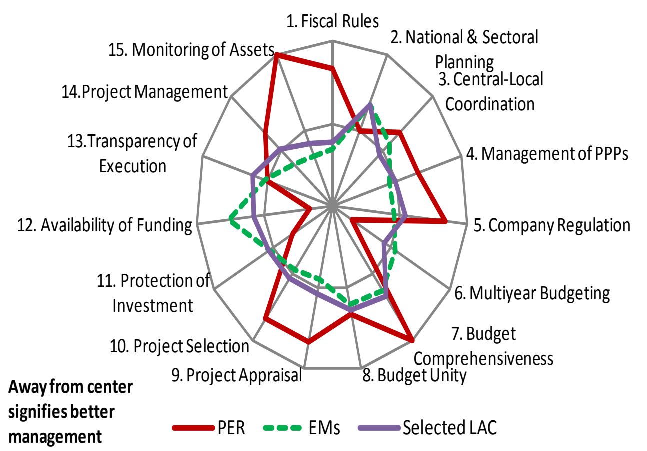
Important improvements will be necessary to achieve a greater bang for every sol invested. So far, Peru is placed at 112th place out of 140 countries for quality of overall infrastructure by the World Economic Forum. Staff estimates of public investment efficiency also points to sub-par outcomes. The PIM system will need to be improved, especially in the areas of multiyear budgeting and national and sectoral planning.

Efficiency Frontier (Hybrid Indicator)



Sources: Center for International Comparisons (2013), World Economic Forum (2014), OECD (2014), World Economic Outlook, World Development Indicators, and Fund staff estimates.
1/ Combines the physical and survey based indicators into a synthetic index of the coverage and quality of infrastrcuture networks.

Strength of Public Investment Management by Institution

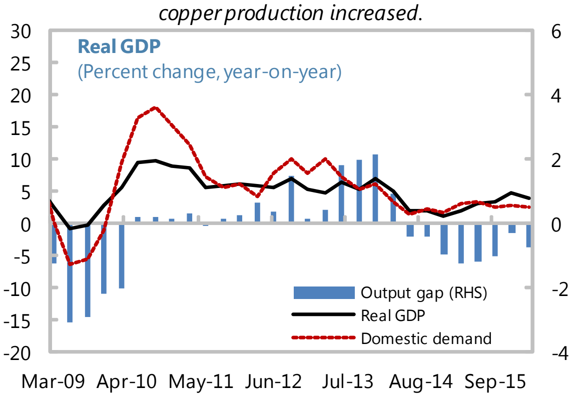


Source: Fund staff calculations on based on FAD and desk surveys of 12 EMS and LAC countires (Argentina, Bahamas, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Grenada, Guatemala, Honduras, Jamaica, Mexico, Panama, Paraguay, and St. Lucia.) Survey for Peru was conducted with the inputs from the Ministry of the Economy and Finance.

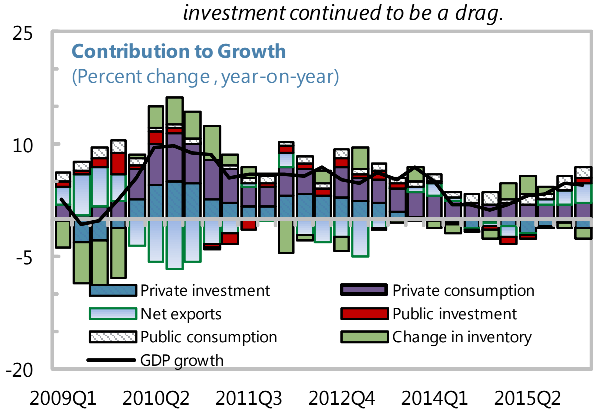
[1] See Chapter 2, in the accompanying *Selected Issues Paper*. 2016 Regional Economic outlook Chapter 5 provides regional comparisons on infrastructure efficiency and PIM.

Figure 1. Peru: Real Sector Developments

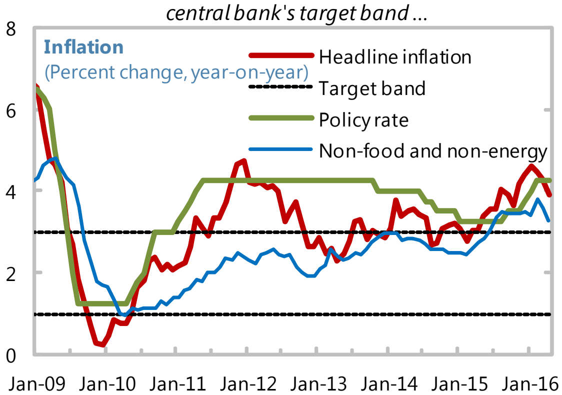
Economic growth rebounded as supply shocks unwound and copper production increased.



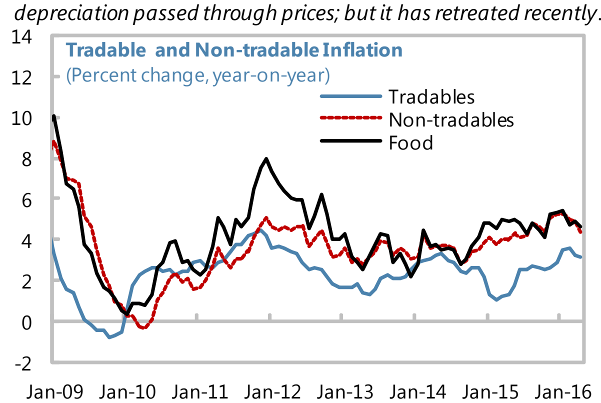
Consumption helped sustain growth, while private investment continued to be a drag.



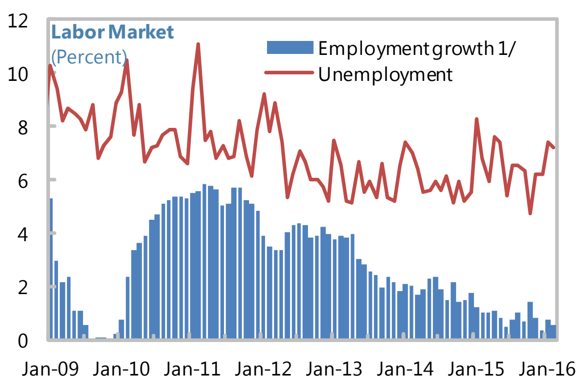
Inflation increased significantly above the upper limit of the central bank's target band…



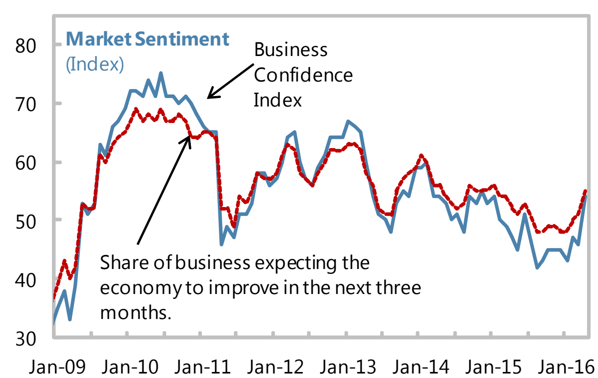
…as food and energy price inflation picked up, and exchange rate depreciation passed through prices; but it has retreated recently.



Employment growth has remained moderate…

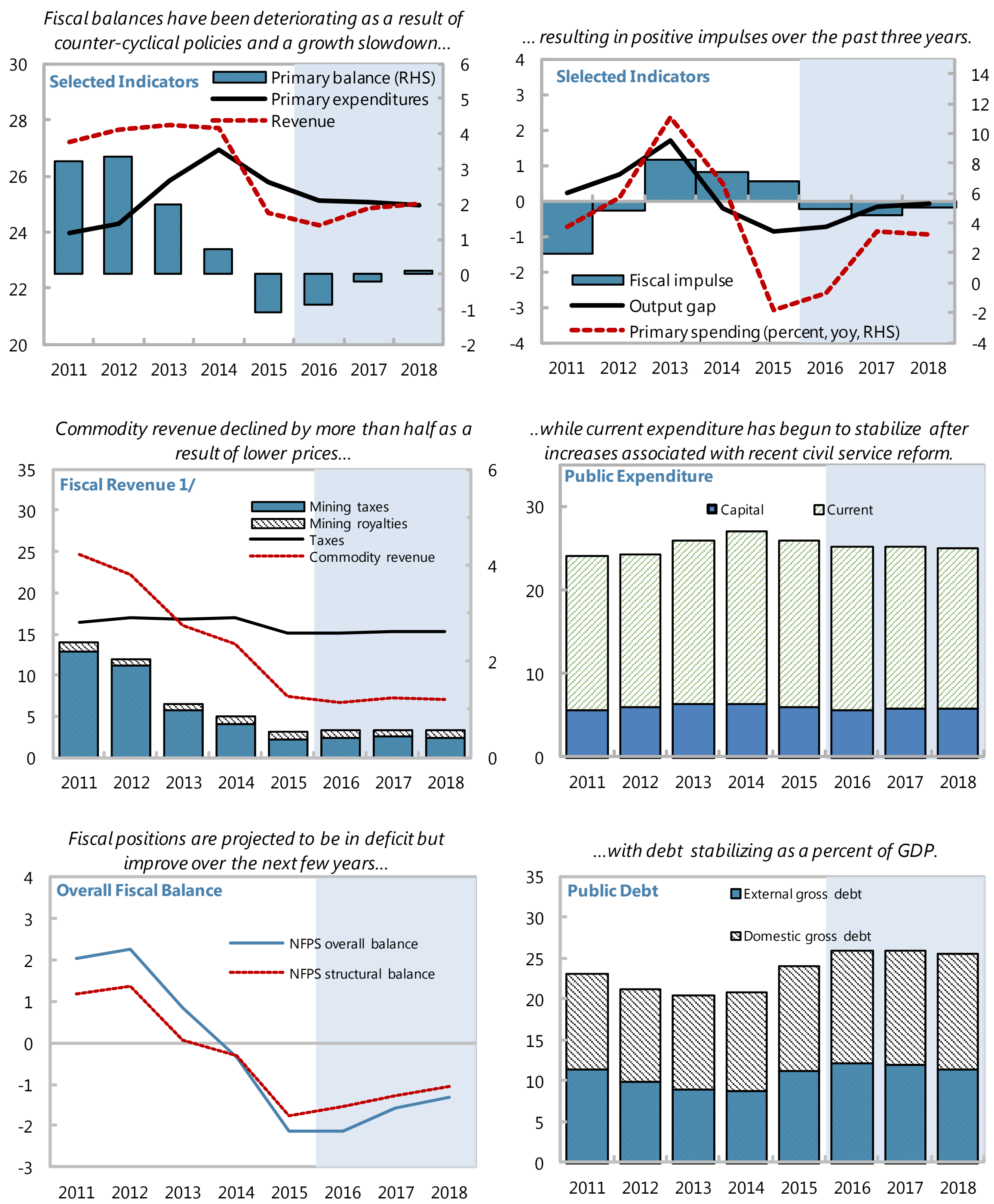


…while market sentiment has recently improved.



Sources: National authorities; and Fund staff calculations.
1/ In firms with 10 or more employees, all urban areas.

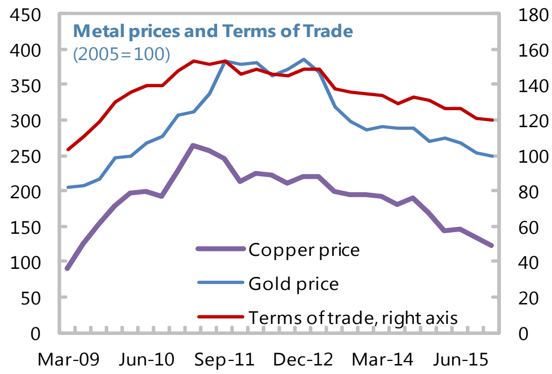
Figure 2. Peru: Fiscal Sector Developments
(Percent of GDP)



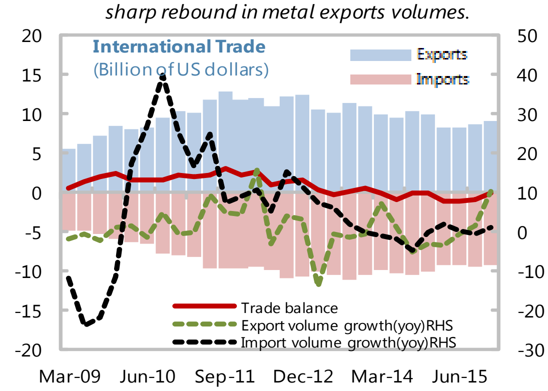
Sources: National authorities; and Fund staff estimates.
1/ Net of restitutions.

Figure 3. Peru: External Sector Developments

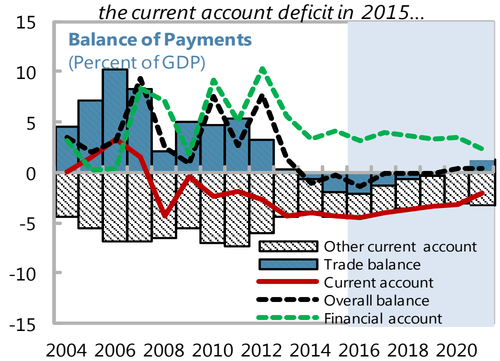
Metal prices and terms of trade have continued to deteriorate…



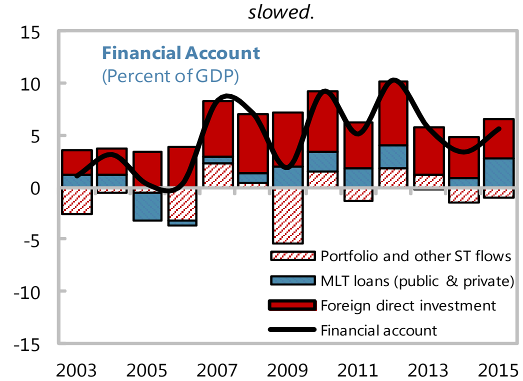
… leading to lower exports for the year, despite a sharp rebound in metal exports volumes.



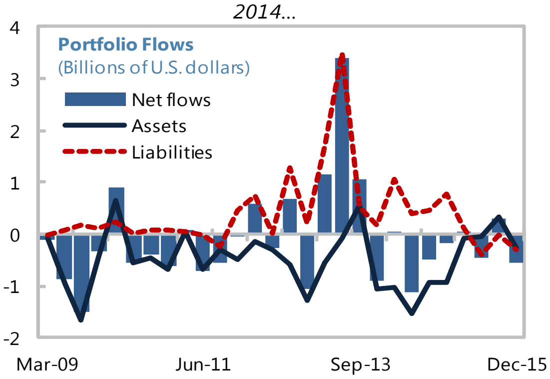
Long-term capital inflows were sufficient to finance the current account deficit in 2015…



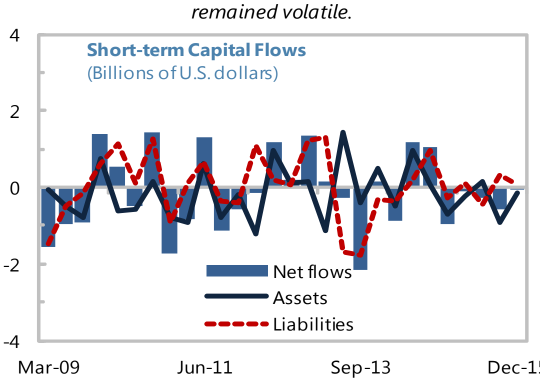
…thanks to higher public and private borrowing, as FDI slowed.



But the pace of outflows moderated compared to 2014…



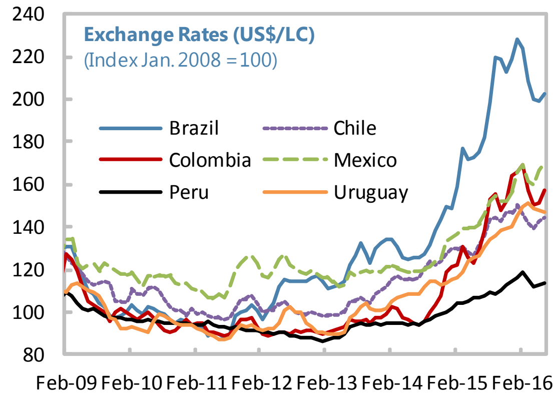
… while short-term capital flows remained volatile.



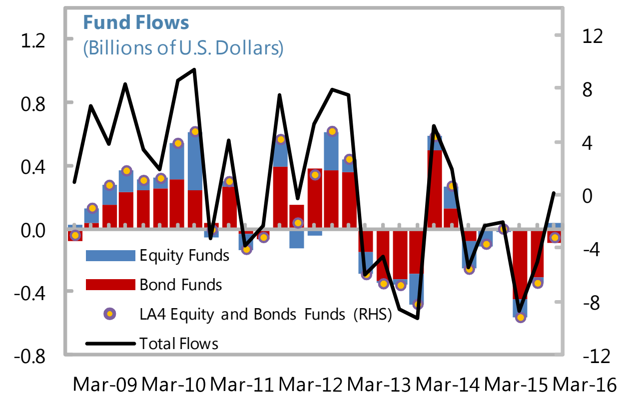
Sources: National authorities; and Fund staff estimates.

Figure 4. Peru: FX and Capital Market Developments

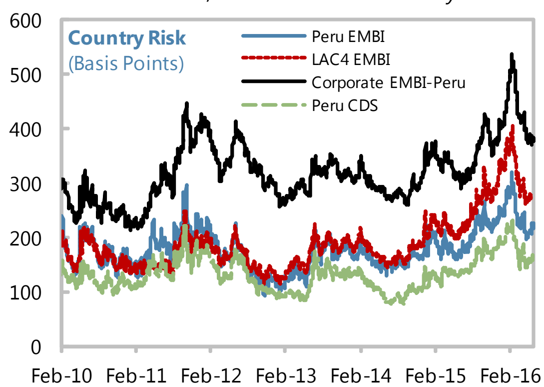
The sol depreciated steadily in 2015.



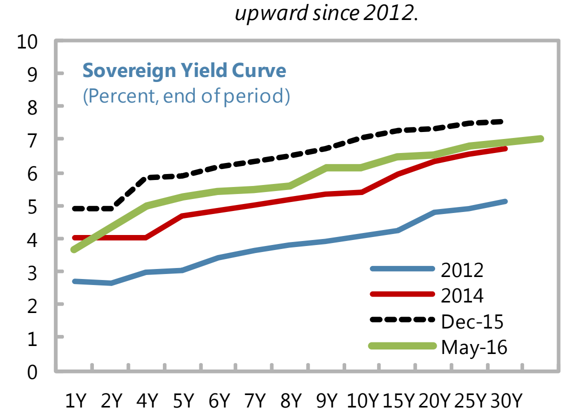
Bond and equity flows retreated in 2015.



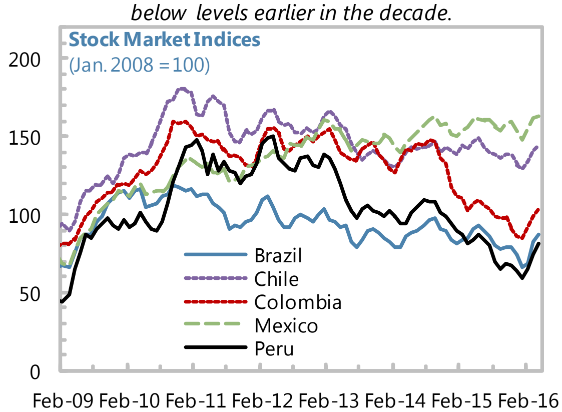
Spreads rose in 2015, in line with other regional economies, but have receded recently…



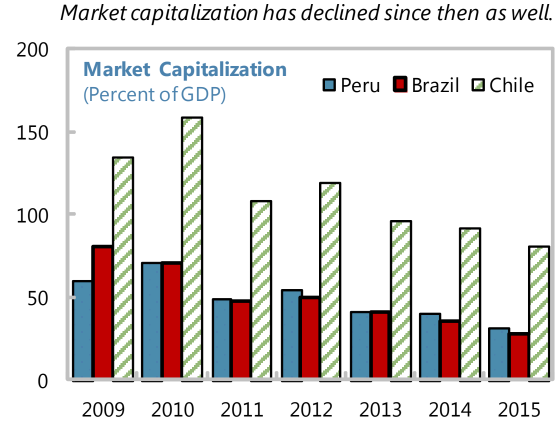
…and the sovereign bond yield curve has shifted upward since 2012.



Equity prices have rebounded recently but continue below levels earlier in the decade.

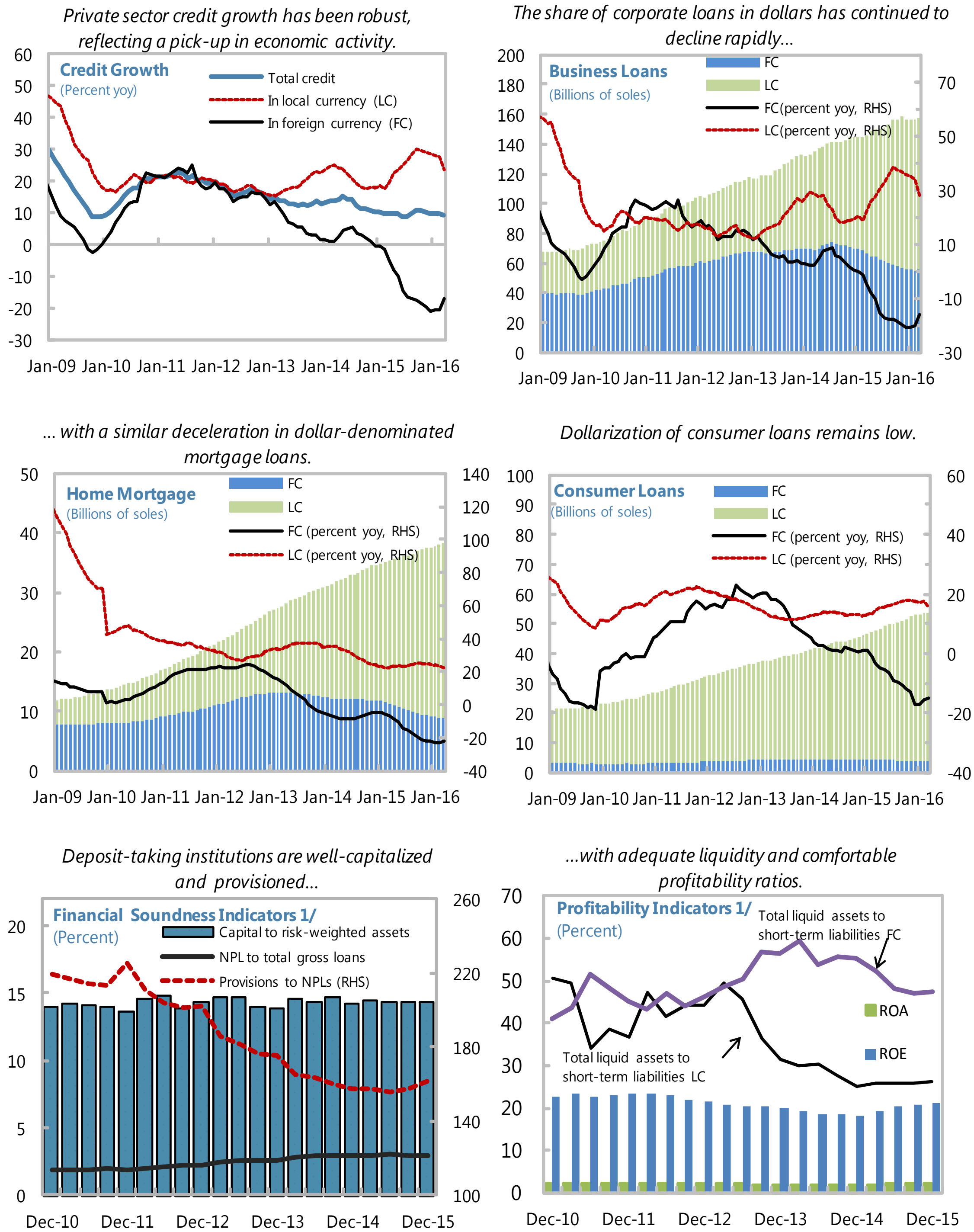


Market capitalization has declined since then as well.



Sources: Bloomberg Haver Analytics; National authorities; and Fund staff estimates.

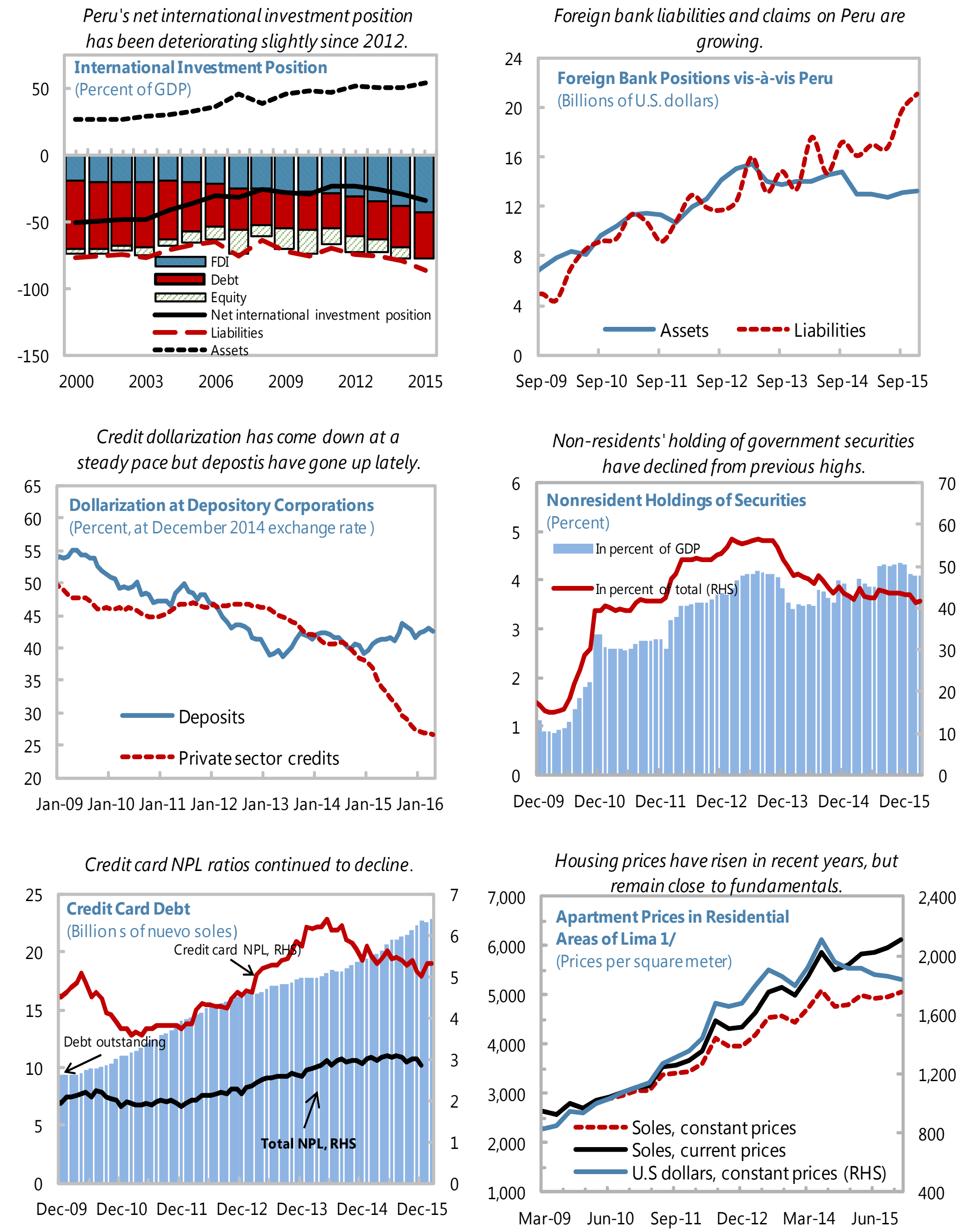
Figure 5. Peru: Financial Sector Developments



Sources: National authorities; and Fund staff estimates.

1/ Data corresponds to depository corporations. Last data available is for Dec-2015.

Figure 6. Peru: Balance Sheet Indicators



Sources: National authorities; Association of Banks; Bank for International Settlements; and Fund staff estimates.

1/ La Molina, Miraflores, San Borja, San Isidro, and Surco.

Figure 7. Peru: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators 1/

	Actual	Prel.		Projections					
	2010-2013 2/	2014	2015	2016	2017	2018	2019	2020	2021
Nominal gross public debt	22.5	20.7	23.1	25.3	25.5	25.4	25.2	25.1	24.9
Public gross financing needs	0.6	1.8	3.2	3.6	3.3	2.8	3.0	3.2	1.9
Real GDP growth (in percent)	6.7	2.4	3.3	3.7	4.1	3.6	3.5	3.5	3.5
Inflation (GDP deflator, in percent)	2.8	3.2	3.5	3.1	2.5	2.5	2.5	2.5	2.5
Nominal GDP growth (in percent)	10.6	5.5	6.3	5.1	6.2	6.2	6.1	6.1	6.5
Effective interest rate (in percent) 4/	5.2	5.6	5.6	5.8	6.1	6.1	6.0	6.7	6.8

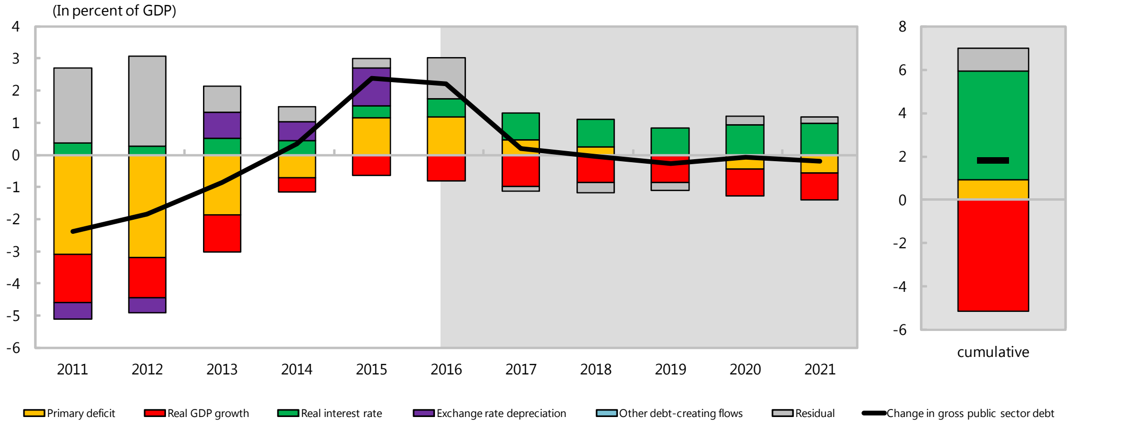
As of December 31, 2015		
Sovereign Spreads		
Spread (bp) 3/		248
CDS (bp)		188
Ratings	Foreign	Local
Moody's	A3 positive	A3 positive
S&Ps	BBB+ stable	A stable
Fitch	BBB+ Stable	A Stable

Contribution to Changes in Public Debt

	Actual	Prel.		Projections							
	2010-2013	2014	2015	2016	2017	2018	2019	2020	2021	cumulative	debt-stabilizing primary balance 9/
Change in gross public sector debt	-2.0	0.4	2.4	2.2	0.2	-0.1	-0.3	-0.1	-0.2	1.8	
Identified debt-creating flows	-3.4	-0.1	2.1	1.6	0.3	0.2	0.0	-0.3	-0.4	1.5	
Primary deficit	-2.3	-0.7	1.2	1.2	0.5	0.3	0.0	-0.4	-0.6	0.9	0.2
Primary (noninterest) revenue and grants	27.0	27.6	24.7	24.4	24.8	24.7	24.8	24.9	24.9	148.6	
Primary (noninterest) expenditure	24.8	26.9	25.9	25.6	25.3	25.0	24.8	24.5	24.4	149.5	
Automatic debt dynamics 5/	-1.2	0.6	0.9	0.4	-0.1	0.0	0.0	0.1	0.2	0.6	
Interest rate/growth differential 6/	-1.0	0.0	-0.3	-0.2	-0.1	0.0	0.0	0.1	0.2	-0.1	
Of which: real interest rate	0.5	0.4	0.4	0.6	0.8	0.9	0.8	1.0	1.0	5.0	
Of which: real GDP growth	-1.5	-0.5	-0.6	-0.8	-1.0	-0.9	-0.8	-0.8	-0.8	-5.2	
Exchange rate depreciation 7/	-0.2	0.6	1.2	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other debt-creating flows (specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes 8/	1.4	0.5	0.3	1.3	-0.1	-0.3	-0.2	0.2	0.2	1.1	

Debt-Creating Flows

(In percent of GDP)



Sources: National authorities and Fund staff estimates.

1/ Public sector is defined as non-financial public sector.

2/ Based on available data.

3/ Bond Spread over U.S. Bonds.

4/ Defined as interest payments divided by debt stock at the end of previous year.

5/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the denominator in footnote 4 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

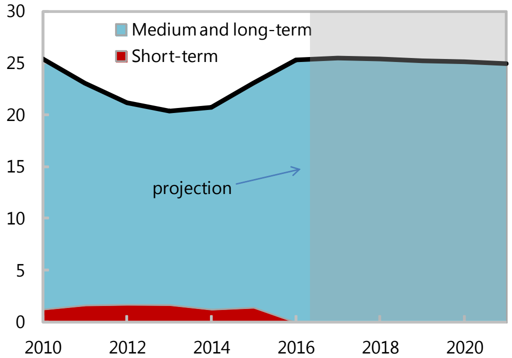
8/ For projections, this line includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 8. Peru: Public DSA—Composition of Public Debt and Alternative Scenarios

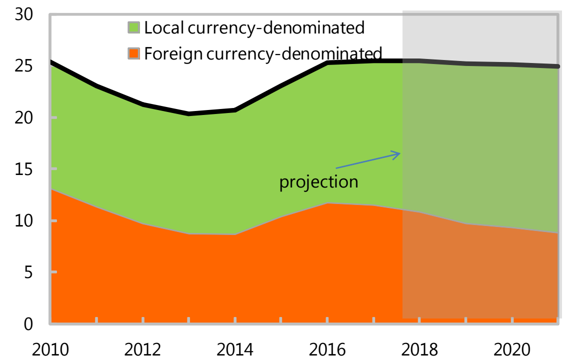
By Maturity

(In percent of GDP)



By Currency

(In percent of GDP)

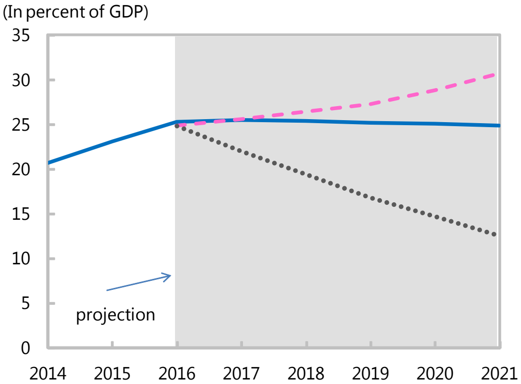


Alternative Scenarios

Baseline Historical Constant Primary Balance

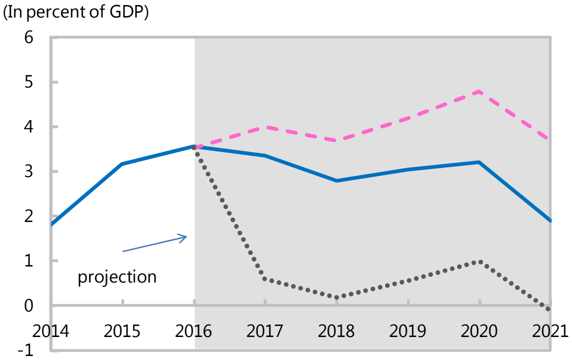
Gross Nominal Public Debt

(In percent of GDP)



Public Gross Financing Needs

(In percent of GDP)



Underlying Assumptions

(In percent)

Baseline Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	3.7	4.1	3.6	3.5	3.5	3.5
Inflation	3.1	2.5	2.5	2.5	2.5	2.5
Primary Balance 1/	-1.2	-0.5	-0.3	0.0	0.4	0.6
Effective interest rate	5.8	6.1	6.1	6.0	6.7	6.8
Constant Primary Balance Scenario						
Real GDP growth	3.7	4.1	3.6	3.5	3.5	3.5
Inflation	3.1	2.5	2.5	2.5	2.5	2.5
Primary Balance	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2
Effective interest rate	5.8	6.1	6.0	5.8	6.2	6.2

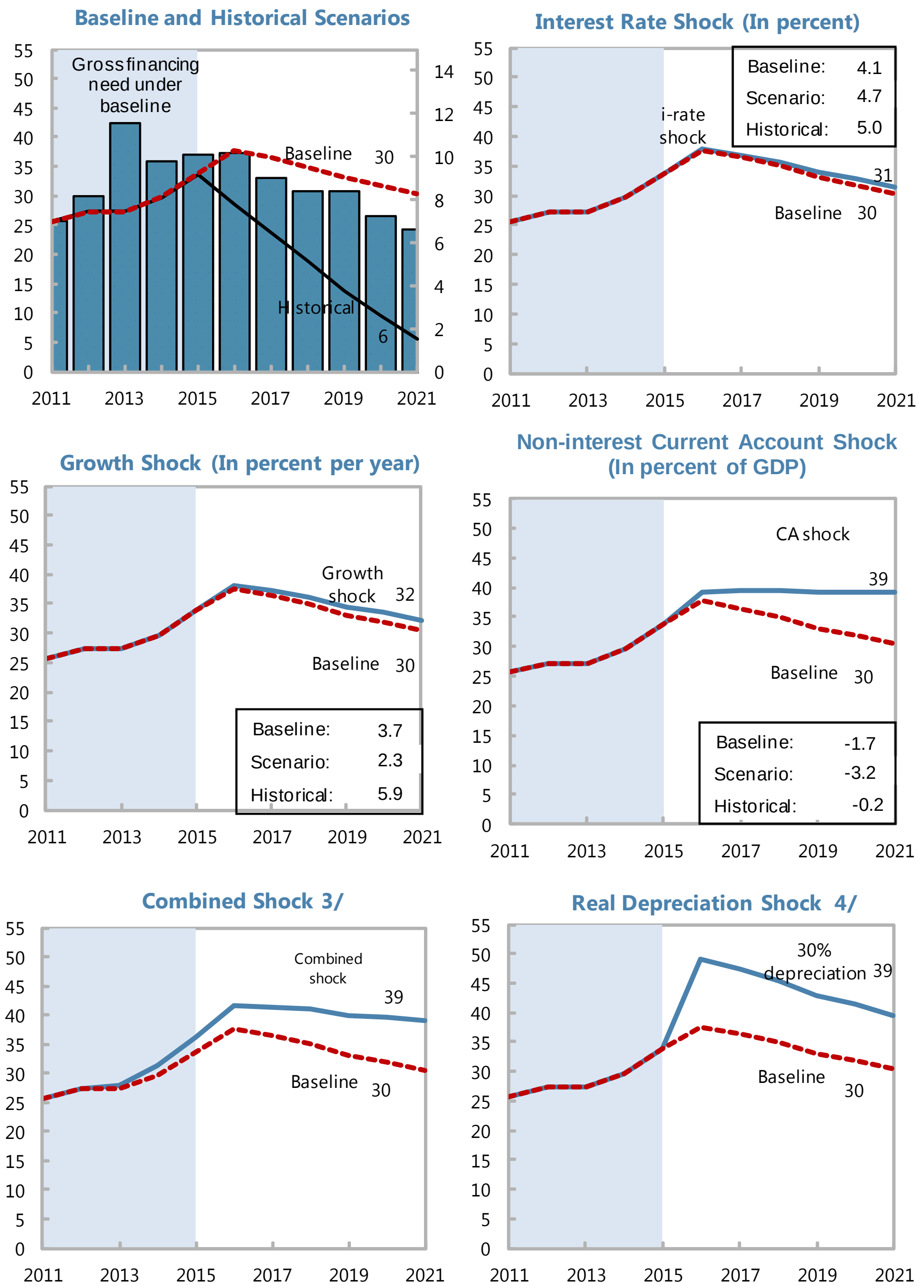
Historical Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	3.7	5.9	5.9	5.9	5.9	5.9
Inflation	3.1	2.5	2.5	2.5	2.5	2.5
Primary Balance	-1.2	2.2	2.2	2.2	2.2	2.2
Effective interest rate	5.8	6.1	6.6	7.1	8.6	9.6

Source: Fund staff estimates.

1/ Excludes interest income.

Figure 9. Peru: External Debt Sustainability: Bound Tests 1/ 2/

(In percent of GDP)



Source: Fund staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2016.

Table 1. Peru: Selected Economic Indicators

						Proj.					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Social Indicators											
Life expectancy at birth (years) 1/	73.8	74.0	74.2	74.4	74.6	...	...	...	...	...	...
Infant mortality (per thousand live births)	16.0	17.0	16.0	17.0	17.6	...	...	...	...	...	...
Adult literacy rate 1/	92.9	93.8	93.8	93.7	...	...	...	...	...	...	...
Poverty rate (total)	27.8	25.8	23.9	22.7	21.8	...	...	...	...	...	...
Unemployment rate	7.7	6.8	5.9	5.9	6.5	...	...	...	...	...	...
					(Annual percentage change; unless otherwise indicated)						
Production and prices											
Real GDP	6.5	6.0	5.9	2.4	3.3	3.7	4.1	3.6	3.5	3.5	3.5
Real domestic demand	7.7	7.2	7.3	2.2	2.9	2.3	3.3	3.2	3.3	3.4	3.4
Output gap (percent of potential GDP)	0.2	0.7	1.7	-0.2	-0.9	-0.7	-0.2	-0.1	0.0	0.0	0.0
Consumer prices (end of period)	4.7	2.6	2.9	3.2	4.4	3.2	2.5	2.5	2.5	2.5	2.5
Consumer prices (period average)	3.4	3.7	2.8	3.2	3.5	3.8	2.5	2.5	2.5	2.5	2.5
External sector											
Exports	29.5	2.2	-9.6	-7.8	-13.4	-1.0	7.1	6.0	5.5	4.7	4.3
Imports	28.9	10.4	3.3	-3.1	-8.9	-4.5	3.9	4.5	4.4	3.7	3.1
Terms of trade (deterioration -)	7.3	-2.6	-5.2	-5.4	-6.3	-1.7	-0.1	0.1	0.1	0.3	0.6
Real effective exchange rate (depreciation -)	-1.4	8.1	-0.2	-1.6	0.8	...	...	...	...	...	...
Money and credit 2/ 3/											
Broad money	15.1	12.5	15.3	9.5	11.6	13.7	14.0	13.7	13.0	12.9	12.2
Net credit to the private sector	21.6	13.3	18.3	13.2	14.0	13.7	14.0	13.7	13.0	12.9	12.2
					(In percent of GDP; unless otherwise indicated)						
Public sector											
NFPS revenue	27.2	27.7	27.8	27.7	24.6	24.3	24.8	25.0	25.1	25.1	25.0
NFPS primary expenditure	24.0	24.3	25.8	26.8	25.7	25.1	25.1	24.9	24.7	24.4	24.3
NFPS primary balance	3.2	3.4	2.0	0.8	-1.1	-0.9	-0.2	0.1	0.4	0.7	0.7
NFPS overall balance	2.0	2.3	0.9	-0.3	-2.1	-2.1	-1.6	-1.3	-0.9	-0.7	-0.7
NFPS structural primary balance 5/	1.6	2.0	0.8	0.0	-0.6	-0.4	0.0	0.2	0.5	0.7	0.7
External sector											
External current account balance	-1.9	-2.7	-4.2	-4.0	-4.4	-3.9	-3.5	-3.0	-2.9	-2.7	-2.3
Gross reserves											
In millions of U.S. dollars	48,859	64,049	65,710	62,353	61,537	62,230	62,930	63,530	63,330	64,130	64,880
Percent of short-term external debt 4/	559	494	539	508	554	559	601	594	541	627	624
Percent of foreign currency deposits at banks	228	300	274	258	224	222	209	198	186	179	174
Debt											
Total external debt	25.6	27.3	27.2	29.7	33.7	37.7	36.5	35.0	33.1	31.8	30.4
Gross non-financial public sector debt (incl. repayment certificates)	23.0	21.2	20.3	20.7	24.0	25.9	25.8	25.5	24.9	24.7	24.6
External	11.4	9.8	8.8	8.7	11.1	12.4	12.1	11.4	10.3	9.8	9.3
Domestic	11.6	11.4	11.5	12.0	12.9	13.5	13.7	14.1	14.7	14.9	15.3
Savings and investment											
Gross domestic investment	25.7	26.0	27.9	26.4	26.0	24.6	24.2	23.9	23.7	23.6	23.5
Public sector (incl. repayment certificates)	4.8	5.4	5.8	5.6	5.0	4.7	4.9	4.9	4.8	4.8	4.8
Private sector (incl. inventories)	20.9	20.6	22.1	20.8	20.9	19.9	19.4	19.0	18.9	18.8	18.6
National savings	23.9	23.4	23.7	22.3	21.6	20.7	20.7	20.9	20.8	20.9	21.2
Public sector	7.5	8.0	7.0	5.9	3.7	3.4	4.1	4.4	4.7	4.9	4.9
Private sector	16.4	15.4	16.6	16.4	17.9	17.4	16.7	16.5	16.1	16.1	16.3
Memorandum items											
Nominal GDP (S/. billions)	469.9	507.7	546.0	576.0	612.0	647.2	688.3	731.8	776.5	823.9	877.3
GDP per capita (in US$)	5,731	6,396	6,629	6,586	6,168	5,548	5,811	6,084	6,356	6,641	6,964

Sources: National authorities; UNDP Human Development Indicators; and Fund staff estimates/projections.
1/ Latest data from the National Statistics Agency, (2015 = proj.).
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.
5/ Adjusted by the economic cycle and commodity prices, and for non-structural commodity revenue. The latter uses as equilibrium commodity prices a moving average estimate that takes 5 years of historical prices and 3 years of forward prices according to IMF World Economic Outlook.

Table 2. Peru: Nonfinancial Public Sector Main Fiscal Aggregates

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						Projections					
	(In millions of soles; unless otherwise indicated)										
Revenues	**127,819**	**140,842**	**151,932**	**159,370**	**150,478**	**156,948**	**170,960**	**183,135**	**194,689**	**206,607**	**219,311**
Taxes	77,261	86,097	91,617	97,646	92,788	97,582	105,000	111,253	118,868	126,401	134,446
Other	50,558	54,745	60,315	61,723	57,690	59,366	65,960	71,882	75,821	80,206	84,865
Primary expenditures 1/	**112,670**	**123,413**	**140,984**	**154,630**	**157,045**	**162,651**	**172,468**	**182,569**	**191,475**	**201,087**	**213,285**
Current	86,729	93,507	106,446	118,206	121,651	126,625	133,084	140,648	147,520	154,703	163,400
Capital	25,941	29,906	34,538	36,424	35,393	36,026	39,384	41,921	43,955	46,385	49,886
Primary balance	**15,150**	**17,429**	**10,948**	**4,739**	**-6,567**	**-5,704**	**-1,508**	**566**	**3,214**	**5,519**	**6,026**
Interest	5,541	5,577	6,005	6,206	6,430	8,129	9,441	10,061	10,146	11,411	12,143
Overall balance	**9,609**	**11,852**	**4,944**	**-1,467**	**-12,997**	**-13,832**	**-10,949**	**-9,495**	**-6,932**	**-5,892**	**-6,117**
External financing	747	-1,385	-4,386	-843	10,064	7,740	3,128	61	-3,740	1,382	573
Domestic financing	-10,356	-10,468	-558	2,310	2,933	6,092	7,821	9,434	10,672	4,510	5,544
Public Gross Debt 2/	**108,184**	**107,704**	**111,009**	**119,252**	**146,704**	**167,373**	**177,706**	**186,585**	**193,517**	**203,794**	**215,424**
External	53,534	49,719	48,084	50,373	68,003	80,169	83,297	83,359	79,618	81,000	81,570
Domestic	49,990	53,925	58,961	65,013	74,639	83,986	91,491	100,608	111,581	120,775	132,136
Repayment Certificates	4,328	3,983	3,964	3,866	4,062	3,218	2,918	2,618	2,318	2,018	1,718
Public Assets	**62,031**	**76,999**	**85,404**	**90,618**	**99,497**	**...**	**...**	**...**	**...**	**...**	**...**
	(In percent of GDP; unless otherwise indicated)										
Revenues	**27.2**	**27.7**	**27.8**	**27.7**	**24.6**	**24.3**	**24.8**	**25.0**	**25.1**	**25.1**	**25.0**
Taxes	16.4	17.0	16.8	17.0	15.2	15.1	15.3	15.2	15.3	15.3	15.3
Other	10.8	10.8	11.0	10.7	9.4	9.2	9.6	9.8	9.8	9.7	9.7
Primary expenditures 1/	**24.0**	**24.3**	**25.8**	**26.8**	**25.7**	**25.1**	**25.1**	**24.9**	**24.7**	**24.4**	**24.3**
Current	18.5	18.4	19.5	20.5	19.9	19.6	19.3	19.2	19.0	18.8	18.6
Capital	5.5	5.9	6.3	6.3	5.8	5.6	5.7	5.7	5.7	5.6	5.7
Primary balance	**3.2**	**3.4**	**2.0**	**0.8**	**-1.1**	**-0.9**	**-0.2**	**0.1**	**0.4**	**0.7**	**0.7**
Interest	1.2	1.1	1.1	1.1	1.1	1.3	1.4	1.4	1.3	1.4	1.4
Overall balance	**2.0**	**2.3**	**0.9**	**-0.3**	**-2.1**	**-2.1**	**-1.6**	**-1.3**	**-0.9**	**-0.7**	**-0.7**
External financing	0.2	-0.3	-0.8	-0.1	1.6	1.2	0.5	0.0	-0.5	0.2	0.1
Domestic financing	-2.2	-2.1	-0.1	0.4	0.5	0.9	1.1	1.3	1.4	0.5	0.6
Public Gross Debt 2/	**23.0**	**21.2**	**20.3**	**20.7**	**24.0**	**25.9**	**25.8**	**25.5**	**24.9**	**24.7**	**24.6**
External	11.4	9.8	8.8	8.7	11.1	12.4	12.1	11.4	10.3	9.8	9.3
Domestic	10.6	10.6	10.8	11.3	12.2	13.0	13.3	13.7	14.4	14.7	15.1
Repayment Certificates	0.9	0.8	0.7	0.7	0.7	0.5	0.4	0.4	0.3	0.2	0.2
Public Assets	**13.2**	**15.2**	**15.6**	**15.7**	**16.3**	**...**	**...**	**...**	**...**	**...**	**...**
Of which: Treasury Deposits and Fiscal Stabilization Fund	6.3	8.2	8.1	8.2	9.0	...	...	...	...	...	...
Public Net Debt	**9.8**	**6.0**	**4.7**	**5.0**	**7.7**	**...**	**...**	**...**	**...**	**...**	**...**
Memorandum items											
Commodity related revenues 3/	4.2	3.8	2.8	2.4	1.3	1.1	1.2	1.2	1.2	1.2	1.2
Output gap (percent of potential GDP)	0.2	0.7	1.7	-0.2	-0.9	-0.7	-0.2	-0.1	0.0	0.0	0.0
SPNF non-commodity structural balance	-2.2	-1.7	-2.4	-3.0	-2.9	-3.0	-2.8	-2.5	-2.1	-1.9	-1.9
SPNF non-commodity primary structural balance	-1.1	-0.6	-1.3	-1.9	-1.8	-1.8	-1.4	-1.1	-0.8	-0.6	-0.5
NFPS structural balance 4/	0.4	0.9	-0.3	-1.1	-1.7	-1.6	-1.3	-1.2	-0.8	-0.7	-0.7
NFPS structural primary balance 4/	1.6	2.0	0.8	0.0	-0.6	-0.4	0.0	0.2	0.5	0.7	0.7
Fiscal impulse (+ = expansionary)	-1.5	-0.4	1.2	0.8	0.6	-0.2	-0.4	-0.2	-0.3	-0.2	0.0

Sources: National Authorities; and Fund staff estimates.

1/ Official data excludes expense accrued during the period by Repayment Certificates (CRPAOs) and Petrolium Price Stabilzation Fund (FEPC), (FEPC) but includes corresponding cash payments.

2/ Official data excludes stock of debt accumulated and not paid during the period by Repayment Certificates (CRPAOs) and Petrolium Price Stabilzation Fund (FEPC).

3/ Net of tax restitutions. In 2014, excludes one-off revenue from the sale of a mine Las Bambas.

4/ Adjusted by the economic cycle and commodity prices, and for non-structural commodity revenue. The latter uses as equilibrium commodity prices a moving average estimate that takes 5 years of historical prices and 3 years of forward prices according to IMF World Economic Outlook.

Table 3. Peru: Statement of Operations of the General Government 1/

(In percent of GDP; unless otherwise indicated)

						Projections					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	**21.8**	**22.4**	**22.3**	**22.3**	**20.1**	**20.1**	**20.4**	**20.7**	**20.9**	**20.9**	**21.0**
Taxes	16.4	17.0	16.8	17.0	15.2	15.1	15.3	15.2	15.3	15.3	15.3
Social Contributions	1.9	2.0	2.1	2.2	2.0	1.9	1.8	2.0	2.0	2.0	2.1
Grants	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other revenue	3.2	3.3	3.3	3.1	2.8	3.1	3.3	3.4	3.5	3.5	3.6
Of which: Interest income	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Expense 2/	**14.8**	**14.7**	**15.4**	**16.6**	**16.8**	**17.0**	**16.7**	**16.6**	**16.5**	**16.3**	**16.4**
Compensation of employees	4.9	4.9	5.3	6.0	6.2	6.3	6.4	6.3	6.4	6.4	6.6
Use of goods and services	5.1	5.6	6.2	6.0	6.5	6.0	5.6	5.8	5.7	5.6	5.6
Consumption of fixed capital 2/	5.0	5.7	6.1	6.0	5.4	5.2	5.2	5.3	5.2	5.2	5.3
Interest	1.2	1.1	1.1	1.1	1.0	1.3	1.4	1.4	1.3	1.4	1.4
Social benefits	2.1	2.0	2.0	1.9	2.0	1.9	2.2	2.1	2.0	1.8	1.7
Other expenses 3/	1.5	1.1	0.8	1.6	1.2	1.4	1.1	1.1	1.1	1.1	1.1
Net acquisition of nonfinancial assets	**5.0**	**5.7**	**6.1**	**6.0**	**5.4**	**5.2**	**5.2**	**5.3**	**5.2**	**5.2**	**5.3**
Acquistions of nonfinancial assets	5.0	5.7	6.1	6.0	5.4	5.2	5.2	5.3	5.2	5.2	5.3
Gross Operating Balance	7.0	7.8	6.8	5.7	3.2	3.2	3.8	4.1	4.4	4.6	4.7
Net lending (+) borrowing (-) 4/	**2.0**	**2.1**	**0.7**	**-0.3**	**-2.2**	**-2.0**	**-1.5**	**-1.2**	**-0.8**	**-0.6**	**-0.6**
Net acquistion of financial assets 5/	**1.2**	**2.0**	**0.0**	**0.0**	**0.0**	**0.4**	**-0.1**	**-0.1**	**0.0**	**-0.5**	**-0.6**
By instrument											
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits 6/	1.2	2.0	0.0	0.0	0.0	0.4	-0.1	-0.1	0.0	-0.5	-0.6
By residency											
Domestic	1.2	2.0	0.0	0.0	0.0	0.4	-0.1	-0.1	0.0	-0.5	-0.6
External	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities 7/	**-0.8**	**0.0**	**-0.7**	**0.3**	**2.2**	**2.4**	**1.4**	**1.1**	**0.8**	**0.1**	**0.0**
By instrument											
Debt securities	-0.9	0.1	0.1	0.4	2.3	1.2	0.9	1.1	1.3	-0.1	-0.1
Loans	0.1	-0.1	-0.8	-0.1	-0.1	1.2	0.5	0.0	-0.5	0.2	0.1
By residency											
Domestic	-0.9	0.1	0.1	0.4	2.3	1.2	0.9	1.1	1.3	-0.1	-0.1
External	0.1	-0.1	-0.8	-0.1	-0.1	1.2	0.5	0.0	-0.5	0.2	0.1
Memorandum items											
Central Government Net lending (+) borrowing (-)	0.3	0.8	-0.1	-1.1	-2.7	-2.0	-2.1	-2.2	-2.2	-2.3	-2.5
Regional Governments Net lending (+) borrowing (-)	0.6	0.6	0.4	0.6	0.6	0.2	0.3	0.4	0.5	0.6	0.6
Local Governments Net lending (+) borrowing (-)	-1.1	-0.2	-0.2	0.2	0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
General Government Primary Balance	3.2	3.1	1.8	0.8	-1.2	-0.8	-0.2	0.1	0.4	0.7	0.7
General Government Overall Balance	2.0	2.1	0.7	-0.3	-2.2	-2.1	-1.6	-1.3	-0.9	-0.7	-0.7
Gen. Gov. primary spending (real percentage change)	1.8	7.6	11.1	7.3	1.5	-0.6	2.1	3.7	2.8	2.5	4.4
Of which: Current spending	7.0	4.8	10.5	10.6	4.6	0.9	1.1	3.4	2.8	2.2	4.0
Capital spending	-9.6	14.8	12.4	-0.4	-6.6	-4.8	5.3	4.4	2.7	3.4	5.5
General Government non-financial expenditures	18.6	19.3	20.5	21.5	21.3	20.9	20.5	20.5	20.4	20.2	20.3

Sources: National authorities and Fund staff estimates.

1/ Fiscal data is not fully compiled on an accrual basis.

2/ Official data excludes expense accrued during the period by Repayment Certificates (CRPAOs) and Petroleum Price Stabilzation Fund (FEPC), but includes corresponding cash payments.

3/ Includes transfers to the Petrolium Price Stabilzation Fund (FEPC).

4/ Net lending (+)/ borrowing (-) is equal to gross operating balance minus net acquistions of nonfinancial assets.

5/ (+) corresponds to increase in financial assets; (-) to a decrease in financial assets.

6/ Includes Fiscal Stabilization Fund (FEF).

7/ (+) corresponds to increase in liabilities (disbursement and/or issuance); (-) to decrease in liabilities (amortizations).

Table 4. Peru: General Government Stock Positions

(In percent of GDP; unless otherwise indicated)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						Projections 1/					
Stock positions:											
Net worth	....	....	....	....	....	....	....	....	....	....	....
Nonfinancial assets	....	....	....	....	....	....	....	....	....	....	....
Net financial worth	**-7.2**	**-4.6**	**-3.5**	**-3.6**	**-5.6**	**-7.4**	**-8.5**	**-9.2**	**-9.5**	**-9.5**	**-9.6**
Financial assets	**11.7**	**12.9**	**11.9**	**11.3**	**10.7**	**10.5**	**9.8**	**9.1**	**8.6**	**7.6**	**6.5**
By instrument											
Currency and deposits 2/	11.3	12.5	11.7	11.0	10.4	10.3	9.6	8.9	8.4	7.4	6.3
Debt securities	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2
By residency											
Domestic	11.3	12.5	11.7	11.0	10.4	10.3	9.6	8.9	8.4	7.4	6.3
External	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2
By currency 3/											
Domestic	11.6	12.7	11.2	10.4	9.7	10.2	9.5	8.8	8.3	7.3	6.3
Foreign	0.4	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2
Liabilities 4/	**18.8**	**17.4**	**15.5**	**14.9**	**16.3**	**17.9**	**18.3**	**18.3**	**18.1**	**17.1**	**16.1**
By instrument											
Debt securities	12.8	11.9	11.2	11.0	12.6	13.2	13.4	13.7	14.2	13.3	12.4
Loans	6.1	5.5	4.3	3.9	3.6	4.7	4.9	4.6	3.9	3.8	3.6
By residency											
Domestic	7.1	6.7	6.3	6.4	8.2	9.1	9.5	10.0	10.8	10.1	9.4
External	11.7	10.8	9.2	8.6	8.0	8.9	8.8	8.3	7.3	7.1	6.7
By currency 3/											
Domestic	10.5	10.4	10.0	10.3	104.8	12.5	12.9	13.3	14.0	14.3	14.7
Foreign	8.3	7.0	5.4	4.6	-88.6	5.4	5.4	5.0	4.1	2.8	1.4
Memorandum items											
Fiscal Stabilization Fund and other public savings	3.3	3.7	4.3	4.5	4.1	4.8	4.4	4.0	3.8	3.6	3.4
Debt of SOEs guaranteed by government 5/	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.5

Sources: National authorities and Fund staff estimates.

1/ Assuming zero other economic flows.

2/ Includes stocks of Fiscal Stabilization Fund (FEF).

3/ Preliminary data.

4/ Excludes debt of public enterprises guaranteed by the central government, debt of Petroleum Price Stabilzation Fund (FEPC), and Repayment Certificates (CRPAOs).

5/ This debt is excluded from general government liabilities since it is a liability of SOEs.

Table 5. Peru: Balance of Payments

(In billions of U.S. dollars; unless otherwise noted)

						Projections					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Current account	**-3.2**	**-5.1**	**-8.6**	**-8.2**	**-8.4**	**-7.0**	**-6.6**	**-6.1**	**-6.3**	**-6.1**	**-5.6**
Merchandise trade	9.2	6.4	0.5	-1.5	-3.1	-1.9	-0.9	-0.3	0.1	0.5	1.0
Exports	46.4	47.4	42.9	39.5	34.2	33.8	36.2	38.4	40.5	42.4	44.3
Traditional	35.9	35.9	31.6	27.7	23.3	22.9	24.9	26.2	27.4	28.6	29.6
Mining	27.5	27.5	23.8	20.5	18.8	19.2	20.6	21.5	22.4	23.3	24.0
Nontraditional and others	10.5	11.5	11.3	11.8	10.9	10.9	11.3	12.2	13.1	13.9	14.7
Imports	-37.2	-41.0	-42.4	-41.0	-37.4	-35.7	-37.1	-38.7	-40.4	-41.9	-43.3
Services, income, and current transfers (net)	-12.4	-11.5	-9.1	-6.7	-5.2	-5.1	-5.8	-5.8	-6.4	-6.6	-6.6
Services	-2.2	-2.4	-1.8	-1.7	-1.7	-1.7	-1.8	-1.7	-1.8	-1.9	-2.0
Investment income	-13.4	-12.4	-10.6	-9.3	-6.8	-6.9	-7.6	-7.8	-8.5	-8.9	-9.2
Current transfers	3.2	3.3	3.3	4.4	3.3	3.4	3.6	3.7	3.9	4.3	4.6
Capital and financial account balance	**8.7**	**19.8**	**11.4**	**6.8**	**10.2**	**7.7**	**7.3**	**6.7**	**6.1**	**6.9**	**6.3**
Public sector	0.7	1.4	-1.3	0.0	4.0	2.1	0.8	0.0	-1.0	0.4	0.2
Medium-term loans 1/	0.1	0.2	-1.3	1.3	4.0	2.2	0.9	0.0	-1.0	0.4	0.2
Disbursements	1.0	1.4	1.3	2.9	5.2	3.5	1.7	1.1	1.1	1.1	1.1
Amortization	0.9	-1.2	-2.6	-1.6	-1.2	1.4	0.8	1.1	2.1	0.7	0.9
Other public sector flows 2/	0.5	1.2	0.0	-1.3	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0
Net external assets	-0.3	-0.5	0.1	-0.6	0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Other transactions of Treasury bonds	0.8	1.7	-0.1	-0.8	-0.2	0.1	0.2	0.2	0.2	0.2	0.2
Short-term flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private sector	8.1	18.4	12.8	6.8	6.3	5.6	6.5	6.7	7.1	6.5	6.1
Foreign direct investment (net) 3/	7.5	11.8	9.2	7.8	6.7	4.8	4.9	5.0	5.2	5.2	5.2
Medium- and long-term loans	3.0	4.0	1.0	0.5	1.3	0.7	0.8	0.8	0.7	0.6	0.5
Portfolio investment	-1.2	-0.1	4.7	-1.8	-0.7	0.2	0.6	0.7	0.7	0.7	0.7
Short-term flows 4/	-1.2	2.6	-2.1	0.4	-1.0	-0.1	0.2	0.2	0.5	0.0	-0.2
Errors and omissions	**-0.9**	**0.1**	**0.1**	**-0.8**	**-1.8**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**4.7**	**14.8**	**2.9**	**-2.2**	**0.1**	**0.7**	**0.7**	**0.6**	**-0.2**	**0.8**	**0.8**
Financing	**-4.7**	**-14.8**	**-2.9**	**2.2**	**-0.1**	**-0.7**	**-0.7**	**-0.6**	**0.2**	**-0.8**	**-0.8**
NIR flow (increase -)	-4.7	-14.8	-2.9	2.2	-0.1	-0.7	-0.7	-0.6	0.2	-0.8	-0.8
Change in NIR (increase -)	-4.7	-15.2	-1.7	3.4	0.8	-0.7	-0.7	-0.6	0.2	-0.8	-0.8
Valuation change	0.0	0.4	-1.2	-1.2	-0.9	0.0	0.0	0.0	0.0	0.0	0.0
					(In percent of GDP)						
Current account balance	**-1.9**	**-2.7**	**-4.2**	**-4.0**	**-4.4**	**-3.9**	**-3.5**	**-3.0**	**-2.9**	**-2.7**	**-2.3**
Trade balance	5.4	3.3	0.2	-0.7	-1.6	-1.0	-0.5	-0.2	0.0	0.2	0.4
Exports	27.2	24.6	21.2	19.5	17.8	18.8	18.9	18.9	18.8	18.5	18.2
Traditional	21.0	18.6	15.6	13.6	12.1	12.8	13.0	12.9	12.7	12.5	12.1
Mining	16.1	14.3	11.8	10.1	9.8	10.7	10.8	10.6	10.4	10.2	9.9
Nontraditional and others	6.1	6.0	5.6	5.8	5.7	6.1	5.9	6.0	6.1	6.1	6.0
Imports	-21.8	-21.3	-21.0	-20.2	-19.5	-19.8	-19.4	-19.1	-18.7	-18.3	-17.7
Services, income, and current transfers (net)	-7.3	-6.0	-4.5	-3.3	-2.7	-2.8	-3.0	-2.9	-3.0	-2.9	-2.7
Investment income	-7.8	-6.4	-5.3	-4.6	-3.6	-3.8	-4.0	-3.8	-3.9	-3.9	-3.8
Capital and financial account balance	**5.1**	**10.3**	**5.6**	**3.4**	**5.3**	**4.3**	**3.8**	**3.3**	**2.8**	**3.0**	**2.6**
Foreign direct investment (net)	4.4	6.2	4.5	3.8	3.5	2.7	2.6	2.5	2.4	2.3	2.1
Overall balance	**2.7**	**7.7**	**1.4**	**-1.1**	**0.0**	**0.4**	**0.4**	**0.3**	**-0.1**	**0.3**	**0.3**
Memorandum items					(Annual percentage change)						
Export value	29.5	2.2	-9.6	-7.8	-13.4	-1.2	7.1	6.0	5.5	4.7	4.3
Volume growth	6.6	4.6	-4.2	-1.0	1.8	6.7	5.1	4.6	3.9	3.2	2.9
Price growth	21.5	-2.2	-5.7	-6.9	-14.9	-7.2	1.8	1.3	1.5	1.4	1.3
Import value	28.9	10.4	3.3	-3.1	-8.9	-4.6	3.9	4.5	4.4	3.7	3.1
Volume growth	13.8	9.9	3.8	-1.6	0.3	1.1	1.9	3.2	2.9	2.6	2.4
Price growth	13.3	0.4	-0.5	-1.5	-9.2	-5.6	2.0	1.2	1.4	1.1	0.7
Terms of trade	7.3	-2.6	-5.2	-5.4	-6.3	-1.7	-0.1	0.1	0.1	0.3	0.6
Gross international reserves (in billions of US$)	48.9	64.0	65.7	62.4	61.5	62.2	62.9	63.5	63.3	64.1	64.9

Sources: National authorities and Fund staff estimates/projections.
1/ Includes financial public sector.
2/ Includes public sector's net external assets and other transactions involving Treasury bonds.
3/ Excluding privatization.
4/ Includes Financial Corporation for Development (COFIDE) and the National Bank.

Table 6. Peru: Monetary Survey 1/

(In billions of soles; unless otherwise noted)

	2011	2012	2013	2014	2015	Projections 2016	2017	2018
	I. Central Reserve Bank							
Net foreign assets	**110**	**138**	**144**	**140**	**133**	**146**	**146**	**146**
(In billions of U.S. dollars)	57	74	80	78	84	84	85	87
Net international reserves 2/	132	163	184	186	210	224	**226**	229
(In billions of U.S. dollars)	49	64	66	62	61	62	63	63
Long-term net external assets	0	0	0	0	0	0	0	0
Foreign currency liabilities	-22	-25	-40	-46	-77	-78	-80	-83
Net domestic assets	**-70**	**-85**	**-92**	**-86**	**-82**	**-88**	**-82**	**-74**
Net credit to nonfinancial public sector	-42	-55	-61	-67	-71	-70	-68	-63
Credit to the financial sector 3/	-11	-9	-8	2	23	23	23	23
Securities issued	-16	-27	-22	-14	-20	-22	-24	-27
Other assets (net)	-1	6	-2	-6	-13	-19	-12	-7
Monetary base	**40**	**53**	**52**	**54**	**51**	**58**	**64**	**72**
Currency	27	32	35	39	41	44	49	53
Reserve	13	20	17	15	11	13	16	18
	II. Depository Corporations 4/							
Net foreign assets	**111**	**132**	**152**	**152**	**171**	**185**	**188**	**190**
Net domestic assets	**46**	**45**	**52**	**72**	**78**	**99**	**136**	**178**
Net credit to the public sector	-53	-69	-73	-73	-78	-72	-64	-55
Credit to the private sector	148	168	198	224	256	291	332	377
Other assets (net)	-49	-53	-74	-79	-100	-120	-132	-144
Broad money	**157**	**177**	**204**	**224**	**250**	**284**	**324**	**368**
Domestic currency	100	123	137	152	156	183	215	252
Foreign currency	58	54	67	72	94	101	108	116
	III. Financial System 5/							
Net foreign assets	**151**	**178**	**203**	**211**	**237**	**248**	**251**	**253**
Net domestic assets	**103**	**115**	**119**	**143**	**157**	**200**	**260**	**327**
Net credit to the public sector	-36	-51	-58	-50	-52	-48	-43	-36
Credit to the private sector	188	213	240	271	303	342	377	409
Other assets (net)	-49	-48	-63	-77	-94	-94	-75	-45
Liabilities to the private sector	**254**	**293**	**322**	**355**	**394**	**448**	**510**	**580**
Domestic currency	187	229	246	273	288	334	389	451
Foreign currency	67	64	76	82	106	113	121	129
	(12-month percentage change)							
Monetary base	16.8	31.9	-1.5	3.7	-4.8	12.6	11.6	11.1
Broad money	15.1	12.5	15.3	9.5	11.6	13.7	14.0	13.7
Domestic currency	16.6	23.3	11.6	10.6	3.0	17.4	17.5	17.1
Foreign currency	12.6	-6.2	23.6	7.3	29.8	7.6	7.6	6.9
Liabilities to the private sector	5.5	15.4	10.1	10.2	10.9	13.7	14.0	13.7
Domestic currency	4.8	22.4	7.6	11.1	5.5	16.0	16.3	15.9
Foreign currency	7.6	-4.3	19.0	7.4	29.2	7.3	7.2	6.5
Depository corporations credit to the private sector	21.6	13.3	18.3	13.2	14.0	13.7	14.0	13.7
Domestic currency	20.4	16.0	22.6	17.7	28.4	24.1	21.5	18.0
Foreign currency	23.2	9.8	12.6	6.5	-9.4	-10.3	-10.0	-5.0

Sources: National Authorities; and Fund staff estimates.

1/ Stocks in foreign currency are valued at the end-of-period exchange rate.

2/ Excludes subscriptions to the IMF and the Latin American Reserve Fund, Pesos Andinos, credit lines to other central banks, Andean Development Corporation bonds, and foreign assets temporarily held by the Central Bank as part of swap operations.

3/ Including the National Bank.

4/ Depository corporations comprise the Central Bank, the National Bank, commercial banks, the Agricultural Bank, financial firms, municipal banks, rural banks and credit unions.

5/ Financial system comprises depository corporations and other financial corporations. Other financial companies include mutual funds, COFIDE, insurance companies, leasing companies, pension funds, the Financing Agency for Small and Medium-sized Enterprises and the Fund for Financing Housing.

Table 7. Peru: Financial Soundness Indicators 1/

(In percent; unless otherwise indicated)

	2011	2012	2013	2014	2015
			(as of December)		
Capital Adequacy					
Capital to risk-weighted assets 2/	13.7	14.4	13.9	14.2	14.3
Regulatory Tier I capital to risk-weighted assets 3/	10.8	10.9	10.4	10.4	10.3
Nonperforming loans net of provisions to capital 4/	-14.7	-12.6	-10.8	-9.0	-9.4
Leverage 5/	7.7	7.9	7.9	8.3	7.9
Asset Quality					
Nonperforming loans to total gross loans 4/	1.8	2.2	2.6	2.9	2.9
In domestic currency	2.5	3.0	3.3	3.4	2.9
In foreign currency	1.0	1.1	1.5	2.1	2.9
Nonperforming, refinanced and restructured loans to total gross loans 4/ 6/	2.9	3.2	3.6	4.0	4.0
In domestic currency	3.5	4.2	3.3	3.4	2.9
In foreign currency	1.9	1.8	1.5	2.1	2.9
Refinanced and restructured loans to total gross loans	1.1	1.1	1.0	1.1	1.1
Provisions to nonperforming loans 4/	225.2	202.0	175.2	157.7	161.8
Provisions to nonperforming, restructured, and refinanced loans 4/ 6/	142.3	134.9	126.3	114.4	116.5
Sectoral distribution of loans to total loans					
Consumer loans	18.6	19.1	18.4	18.1	18.3
Mortgage loans	13.5	14.7	15.3	15.5	15.2
Large corporations	18.1	15.8	17.6	17.2	21.4
Small corporations	15.4	15.3	15.5	17.0	15.8
Medium size firms	17.2	17.5	17.6	18.3	16.9
Small firms	11.8	12.5	11.4	10.1	9.0
Microenterprises	5.5	5.2	4.3	3.8	3.4
Earnings and Profitability					
Return on equity (ROE)	23.5	21.5	20.0	18.2	21.1
Return on assets (ROA)	2.3	2.2	2.0	1.9	2.1
Financial revenues to total revenues	82.0	82.7	85.6	85.0	85.2
Annualized financial revenues to revenue-generating assets	11.1	11.2	10.9	10.6	10.5
Liquidity					
Total liquid assets to total short-term liabilities (monthly average basis)	40.5	45.0	43.0	39.4	37.7
In domestic currency	36.7	44.2	31.4	25.3	26.2
In foreign currency	45.0	46.2	56.4	55.2	47.5
Deposit-to-loan	95.3	95.2	98.1	90.5	92.0
Foreign Currency Position and Dollarization					
Share of foreign currency deposits in total deposits	43.9	38.2	43.6	43.4	49.5
Share of foreign currency loans in total credit	45.8	44.4	41.1	38.4	30.1
Operational efficiency					
Financing to related parties to capital 7/	9.3	11.5	9.3	9.4	12.3
Nonfinancial expenditure to total revenues 8/	33.7	33.6	33.7	33.0	30.9
Annualized Nonfinancial expenditure to total revenue-generating assets 8/	4.6	4.6	4.3	4.1	3.8
Memorandum items					
General Stock market index, IGBVL	19,474	20,629	15,754	14,794	9,849
EMBI+ PERU spread, basis points	216	117	174	181	243

Source: National authorities.

1/ These indicators correspond to depository corporations.

2/ Since July 2009, the regulatory capital requirement applied to all risks: credit, market and operational risk.

3/ Since July 2009, Banking Law component establishes that the Tier I capital have to be defined, and Risk-weighted assets include overall risks (credit, market and operational).

4/ Nonperforming loans are overdue loans after 15 days since the due date for commercial loans, and after 30 days for small businesses loans. In the case of mortgage, consumer and leasing loans, they are considered overdue after 30 days since the due date only for the non paid portion and after 90 days for all the credit. The overdue loans include credits under judicial resolution.

5/Tier I regulatory capital / Total Exposure (on-balance sheet exposures, derivative exposures and off-balance exposures converted into credit exposure equivalents using credit conversion factors).

6/ Includes restructured loans, refinanced loans, and arrears. Refinanced loans refer to those loans subjected to either term and/or principal modifications with respect to the initial debt contract. Restructured loans refer to those loans whose payments have been restructured according to the "Ley General del Sistema Concursal."

7/ Financing to related parties corresponds to those loans to individuals and firms owning more than 4 percent of the bank.

8/ Nonfinancial expenditures do not consider provisions nor depreciation.

Table 8. Peru: Financial and External Vulnerability Indicators

(In percent; unless otherwise indicated)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						Projections					
Financial indicators											
Public sector debt/GDP	23.0	21.2	20.3	20.7	24.0	25.9	25.8	25.5	24.9	24.7	24.6
Of which: in domestic currency (percent of GDP)	11.2	11.0	11.5	12.0	12.9	13.5	13.7	14.1	14.7	14.9	15.3
90-day prime lending rate, domestic currency (end of period)	5.4	5.0	4.5	4.7	…	…	…	…	…	…	…
90-day prime lending rate, foreign currency (end of period)	2.4	4.0	1.0	0.7	1.1	…	…	…	…	…	…
Velocity of money 1/	3.0	2.9	2.7	2.6	2.5	2.3	2.1	2.0	1.9	1.8	1.7
Net credit to the private sector/GDP 2/	31.5	33.0	36.3	39.0	41.8	45.0	48.2	51.5	54.9	58.4	61.5
External indicators											
Exports, U.S. dollars (percent change)	29.5	2.2	-9.6	-7.8	-13.4	-1.0	7.1	6.0	5.5	4.7	4.3
Imports, U.S. dollars (percent change)	28.9	10.4	3.3	-3.1	-8.9	-4.5	3.9	4.5	4.4	3.7	3.1
Terms of trade (percent change) (deterioration -) 3/	7.3	-2.6	-5.2	-5.4	-6.3	-1.7	-0.1	0.1	0.1	0.3	0.6
Current account balance (percent of GDP)	-1.9	-2.7	-4.2	-4.0	-4.4	-3.9	-3.5	-3.0	-2.9	-2.7	-2.3
Capital and financial account balance (percent of GDP)	5.1	10.3	5.6	3.4	5.3	4.3	3.8	3.3	2.8	3.0	2.6
Total external debt (percent of GDP)	25.6	27.3	27.2	29.7	33.7	37.7	36.5	35.0	33.1	31.8	30.4
Medium- and long-term public debt (in percent of GDP) 4/	11.6	10.2	9.0	9.6	12.2	14.3	13.9	13.1	11.8	11.3	10.7
Medium- and long-term private debt (in percent of GDP)	10.3	12.5	15.0	16.6	17.8	19.5	19.1	18.7	18.3	17.8	17.2
Short-term public and private debt (in percent of GDP)	3.7	4.6	3.2	3.4	3.7	3.8	3.5	3.2	3.0	2.7	2.5
Total external debt (in percent of exports of goods and services) 4/	86.3	100.3	113.0	132.3	160.2	168.5	163.1	157.3	150.2	147.1	143.8
Total debt service (in percent of exports of goods and services) 5/	8.0	11.0	16.0	16.4	16.4	16.9	15.0	15.6	17.3	14.0	14.2
Gross official reserves											
In millions of U.S. dollars	48,859	64,049	65,710	62,353	61,537	62,230	62,930	63,530	63,330	64,130	64,880
In percent of short-term external debt 6/	559.1	494.2	539.5	508.3	554.0	559.3	601.2	594.5	541.4	627.2	624.4
In percent of short-term external debt, foreign currency deposits, and adjusted CA balance 6/ 7/	125.2	132.7	127.3	123.5	118.4	125.2	123.7	120.5	113.2	114.4	113.6
In percent of broad money 8/	83.7	93.2	90.0	83.2	83.3	78.9	70.0	62.2	54.9	49.2	44.4
In percent of foreign currency deposits at banks	227.7	300.5	273.9	257.8	224.3	222.4	209.1	197.5	186.1	179.1	174.1
In months of next year's imports of goods and services	12.1	15.4	16.2	16.5	16.6	16.4	16.0	15.5	14.9	14.6	n.a.
Net international reserves (in millions of U.S. dollars)	48,816	63,991	65,663	62,308	61,485	62,185	62,885	63,485	63,285	64,085	64,835
Central Bank's Foreign Exchange Position	33,300	46,063	41,097	35,368	25,858	26,558	27,258	27,858	27,658	28,458	29,208

Sources: National authorities; IMF's Information Notice System (INS); and Fund staff estimates/projections.
1/ Defined as of the ratio of annual GDP to end-period broad money.
2/ Corresponds to depository corporations.
3/ End of period; data from INS.
4/ Includes Central Bank's debt.
5/ Includes debt service to the Fund.
6/ Short-term debt includes amortization of medium- and long-term loans falling due over the following year, including debt swaps.
7/ Current Account deficit adjusted for 0.75*net FDI inflows; if adjusted CA balance>0, set to 0.
8/ At end-period exchange rate.

Table 9. Peru: Medium-Term Macroeconomic Framework

						Proj.					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						(Annual percentage change)					
Production											
GDP at constant prices	6.5	6.0	5.9	2.4	3.3	3.7	4.1	3.6	3.5	3.5	3.5
Consumer prices (end of period)	4.7	2.6	2.9	3.2	4.4	3.2	2.5	2.5	2.5	2.5	2.5
GDP deflator	5.2	2.0	1.6	3.0	2.9	1.9	2.2	2.6	2.5	2.5	2.9
Trade											
Merchandise trade											
Exports, f.o.b.	29.5	2.2	-9.6	-7.8	-13.4	-1.0	7.1	6.0	5.5	4.7	4.3
Imports, f.o.b.	28.9	10.4	3.3	-3.1	-8.9	-4.5	3.9	4.5	4.4	3.7	3.1
Terms of trade (deterioration -)	7.3	-2.6	-5.2	-5.4	-6.3	-1.7	-0.1	0.1	0.1	0.3	0.6
						(In percent of GDP; unless otherwise indicated)					
External current account balance	-1.9	-2.7	-4.2	-4.0	-4.4	-3.9	-3.5	-3.0	-2.9	-2.7	-2.3
Total external debt service 1/	2.4	3.0	3.8	3.7	3.5	3.8	3.4	3.5	3.8	3.0	3.0
Medium- and long-term	2.3	2.9	3.8	3.6	3.4	3.7	3.3	3.4	3.8	3.0	3.0
Nonfinancial public sector	1.1	1.2	1.8	1.3	1.3	1.4	1.0	1.1	1.5	0.8	0.8
Private sector	1.2	1.7	1.9	2.3	2.1	2.4	2.3	2.3	2.2	2.2	2.1
Short-term 2/	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.0	0.0
Nonfinancial public sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private sector	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.0	0.0
Interest	1.0	0.9	1.0	1.1	1.4	1.4	1.4	1.4	1.4	1.3	1.2
Amortization (medium-and long-term)	1.4	2.1	2.8	2.6	2.1	2.3	2.0	2.0	2.5	1.7	1.8
Public sector											
NFPS primary balance 3/	3.2	3.4	2.0	0.8	-1.1	-0.9	-0.2	0.1	0.4	0.7	0.7
General government revenue	21.8	22.4	22.3	22.3	20.1	20.1	20.4	20.7	20.9	20.9	21.0
General govt. non-interest expenditure 3/	24.0	24.3	25.8	26.8	25.7	25.1	25.1	24.9	24.7	24.4	24.3
NFPS interest due	1.2	1.1	1.1	1.1	1.1	1.3	1.4	1.4	1.3	1.4	1.4
NFPS overall balance 3/	2.0	2.3	0.9	-0.3	-2.1	-2.1	-1.6	-1.3	-0.9	-0.7	-0.7
Public sector debt 3/	23.0	21.2	20.3	20.7	24.0	25.9	25.8	25.5	24.9	24.7	24.6
Savings and investment											
Gross domestic investment	25.7	26.0	27.9	26.4	26.0	24.6	24.2	23.9	23.7	23.6	23.5
Public sector 3/	4.8	5.4	5.8	5.6	5.0	4.7	4.9	4.9	4.8	4.8	4.8
Private sector	20.9	20.6	22.1	20.8	20.9	19.9	19.4	19.0	18.9	18.8	
Private sector (excluding inventories)	19.1	20.3	20.7	20.1	19.3	18.3	18.3	18.3	18.0	17.8	17.4
Inventory changes	1.9	0.3	1.4	0.7	1.6	1.6	1.1	0.8	0.8	1.0	1.2
National savings	23.9	23.4	23.7	22.3	21.6	20.7	20.7	20.9	20.8	20.9	21.2
Public sector 4/	7.5	8.0	7.0	5.9	3.7	3.4	4.1	4.4	4.7	4.9	4.9
Private sector	16.4	15.4	16.6	16.4	17.9	17.4	16.7	16.5	16.1	16.1	16.3
External savings	1.9	2.7	4.2	4.0	4.4	3.9	3.5	3.0	2.9	2.7	2.3
Memorandum items											
Nominal GDP (billions of nuevos soles)	469.9	507.7	546.0	576.0	612.0	647.2	688.3	731.8	776.5	823.9	877.3
Gross international reserves (billions of U.S. dollars)	48.9	64.0	65.7	62.4	61.5	62.2	62.9	63.5	63.3	64.1	64.9
External debt service (percent of exports of GNFS)	8.0	11.0	16.0	16.4	16.4	16.9	15.0	15.6	17.3	14.0	14.2
Short-term external debt service (percent of exports of GNFS)	0.3	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.2	0.2	0.2
Public external debt service (percent of exports of GNFS)	3.8	4.4	7.6	5.7	6.0	6.1	4.5	5.0	6.9	3.7	3.9

Sources: National authorities and Fund staff estimates.
1/ Includes interest payments only.
2/ Includes the financial public sector.
3/ Includes Repayment Certificates (CRPAOs).
4/ Excludes privatization receipts.

Table 10. Peru: External Debt Sustainability Framework, 2014–21

(In percent of GDP, unless otherwise indicated)

	2014	2015	2016	2017	2018	2019	2020	2021	Debt-stabilizing non-interest current account 6/
			Projections						
Baseline: External debt	**29.7**	**33.7**	**37.7**	**36.5**	**35.0**	**33.1**	**31.8**	**30.4**	**-3.1**
Change in external debt	2.4	4.1	3.9	-1.2	-1.5	-1.9	-1.2	-1.5	
Identified external debt-creating flows (4+8+9)	0.4	0.2	-0.3	-0.9	-1.0	-1.0	-1.0	-1.2	
Current account deficit, excluding interest payments	3.0	3.0	2.4	2.1	1.6	1.6	1.4	1.1	
Deficit in balance of goods and services	1.6	2.5	2.0	1.4	1.0	0.8	0.6	0.4	
Exports	22.4	21.1	22.3	22.4	22.2	22.0	21.6	21.1	
Imports	24.0	23.6	24.3	23.7	23.3	22.8	22.3	21.5	
Net non-debt creating capital inflows (negative)	-3.0	-3.1	-2.8	-2.9	-2.8	-2.8	-2.6	-2.4	
Net foreign direct investment, equity	3.8	3.5	2.7	2.6	2.5	2.4	2.3	2.1	
Net portfolio investment,equity	-0.9	-0.4	0.1	0.3	0.3	0.3	0.3	0.3	
Automatic debt dynamics 1/	0.4	0.3	0.1	0.0	0.2	0.2	0.2	0.2	
Denominator: 1+g+r+gr	1.0	0.9	0.9	1.1	1.1	1.1	1.1	1.1	
Contribution from nominal interest rate	1.1	1.4	1.4	1.4	1.4	1.4	1.3	1.2	
Contribution from real GDP growth	-0.6	-1.0	-1.3	-1.5	-1.2	-1.2	-1.1	-1.0	
Contribution from price and exchange rate changes 2/	...	...	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	2.0	3.9	4.2	-0.3	-0.5	-0.9	-0.2	-0.3	
External debt-to-exports ratio (in percent)	132.3	160.2	168.5	163.1	157.3	150.2	147.1	143.8	
Gross external financing need (in billions of U.S. dollars) 4/	19.9	19.4	18.3	17.3	17.0	18.2	16.5	16.1	
In percent of GDP	9.8	10.1	10.2	9.0	8.4	8.4	7.2	6.6	
Scenario with key variables at their historical averages 5/	**29.7**	**33.7**	**28.4**	**23.3**	**18.3**	**13.3**	**8.9**	**4.8**	**-4.4**
Key Macroeconomic Assumptions Underlying Baseline									
Real GDP growth (in percent)	2.4	3.3	3.7	4.1	3.6	3.5	3.5	3.5	
GDP deflator in U.S. dollars (change in percent)	-1.9	-8.3	-9.8	2.2	2.6	2.5	2.5	2.9	
Nominal external interest rate (in percent)	4.0	4.3	4.0	4.0	4.2	4.1	4.1	4.1	
Growth of exports and services (U.S. dollar terms, in percent)	-6.6	-11.0	-0.7	6.5	5.6	5.1	4.3	3.9	
Growth of imports and services (U.S. dollar terms, in percent)	-2.5	-6.9	-3.6	3.9	4.1	4.1	3.6	3.0	
Current account balance, excluding interest payments	-3.0	-3.0	-2.4	-2.1	-1.6	-1.6	-1.4	-1.1	
Net non-debt creating capital inflows	3.0	3.1	2.8	2.9	2.8	2.8	2.6	2.4	

Source: National authorities and Fund staff calculations.

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex I. Implementation of Past IMF Recommendations

1. **By and large, Peruvian authorities have been appreciative of staff advice and research contributions.** Peru is also one of the highest recipients of Fund's technical assistance, especially in the fiscal area. Consistent with past Fund advice, the authorities pushed to improve the execution of public investment but this was derailed by issues stemming from excessive paperwork, the unfinished decentralization process, and poor sub-national capacity. The authorities have been making efforts to improve tax collection to offset revenue losses, and improve fiscal transparency. Recommendations on the design of the structural fiscal rule were also taken into account when the methodology was recently amended. Greater exchange rate flexibility was allowed in 2015, in line with staff advice. A majority of 2011 FSAP recommendations have been implemented.

Peru: Progress on Implementation of Selected FSAP (2011) Recommendations

Recommendations	Progress
Banking Oversight	
Tighten the regulation of related party and intra-group transactions.	Stricter criteria have been established for determining related parties, and the definition of the economic group has been updated in line with international standards (SBS Resolution No. 5780-2015)
Strengthen consolidated supervision and regulate holdings.	The regulation of holding companies requires a change of law and has not been implemented. Consolidated supervision has been strengthened through group-level supervision and exchange of data.
Insurance and Pensions	
Eliminate requirement for the SBS to pre-authorize issuers and instruments in which the AFPs can invest.	Implemented through the SBS Resolution No. 1293-2014.
Introduce auction mechanisms for new entrants and automatic assignation of undecided contributors to lower the commission of the AFPs.	Implemented through Law No. 29903 and SBS Resolution No. 8517-2012.
Reduce the incentives to invest in marketing by either introducing a flat component in fees, or limiting the frequency of switches, or allowing switches only toward lower-fee AFPs.	The incentives for marketing have been limited to procurement, as part of Law No. 29903.
Base market risk monitoring on exogenous benchmarks and relative VAR.	AFPs to incorporate benchmarks into their models of investment management and monitor the expected losses of managed portfolios in relation to the VAR (SBS Resolution No. 6253-2014).
Update mortality table for pension annuities.	In progress. Updated tables are pre-published and are being evaluated.

Annex II. External Sector Assessment

Overall, Peru's current external position is assessed to be moderately weaker than fundamentals with a moderately positive real effective exchange rate gap and a current account deficit wider than the estimated norm. However, under current policies and given small Peru-specific policy gaps, the current account is expected to gradually narrow closer to its norm in the medium term, financed mostly by longer-term capital flows. In addition, Peru's reserve position remains strong and external debt remains low.

1. **The current account deteriorated somewhat in 2015.** The current account deficit has widened by ½ percent of GDP to 4.4 percent of GDP in 2015. Falling copper prices significantly weighed on the trade balance, despite an improvement in mineral export volumes as new production came on-stream. The deterioration in the trade balance was fully offset by lower profit payments, which declined by some 34 percent. In addition, current transfers fell ½ percent of GDP, back to their historical trend. Over the medium term, the current account should narrow as copper production is expected to double by 2018, and would remain financed mainly by FDI flows.

Current Account and REER Gaps, 2015

(In percent of GDP, unless stated otherwise)

	EBA methodology			CGER External
	CA Regression	RER Regression	RER Regression	Sustainability Methodology
CA headline	-4.4	..	..	**-4.4**
CA underlying 1/	-3.5	..	..	-2.4
CA norm	-2.0	..	..	-1.8
CA gap 2/	-1.5	..	..	-0.5
RER gap (in percent) 3/	***7.1***	***6.3***	***15.4***	***2.4***
Adjusted 4/				
CA underlying 1/	-3.1	..	..	-2.0
CA norm	-2.0	..	..	-1.8
CA gap 2/	-1.1	..	..	-0.2
RER gap (in percent) 3/	***5.3***	***6.3***	***15.4***	***1.0***

Source: Fund staff estimates.

1/ Cyclically adjusted CA for EBA results. Medium-term adj. CA for CGER.

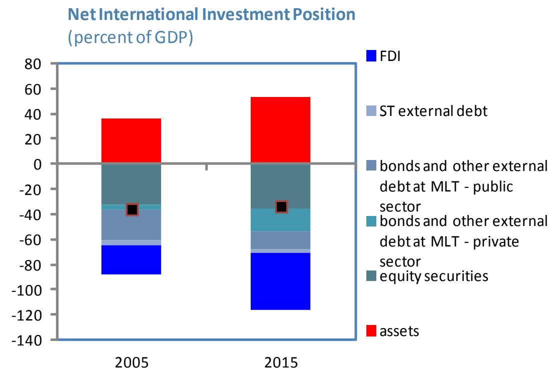
2/ CA gap is CA underlying minus CA norm.

3/ Positive value indicates overvaluation.

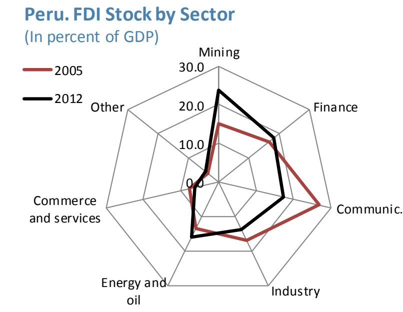
4/ Adjusted for under-reporting in the illegal exports of gold estimated at 0.4 percent of GDP.

2. **The real effective exchange rate depreciated little since the 2015 Article IV Consultation and is moderately strong** (Table above). Model-based estimates currently indicate moderately weaker fundamentals, but only a small part of the CA gap (0.4 percentage points) results from policy gaps. However, staff expects that the current account will narrow by about 1¼ percent of GDP—the amount required to close the gap with the estimated norm—over the medium term, owing to an increase in copper exports. The REER level regression results reported in the table above have historically shown large residuals for Peru and therefore are considered less reliable than other estimates.

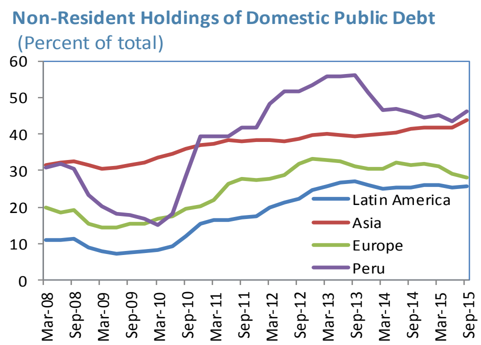
3. **Peru's net IIP liabilities and foreign participation in the local bond market have historically been sizeable but do not pose immediate risks.** A large increase in FDI liabilities over the past decade, especially in mining, and in private sector debt has coincided with a significant increase in foreign assets. And while large, most IIP liabilities have long maturities, with short-term external debt not exceeding 4 percent of GDP. Non-resident holdings of domestic public debt are also significant, albeit declining, and Peru's total public debt remains modest, attenuating risks from a sudden reversal of investor appetite.



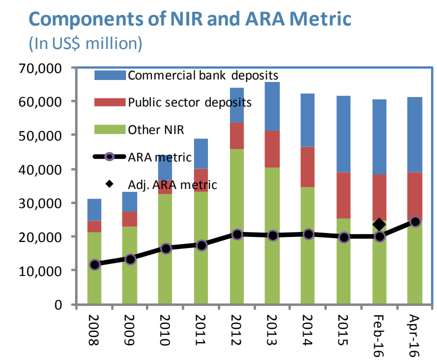
Source: Central Reserve Bank of Peru.



Source: National authorities.



Source: National authorities.



Sources: National authorities; and Fund staff calculations.

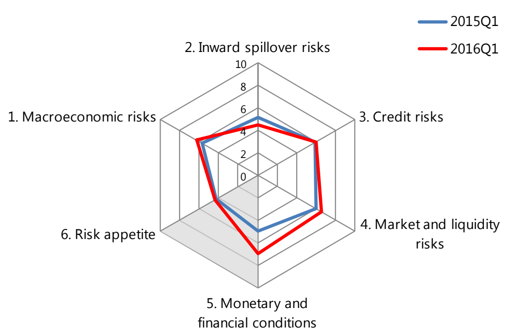
4. Peru's international reserves comfortably exceed adequacy metrics despite sizable foreign exchange intervention. Gross reserves stood at US$61 billion. The BCRP has sold significant amounts of FX (US$8 billion in spot sales) to limit exchange rate volatility (in addition to sales of swaps) and required high reserves against FX deposits with commercial banks. A significant part of the NIR consists of domestic FX liabilities—including the Fiscal Stabilization Fund, commercial banks' reserves requirements on FX deposits, and deposits corresponding to FX repos—which are mostly of longer-term nature and do not pose short-term risks to reserves—repos have 2–5 year maturities, access to FSF resources is limited by law, and high commercial banks' reserve requirements on dollar deposits protect against dollar liquidity risks. Even when adjusting the NIR for theses liabilities, reserves remain within the adequacy range. Reserves also remain adequate when augmenting the ARA metric with a commodity price buffer (US$4 billion based on prices at 68 percent of the confidence interval of futures data)—they stood at 250 percent of the augmented metric, and excluding commercial bank deposits, at 162 percent of the augmented metric. Such higher precautionary liquidity could be useful to buffer against sudden drops in commodity prices and smooth adjustment to commodity price changes.

Annex III. Macro-Financial Stability Update

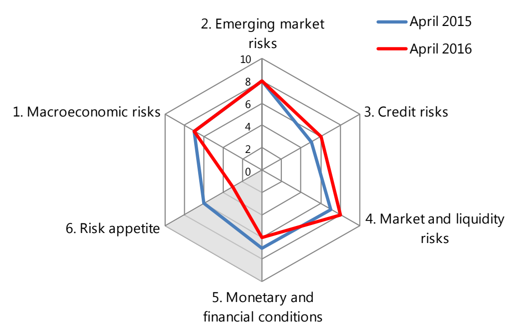
A. Overall Macro-Financial Stability

1. Peru remains broadly stable in macro-financial terms. Market and liquidity risks have risen slightly, while inward spillover risks declined. Purely domestic monetary and financial conditions have eased, despite the policy interest rate hikes from September 2015 to February 2016. With the exception of risk appetite and monetary and financial conditions, these trends are broadly consistent with the corresponding global risks as reported in the April 2016 Global Financial Stability Report (GFSR).

Peru



Comparable Global Financial Stability Map



Note: Away for center signifies higher risks, easier monetary and financial conditions, or higher risk appetite.
Sources: National Authorities, and Fund staff calculations.

B. Financial Sector Risk Assessment

2. As of end-2015, the financial sector faces medium vulnerability risks, with adequate buffers to contain them (Map). Credit growth has been robust, consistent with the pickup in economic activity in 2015 and continued financial deepening.[1] Banks are sufficiently capitalized and liquid, reporting highest profitability and return on assets since end-2012. Non-performing loans (NPL) appear to have stabilized, and are sufficiently provisioned for. Non-bank deposit-taking institutions (micro-enterprises, and small and medium enterprises) have higher NPLs than banks, as they are more sensitive to the economic cycle, but they constitute only a small part of financial system assets (7 percent).[2]

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[1] The ratio of private sector credit to GDP in Peru (42 percent in 2015) is lower than expected for a country with its population and income levels. Benchmarks used according to Finstats 2016.

[2] In 2015, the SBS took receivership of one caja (a small cooperative), while other small intermediaries continued to struggle, as their portfolios (concentrated in small firms) have deteriorated. However, systemic risk is limited due to the small share of cajas in total financial sector assets and an expected wave of consolidation in the sector.

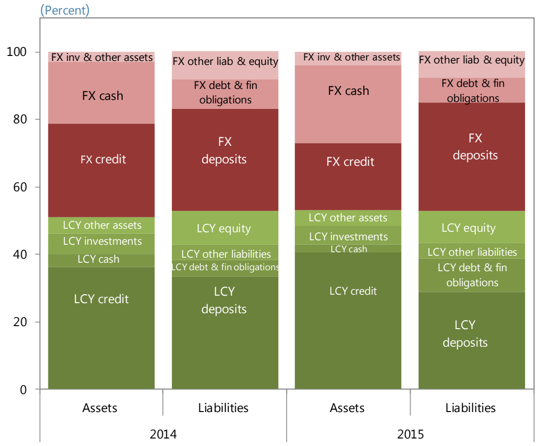
Financial Soundness Indicator Map 1/

Peru	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3	2014Q4	2015Q1	2015Q2	2015Q3	2015Q4	Latest
Overall Financial Sector Rating	M	M	H	M	M	M	M	M	M	M	M	M
Credit cycle	L	L	H	M	L	L	L	M	M	M	M	M
Change in credit / GDP ratio (pp, annual)	2.0	2.6	3.2	3.2	2.3	2.0	2.4	3.3	3.3	3.8	3.0	3.0
Growth of credit / GDP (%, annual)	7.3	9.3	11.4	11.1	7.8	6.5	7.7	10.3	10.2	11.5	11.5	11.5
Credit-to-GDP gap (st. dev)	1.4	1.6	1.5	1.1	1.0	0.7	0.9	0.9	0.7	0.4	-0.8	-0.8
Balance Sheet Soundness	M	M	M	M	M	M	M	M	M	M	M	M
Balance Sheet Structural Risk	H	H	H	M	M	M	M	M	M	M	M	M
Deposit-to-loan ratio	97.6	98.4	97.3	97.5	94.9	91.6	89.6	89.4	88.3	89.4	91.6	91.6
FX liabilities % (of total liabilities)	47.8	49.5	49.6	50.2	49.4	49.6	48.4	48.8	48.5	49.5	49.2	49.2
FX loans % (of total loans)	43.8	42.1	40.8	39.5	39.9	39.7	38.2	36.4	33.7	31.2	30.1	30.1
Balance Sheet Buffers	L	L	L	L	L	L	L	L	L	L	L	L
Leverage	L	L	L	L	L	L	L	L	L	L	L	L
Leverage ratio (%)	9.6	9.9	10.1	9.9	10.3	10.4	10.7	9.9	10.1	9.9	10.1	10.1
Profitability	L	L	L	L	L	L	L	L	L	L	L	L
ROA	2.0	2.0	2.0	1.9	1.9	1.9	1.9	2.0	2.1	2.1	2.1	2.1
ROE	20.3	20.1	19.9	19.2	18.5	18.5	18.2	19.4	20.5	20.7	21.1	21.1
Asset quality	M	M	M	M	M	M	M	M	M	L	L	L
NPL ratio	3.5	3.5	3.5	3.7	3.8	3.9	4.0	4.0	4.1	4.0	n.a.	4.0
NPL ratio change (%, annual)	11.6	9.3	8.3	8.1	8.0	10.6	12.9	8.9	7.9	1.9	-0.7	-0.7

Sources: Haver and Fund staff calculations.
1/ Covers the whole financial sector.

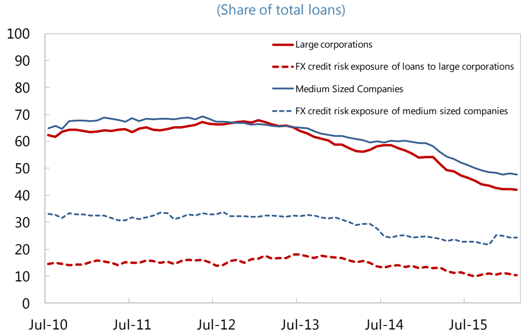
3. Dollarization remains a structural risk, albeit with recent asymmetric trends between credit and deposits. Total credit dollarization has declined rapidly, ahead of BCRP targets, to 27.4 percent in January 2016, with SBS estimates of banks' net exposure to FX risk deemed even lower at around 11 percent (due to collateral and hedging). However, deposit dollarization remains relatively high at around 45 percent, as individuals sought protection against currency depreciation. While there is a growing divergence between the currency matching of loans and deposits, banks have been able to de-dollarize their loan portfolios ahead of deposits, as the BCRP has provided soles through repo operations with 2–5 year maturities, thus supporting credit creation in local currency.

Structure of Banks' Assets and Liabilities
(Percent)



Source: National Authorities and Fund staff calculations.

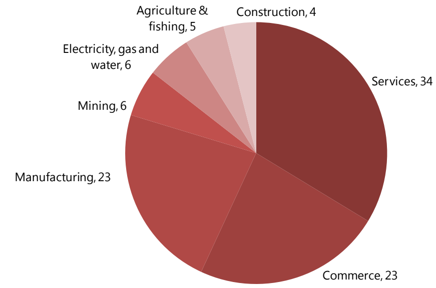
Corporate Sector's Dollarization and FX Credit Exposure
(Share of total loans)



Source: National authorities.

4. Commodity price movements appear to have had little direct and indirect effects on financial stability. Banks' loan portfolios are well-diversified, with mining and agriculture constituting only a small share (5 percent each) of total assets, and NPLs below 2 percent as of December 2015. Several smaller institutions have a higher direct exposure to these sectors, but their weights in the financial sector are small (less that 5 percent).[3] As to indirect impacts, trends in general unemployment rates do not appear to be correlated with growth in mining, which is highly capital intensive, and agriculture, even in regions where these sectors are significant, although a more severe *El Niño* could carry serious consequences in the affected areas.

Sectoral Distribution of Banking Sector Credit
(Percent)

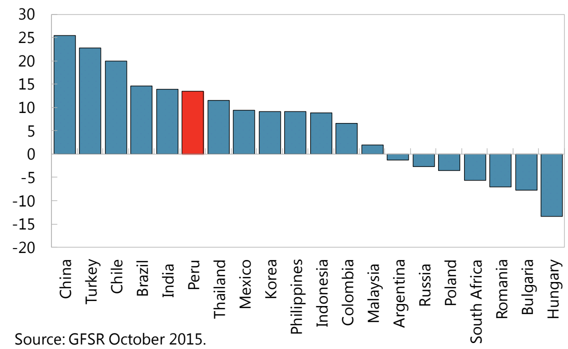


Sources: National authorities, and Fund staff calculations.

C. Non-Financial Sector Risk Assessment

5. Corporate leverage has grown since 2007, in line with trends in emerging markets. In particular, debt issuance abroad grew from 14 percent of total regional issuance in 2012 to 29 percent in 2015, not least due to favorable liquidity conditions and stronger economic fundamentals in the region.

Change in Corporate Debt, 2007-14
(Percent of GDP)



Source: GFSR October 2015.
Note: Debt includes bank credit and bond financing.

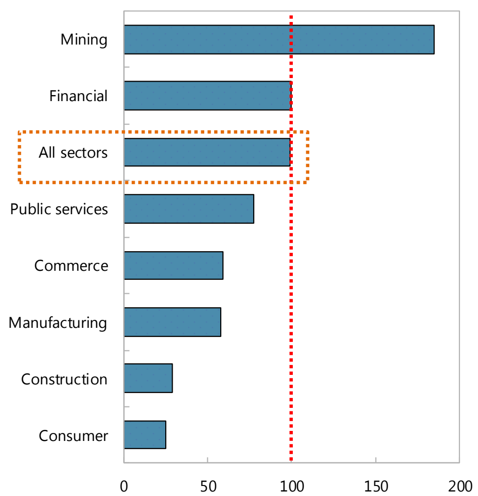
6. Firms operating in the non-tradable sector—about 1/4 of total—are vulnerable to large and abrupt currency depreciations, but actual risks seem manageable. These firms do not have natural FX hedges and are, thus, exposed to currency risk since the bulk of their external issuances are denominated in U.S. dollars. Sectors with large FX asset-to-liability gaps, notably the construction and consumer sectors, suffered the largest FX losses when the sol depreciated in 2015. Nevertheless, estimated FX losses in the aggregate corporate sector were only 0.2 percent of total earnings, as large gains in the mining offset losses in other sectors. Refinancing risks for bonds remain moderate overall as most of debt is at long maturities and fixed interest rates. A recent BCRP survey also showed that a significant portion of the bond proceeds were used for in-house investment as well as to re-profile the existing debt. Some companies conducted debt management operations to increase the share of local currency debt in 2015.

7. Balance sheets of small and medium-size enterprises (SMEs) appear to be deteriorating, while those of households remain relatively healthy. NPLs for SMEs have increased steadily over the past few years. The NPL ratio for medium-sized firms almost doubled, to 5.2 percent, from 2012 to 2015. In the same period, the NPL ratio for small enterprises rose from 5.8 to 8.4 percent. NPL ratios for microenterprises, consumer, and mortgage loans remain relatively low, although they have edged up slightly. The stock of FX mortgage loans has continued to decline

[3] For the *Cajas Municipales*, mining loans (to small local producers) constitute 0.2 percent of their loan portfolio, with the corresponding sectoral NPL ratio at 15.3 percent as of December 2015. For *Cajas Rurales de Ahorro y Credito,* almost 1/3 of their loan portfolio is concentrated in agriculture, with a 7.1 percent NPL ratio in the sector.

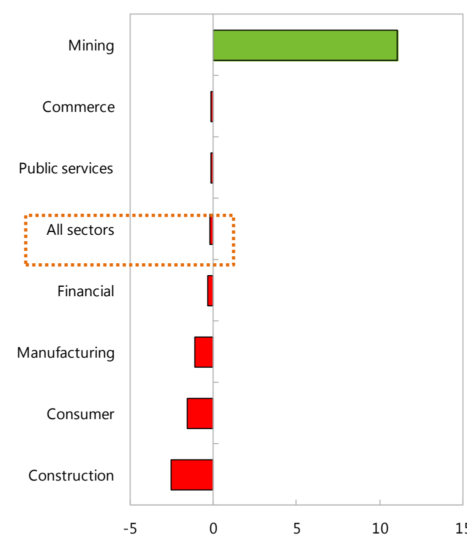
and reached 24 percent of total mortgages in January 2016. Around 15 percent of debtors have a debt-to-income ratio above 40 percent, which is considered high by international standards, however this is concentrated within the high income segment and driven by mortgages.

FX Assets/FX Liabilities
(In percent)



Sources: Apoyo Consultario and Fund staff calculations.
Note: Estimates based on companies listed on the Lima Stock Exchange.

Estimated FX Earnings due to Exchange Rate Depreciation 1/
(In percent of total earnings)

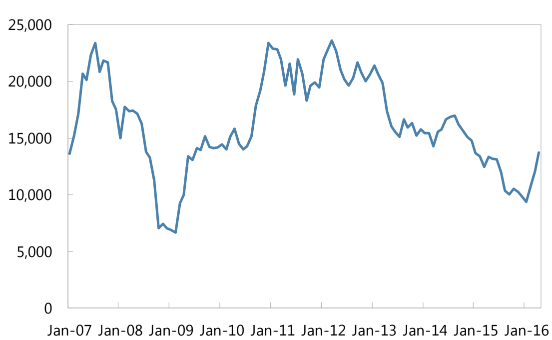


1/ The exchange rate depreciated by 14.4 percent (year-on-year) in 2015.
Sources: Apoyo Consultario and Fund staff calculations.
Note: Estimates based on companies listed on the Lima Stock Exchange.

D. Asset Prices

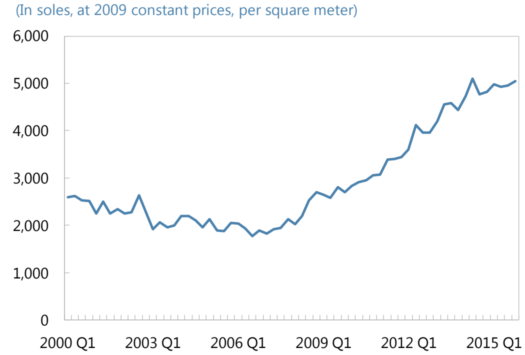
8. Asset price developments do not point to serious risks to either corporations or households. The stock market remains fairly thin and represents a relatively small share of the financial portfolios. Stock prices have been declining since early 2012 in line with commodity prices, but recovered since January 2016 in line with international developments. Measures were taken recently to increase market liquidity. Housing prices, as reflected by the median apartment prices in Lima, appear high although the price increases since the second half of 2014 have been more subdued than in the previous four years (the average annual growth of apartment prices (in constant soles) from 2011 to first half of 2014 was 14 percent). This may not accurately reflect the segmentation in the market, where there is an oversupply of high-end condominiums in certain residential areas in Lima while low-income housing is in short supply.

Lima's General Stock Price Index



Source: Haver.

Median Apartment Prices in Lima
(In soles, at 2009 constant prices, per square meter)



Source: National Authorities.

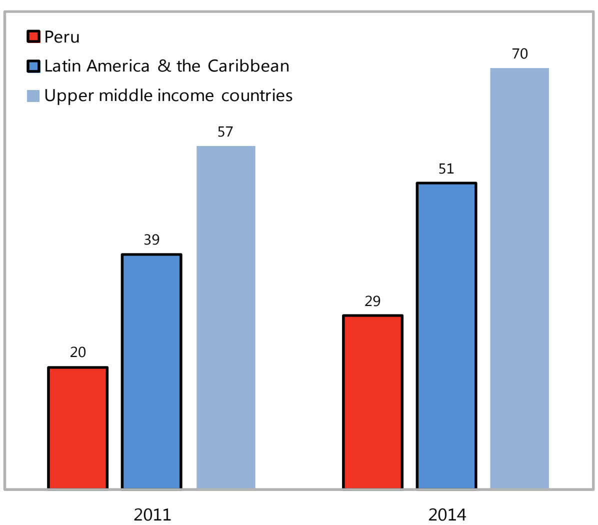
Peru: Progress in Financial Inclusion

Financial inclusion in Peru remains one of the lowest in the region. Only 29 and 12 percent of adults have an account and saved at a formal financial institution, respectively, and credit penetration is only 42 percent. This reflects in part the large informality of the Peruvian economy, as well as geographical challenges in extending financial services to rural areas where a significant segment of the population resides.

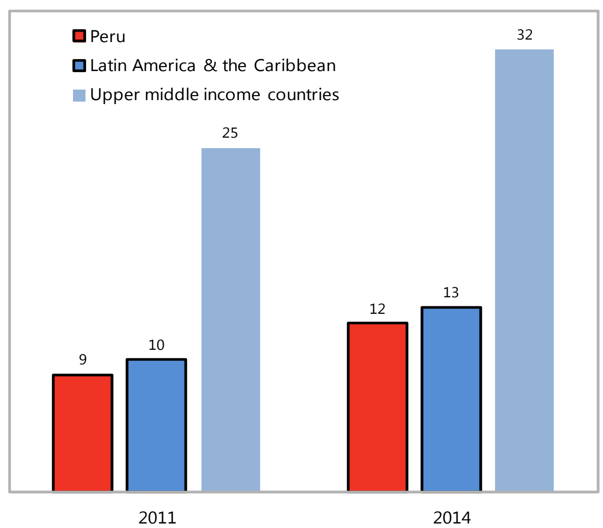
Both public and private sectors have been making inroads into improving access to finance. The authorities (through a multi-sectoral committee) launched the National Financial Inclusion Strategy in July 2015, targeting to increase the access to personal accounts to 50 percent by 2018, and 75 percent by 2021. In the private sector, more than 30 financial institutions and four telecommunications companies formed a partnership, *Modelo Peru*, to jointly build a fully-interoperable mobile money platform (BiM). The creation of this platform was enabled under the 2013 law on electronic money.

BiM is a unique platform with high potential. It is targeting five million users in five years through the use of mobile phones. The platform aims to create a digital ecosystem by enabling services across financial service providers and mobile networks in the country. Users open a simplified transaction account tied to their national ID and phone number, and are able to access the platform even on relatively low-tech devices. As of end-April 2016, there were nine e-money issuers participating, with twenty more expected to join by end-year. Three major telecommunications companies have also joined, with the fourth scheduled to join soon. While it is too early to evaluate the effectiveness of BiM, initial indicators of user take-up are encouraging.

Share of adults with an account at a financial institution



Share of adults who saved at a financial institution



Source: World Bank's Global Findex.

Annex IV. Measures to Improve Tax Revenues

1. **Peru has come a long way in improving the efficiency of the tax system.** In the last 30 years, Peru has successfully progressed from depending largely on trade taxes and a number of small taxes and fees, to a modern regime based on a General Sales Tax (GST) and Income Taxes (IT), with relatively few exemptions. However, tax-to-GDP ratios, slightly above 15 percent, are still below the regional average. The end of the super commodity cycle, 2014 tax rate reductions, and lower potential growth have pushed further down the road raising that ratio to 18 percent, originally a 2016 objective. Continuing social and infrastructure gaps call for alternative revenue enhancing measures to be adopted in the coming years.

2. **Reforming the fiscal regime for the mining sector in 2011 was a remarkable accomplishment.** The government's share in the mining sector was relatively low when the commodity boom started since hardly any royalties were levied and the mining industry benefited from widespread fiscal stability agreements granted by the tax authority. The current administration successfully introduced new profit based and progressive mining royalties, with only a few corporations sticking to their stability agreements. However, with the drop in prices, royalty collections also dropped sharply.

3. **The motivation of the tax reform in 2014 was to spur domestic demand, increase competitiveness of Peruvian corporations, and streamline the tax system.** Income tax and some excise rates were cut, and a number of specific investment incentives were granted; additionally, some important steps were taken to simplify the complex system of withholding and drawbacks. While some of these measures will improve efficiency, several of them will have a significant fiscal cost. Although the cuts to the Corporate Income Tax (CIT) were accompanied with an increase in the withholding tax on dividends, the measure effectively provides more liquidity for companies to reinvest, deferring dividend distributions and hence also tax collection.

4. **Given the new macroeconomic landscape, and lower fiscal intake owing to lower commodity prices and tax rate cuts, the tax policy agenda will need to reemphasize recouping tax revenue losses while overcoming important structural challenges.** The tax agency (SUNAT) still faces the difficult task of enforcing a complex system, in a context of high levels of informality and evasion.

- *Complexity*. The various and widespread GST withholding schemes are costly to manage, but they guarantee a minimum amount of revenue. Enforcing a system more reliant on voluntary compliance may carry some risks, but it is more efficient and Peru has rightly moved in that direction; the system can be further simplified as SUNAT's institutional capabilities are improved. This effort would help reducing the current high level of tax in dispute (tax under litigation is larger than yearly tax revenues), which undercuts the incentive to formalize.

- *Fiscal stability agreements*. There were 877 agreements in 2014, meaning that there were as many potentially different special regimes to control. Aside from the possible distortions and administrative complexity this implies, continuing to grant these agreements is hardly justified;

Peru today has solid macroeconomic, institutional and social credentials, sufficient to foster an attractive investment climate. The reduction in CIT rates should be an opportunity to eliminate a good number of these agreements, as investors may surrender them to benefit from the tax cut.

- *International taxation*. Peru's tax system is adapting to its increasing integration to the world economy, so that cross-border business has clear rules and double taxation is minimized. However, this also entails risks, with increasing exposure to profit shifting and tax base erosion by multinational enterprises. Peru has a number of specific anti-avoidance rules to protect its tax base, which is an appropriate strategy given its administrative capabilities, but some of these rules can be improved.[1] It is important as well that Peru's treaty policy does not undermine this tax base protection in domestic law; special attention should be given to taxation of capital gains on indirect sales of Peruvian assets and improving the capability of exchanging information (Peru has very strict banking secrecy laws).

- *Subnational taxation (property tax)*. Local revenues are relatively low in Peru and there is ample space to increase property tax collection. An essential aspect of this effort should to be to change how properties are valued for tax purposes, bringing the base closer to market values, together with modernizing the administration of local cadastres. This would not only increase revenues, but also improve the progressivity of the whole system

- *Subnational taxation (canon).* The decline in commodity prices has underscored the inappropriateness of too-heavy reliance on volatile natural resource revenue, and the assignment of the mining *canon* to subnational governments should be revisited—with the goals of switching to more stable sources of income for subnational governments, achieving a better distribution of *canon* across localities affected by the mineral extraction, and using the *canon* more effectively to fund larger infrastructure projects.

[1] See an accompanying *Selected Issues Paper*, Chapter 4.

INTERNATIONAL MONETARY FUND

PERU

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

June 3, 2016

Prepared By

The Western Hemisphere Department
(In consultation with other departments)

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FUND RELATIONS

(As of May 31, 2016)

Membership Status: Joined 12/31/1945; accepted the obligations of Article VIII, Sections 2(a), 3, and 4 on 2/15/1961.

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	1334.50	100.00
Fund holdings of currency	1304.17	97.73
Reserve Tranche Position	30.38	2.28

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	609.89	100.00
Holdings	531.11	87.10

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-By	Jan. 26, 2007	Feb. 28, 2009	172.37	0.00
Stand-By	Jun. 09, 2004	Aug. 16, 2006	287.28	0.00
Stand-By	Feb. 01, 2002	Feb. 29, 2004	255.00	0.00

Projected Payments to Fund[1]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2016	2017	2018	2019	2020
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.04	0.05	0.05	0.05	0.05
Total	0.04	0.05	0.05	0.05	0.05

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Arrangements

Peru maintains a unified, floating exchange rate. On December 31, 2015, the average of interbank buying and selling rates was 3.38 soles per U.S. dollar. The exchange system is free of restrictions, except for those maintained solely for the preservation of national or international security, and which have been notified to the Fund pursuant to Executive Board Decision No. 144–(52/51).

Last Article IV Consultation

The 2015 Article IV consultation was concluded on May 20, 2015 (IMF Country Report No. 15/133).

FSAP and ROSCs

Several joint Fund-Bank missions visited Lima in the period September 2000–January 2001 to conduct an FSAP for Peru. The corresponding Financial System Stability Assessment (FSSA) report was discussed by the Executive Board on March 12, 2001. A follow-up FSAP mission was concluded in February 2005. More recently, the Executive Board, on April 20, 2011, took note of the staff's analysis and recommendations in the report on Peru's FSAP-Update. In October 2002, an FAD mission conducted a Fiscal ROSC for Peru (IMF Country Report No. 04/109, 4/16/04), while an STA mission conducted a Data ROSC for Peru in February 2003 (IMF Country Report No. 03/332, 10/24/03).

Technical Assistance

A list of technical assistance provided to Peru in the last several years is provided in Annex V.

Department	**Purpose**
FAD	Treasury management
	Macro-fiscal framework and fiscal rules
	Tax policy and administration
	Fiscal Transparency Evaluation
	General Tax Policy
MCM	Developing fixed income swap markets
LEG	Risk based supervision of securities markets

Resident Representative

Mr. Alejandro Santos became the Senior Resident Representative in Peru in December 2014. The office will close as of end-July 2016, and Mr. Santos will relocate to Asunción, Paraguay.

WORLD BANK RELATIONS

(As of March 29, 2016)

A. Bank Group Strategy

The World Bank Group support to Peru is defined in the Country Partnership Strategy (CPS) approved by the Board on February 1, 2012. The CPS is closely aligned with the Government's strategic vision of strong economic growth with greater inclusion and is focused on four strategic objectives: (i) increased access and quality of social services for the poor; (ii) connecting the poor to services and markets; (iii) sustainable growth and productivity; and (iv) inclusive governance and public sector performance. The CPS also addresses cross-cutting issues such as those of governance and gender. The CPS is a result of extensive consultations with government and civil society.

The indicative lending program is at about US$250 million per annum, reflecting Government's interest in policy reform support through Development Policy Lending and in reform implementation support through an investment lending program. The strategy includes development policy lending operations in the fiscal, social, and environmental sectors mainly through deferred drawdown options.

Peru's current lending portfolio includes 20 active projects with a commitment of US$1.7 billion and an undisbursed balance of US$1.5 billion. In addition to 14 on-going investment lending operations, there are two active DPL-DDOs (Development Policy Loans with Deferred Drawdown Option) and two DPL with a CAT DDO (Catastrophes Deferred Drawdown Options) and two GEFs. The GOP took the DPL-DDOs during the 2008–09 global financial crisis as part of its overall strategy to ensure adequate contingency funding. New lending commitments since the start of the CPS period total US$310 million in seven new projects. Some large investment projects (for example, the Lima Metro II project) and a new CAT-DDO are expected to increase the commitment amounts significantly during the second half of the CPS implementation period (FY 15–FY 16).

As Peru is becoming a stronger middle income country, demand for knowledge services is increasing. This growing demand for knowledge is reflected in the increase in the number of Reimbursable Advisory Services (RAS) arrangements in Peru with the Bank in Education, Social Protection, Financial Inclusion, Disaster Risk Management, Water Resource Management, Water Supply and Sanitation, and Justice sectors. In addition to this new stream of RASs, the Bank has continued to provide analytical services, hands-on support to improve capacities, South-South and South-North knowledge exchanges and just-in-time support on a variety of issues as demanded by the clients.

Finally, the Bank's TF portfolio (currently over US$21 million considering GEF) complements other WB support in the current core engagement areas of this CPS by providing valuable Analytic and Advisory Activities and technical assistance. They support the harmonization and alignment of funding from various development partners behind core government programs.

B. Bank-Fund Collaboration in Specific Areas

OECD. Peru has formally declared its intention to join the OECD by 2021. In July 2014, Peru's Minister of Finance requested support from the WBG for the preparation of the Country Program that consists essentially of about 18 OECD institutional assessments of Peru. While the Bank is finalizing the framework for this technical assistance, it will coordinate the work with other development partners, including with the Fund.

Policy notes. To support the policy debate heading into the Peruvian political transition next July 2016, the WBG will complete a series of policy notes in FY 16. Areas of analysis include: food chains and nutrition, diversified growth, development of mid-sized cities, and connectivity.

Tax reform and fiscal decentralization. While the Fund has been active in providing various technical assistance missions in the tax area, the Bank has finalized a study on Taxation and Equity, looking at the challenges of increasing tax collection equitably. Jointly with the World Bank and IDB, staff has worked on drafting laws and regulations for fiscal decentralization. The World Bank has also focused on the design and implementation of decentralization of the social sectors and pro-poor spending policies.

Customs administration modernization. A needs assessment mission was undertaken together with the IMF to develop an action plan for modernizing customs administration. The joint team presented a technical report to SUNAT.

Public sector management. Bank-Fund collaboration has focused in the area of results based budgeting, the implementation of a Treasury Single Account and modernization of budget processes, institutions and information systems.

Peru: World Bank Portfolio Status

As of March 29, 2016

(In millions of U.S. dollars)

Project Name	Practice name	Board Approval	Net Comm Amt ($m)	Tot Disb ($m)	Tot Undisb Bal ($m)	% Disb
Investment						
PE Sierra Rural Development Project	Agriculture	04/24/2007	39.8	34.3	5.5	86.2%
PE-Sierra Irrigation	Water	07/27/2010	20.0	18.8	1.2	93.9%
PE Justice Services Improv. II	Governance	11/18/2010	20.0	18.7	1.3	93.3%
PE Optimization of Lima Wat & Sewerage	Water	04/07/2011	109.5	53.0	56.5	48.4%
PE Results Nutrition for Juntos SWAp	Social Protection & Labor	03/08/2011	25.0	18.0	7.0	72.1%
PE Cusco Regional Development	Social, Rural, Urban and Resilience	11/22/2013	35.0	0.0	35.0	0.0%
PE Second Rural Electrification	Energy and extractives	04/21/2011	50.0	28.4	21.6	56.9%
PE HIGHER EDUCATION QUALITY IMPROVEMENT	Education	12/04/2012	25.0	5.4	19.6	21.4%
PE Basic Education	Education	01/17/2013	25.0	5.4	19.6	21.6%
PE-Strengthening Sust Mgmt Guano Islands	Environment & Natural Resources	12/06/2013	8.9	3.1	5.8	34.4%
PE-National Ag. Innovation Program	Agriculture	12/17/2013	40.0	1.3	38.7	3.3%
PE Social Inclusion TAL	Social Protection & Labor	12/13/2012	10.0	6.5	3.5	65.4%
PE Cusco Transport Improvement	Transport and ICT	02/28/2014	120.0	0.4	119.6	0.3%
PE Support to the Subnational Transport	Transport and ICT	12/11/2015	50.0	0.0	50.0	0.0%
PE - Lima Metro Line 2 Project	Transport and ICT	09/15/2015	300.0	0.0	300.0	0.0%
Dedicated Grant Mechanism in Peru	Environment & Natural Resources	09/11/2015	5.5	0.0	5.5	0.0%
Adjustment						
PE CAT DDO II	Social, Rural, Urban and Resilience	03/12/2015	400.0	0.0	400.0	0.0%
PERU CAT DDO	Social, Rural, Urban and Resilience	12/09/2010	100.0	0.0	100.0	0.0%
Pub. Exp. and Fiscal Risk Mgmt DPL-DDO	Macro and Fiscal management	02/11/2016	1,250.0	0.0	1,250.0	0.0%
PE Boost. Hum. Cap. and Productivity DPL	Macro and Fiscal management	02/11/2016	1,250.0	0.0	1,250.0	0.0%
Total			**3,883.8**	**193.3**	**3,690.5**	**5.0%**

International Financial Corporation Portfolio

As of April 25, 2016

(In millions of U.S. dollars)

Commitment Fiscal Year	Institution Short Name	LN Cmtd - IFC	LN Repayment - IFC	ET Cmtd - IFC	QL + QE Cmtd - IFC	GT Cmtd - IFC	RM Cmtd - IFC	ALL Cmtd - IFC	ALL Cmtd - Part	LN Out - IFC	ET Out - IFC	QL + QE Out - IFC	GT Out - IFC	RM Out - IFC	ALL Out - IFC	ALL Out - Part
2013/ 2015	APMTC	51.8	5.8	-	-	-	7.5	59.2	188.5	51.8	-	-	-	2.9	54.7	188.5
2011	Arequipa Region	-	-	-	-	0.6	-	0.6	-	-	-	-	0.6	-	0.6	-
2013/ 2007/ 2011/ 2008	B.Continental	25.7	79.9	-	-	-	-	25.7	-	25.7	-	-	-	-	25.7	-
	BPZR	-	-	-	9.9	-	-	9.9	-	-	-	9.9	-	-	9.9	-
2016	BTST	-	-	2.0	-	-	-	2.0	-	-	2.0	-	-	-	2.0	-
2009/ 2010/ 2013/ 2014/ 2007/ 2011/ 2016/ 2012	BanBif	15.0	15.0	37.9	-	15.0	-	67.9	-	15.0	37.9	-	15.0	-	67.9	-
2015/ 2016	Banco Financiero	-	-	-	-	27.1	-	27.1	-	-	-	-	27.1	-	27.1	-
2009/ 2007/ 2004	Cartones America	-	-	-	-	-	0.2	0.2	-	-	-	-	-	-	-	-
2015/ 2012	Compartamos Peru	4.3	7.5	-	-	-	-	4.3	-	4.3	-	-	-	-	4.3	-
2010	Enfoca	-	-	10.4	-	-	-	10.4	-	-	10.0	-	-	-	10.0	-
2009/ 2014/ 2011	F. Confianza	14.8	9.1	12.0	-	-	-	26.8	-	14.8	12.0	-	-	-	26.8	-
2015	HMC Capital	-	-	10.5	-	-	-	10.5	-	-	2.8	-	-	-	2.8	-
2015	La Positiva Gen	-	-	-	18.0	-	-	18.0	-	-	-	18.0	-	-	18.0	-
2007/ 2000	Laredo	3.8	24.2	-	-	-	0.8	4.5	-	3.8	-	-	-	0.3	4.0	-
2007	Lima JCIAirport	-	-	16.8	-	-	-	16.8	-	-	13.4	-	-	-	13.4	-
2006/ 2007/ 2016/ 2002/ 2008/ 2012	MIBANCOPERU	54.6	42.2	-	7.0	-	-	61.6	0.0	54.6	-	7.0	-	-	61.6	-
2014	PEIP	-	-	21.8	-	-	-	21.8	-	-	7.7	-	-	-	7.7	-
2008	Peru LNG	222.9	77.1	-	-	-	-	222.9	-	222.9	-	-	-	-	222.9	-
2015	Tinka	-	-	1.8	-	-	-	1.8	-	-	1.8	-	-	-	1.8	-
2001/ 2012	UPC	26.6	7.1	-	-	-	-	26.6	-	26.6	-	-	-	-	26.6	-
2000/ 1995/ 1994	Yanacocha	-	12.0	0.3	-	-	-	0.3	-	-	0.3	-	-	-	0.3	-
Total Portfolio		**419.5**	**279.9**	**113.5**	**34.9**	**42.7**	**8.5**	**619.2**	**188.5**	**419.5**	**88.0**	**34.9**	**42.7**	**3.2**	**588.3**	**188.5**

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

A. Country Strategy

Peru's current Country Strategy covers the period 2012–16. The strategy has two pillars for the Bank's assistance to the Peruvian authorities by supporting (i) their efforts to close economic and social gaps that still persist between urban and rural areas; and (ii) productivity gains as the main basis for inclusive, and sustainable economic growth.

IDB's strategic engagement with Peru focus on nine areas: (i) social inclusion; (ii) rural development and agriculture; (iii) housing and urban development; (iv) climate change and disaster risk management; (v) water, sanitation, water resources, and solid waste; (vi) energy; (vii) transportation; (viii) public management; and (ix) competitiveness and innovation.

The Country Strategy is under implementation. The Bank has worked with the government on a multi-sector and multi-annual approach of articulated interventions addressing, in a coordinated fashion, various development gaps at the same time. Also, the Bank's intention is to diversify the instruments of support to the country. Innovation in instruments include service contracts with the government in priority areas ("fee for services"), larger private sector operations, and extended use of knowledge sharing and technical cooperation.

The Bank's financial engagement scenario would entail negative net flows to the country between 2012 and 2016, particularly because of the Peruvian early repayment in 2013 to the IDB of 5 loan balances for a total amount of US$1,232 million. However, this does not affect the base scenario, where the Bank will maintain its share as a creditor in Peru's total multilateral debt. The lending framework for the strategy is consistent with the demand assumptions and the external financing strategy of the government.

B. Lending

As of March 2016, the Bank's portfolio of active, public sector operations consisted of 22 loans for a total amount of US$1,479 million, including 2 policy-based loans with a deferred disbursement modality for a total amount of US$600 million. The rest of the active portfolio consists of 20 loans for an amount of US$879 million, of which US$220.4 million (25 percent) have been disbursed. The public sector lending program for 2015 comprised five operations for a total of US$700 million, including the 2 policy-based loans for US$300 million each. The public sector lending program for 2016 comprises three investment loans for a total amount of US$200 million.

Regarding private sector operations, the active portfolio of the IDB Group amounts to US$670.2 million. The IDB Group private sector operations are distributed in the following sectors: Oil and Gas, 44 percent; Energy, 24 percent; Financial Intermediaries, 20 percent; Agro-business, 6 percent; Education, 5 percent; and Tourism, 1 percent.

Peru: IDB Sovereign Guaranteed Loan Portfolio by Sector
As of March 2016
(In millions of U.S. dollars)

Sector	Commitments	Disbursements	% Disbursed
Agriculture	95.0	0.9	1
Science, Technology and Competitiveness	35	21.1	61
Social Investment	670.0	31.0	5
Modernization of the State	111.0	51.4	46
Integration and Trade	20	0	0
Water and Sanitation	124.8	21.3	17
Transportation	423.9	94.7	22
Total	1,479.8	220.4	15

STATISTICAL ISSUES

General. Macroeconomic statistics are broadly adequate for policy formulation, surveillance, and monitoring. Peru subscribes to the Special Data Dissemination Standard (SDDS). A data ROSC was prepared and published in 2003.

Despite progress in recent years, there is scope for improvement in the following areas: (i) coordination among the agencies that compile official statistics to avoid duplication of efforts; (ii) expanding the coverage of the wholesale price index to include mining, oil and gas extraction, electricity and water, public transportation, and communication; (iii) finalizing the migration to the standardized report forms for monetary data with the introduction of report forms for the central bank, other depository corporations, and other financial corporations; and (iv) expanding the scope of data sources for compiling financial flows of individual residents.

National accounts. In 2014, the National Statistics Office (INEI) released a new national account series implementing the 1993 SNA and using 2007 as the base year.

Price statistics. At the present time, the official measure of inflation for Peru is the CPI for Metropolitan Lima, compiled and published by INEI. Starting in January 2010, the Metropolitan Lima CPI has been compiled using updated weights based on the 2008/09 Encuesta Nacional de Presupuestos Familiares (ENAPREF). Since January 2011, city level indices have been compiled and disseminated for the 24 departmental capitals and another large urban area using weights from the 2008/09 ENAPREF and a methodology matching that employed for the Metropolitan Lima CPI. A new law issued in 2009 requires the INEI to compile a new national level CPI that will serve as the official CPI for Peru in the future. An STA mission on the CPI was conducted in May 2–13, 2011 to evaluate the methodology of the new national CPI index. The new national level CPI, starting with the January 2012 index, was disseminated since February 2012 The WPI, statistical techniques used to compile the index generally follow international standards but the weights for the WPI are outdated, and were derived from the 1994 input-output table and other reports and publications of relevant ministries.

Labor market statistics. The authorities monitor labor market developments using four indicators: open unemployment, underemployment, employment, and remunerations. While monthly unemployment, employment and income data for metropolitan area of Lima from INEI are timely, only urban employment indexes are available from the Ministry of Labor for other areas and with some delays; monthly remuneration data for the government are timely but the monthly remuneration data for the private sector are no longer available. The nationwide unemployment and underemployment situation is surveyed quarterly. It would be useful to expand the coverage of labor statistics to national level and develop competitiveness indicators such as productivity and unit labor cost indexes.

Government financial statistics. The Central Bank (BCRP) compiles government finance statistics (GFS) following the GFSM2001, for the general government and its subsectors. Data for all subsectors are reported on a cash basis and financial assets and liabilities are reported at face value. The authorities have not yet sent to the Fund information on the components of expenditures by function. The coverage of published national budget data is narrower than the fiscal statistics prepared for the combined public sector. The authorities report data for publication in the Government Finance Statistics Yearbook (GFSY) using the GFSM 2001. No high frequency data is reported for publication in International Financial Statistics (IFS).

Monetary statistics. The BCRP compiles and publishes the analytical accounts of the central bank, depository corporations, and financial corporations broadly in line with the methodology recommended by the Monetary and Financial Statistics Manual. The main divergences are the exclusion of the deposits of other financial corporations, state and local governments, and public nonfinancial corporations from the definition of broad money; and valuation of some financial assets held to maturity at cost rather than at market prices or at the lower of cost or market price for investment securities. At the request of the authorities, a mission visited the country in January 2007 to assist with the migration to the new standardized report forms (SRFs) for reporting monetary data to the IMF. The mission finalized the SRF for the central bank, recommending improvements in the classification and sectorization of some accounts. A follow-up mission took place in September 2008. The mission completed the work on the SRF for the central bank and developed a bridge table linking the source data reported by banks to the BCRP to the report form 2SR (other depository corporations). The mission identified shortcomings in the management of the database that generate the accounts of the other depository corporations sector at the BCRP. Although the two technical assistant missions finalized the groundwork for the migration to the SRFs, the BCRP has not yet started reporting monetary data using the SRFs. No set date is foreseen for the migration to the SRFs.

Financial soundness indicators. Peru started reporting data and metadata for financial soundness indicators (FSIs) with a quarterly frequency in June 2011.

External sector statistics. The BCRP prepares quarterly data on the balance of payments and international investment position largely in line with the recommendations of the fifth edition of the Balance of Payments Manual (BPM5). Data are reported to the Fund for publication in the IFS and the Balance of Payments Statistics Yearbook. Departures from BPM5 include the lack of coverage of assets held abroad and land acquisition abroad by residents; and not recording on an accrual basis some external debt transactions.

The BCRP has been reporting since August 2001 weekly data on international reserves in accordance with the Operational Guidelines for Data Template on International Reserves and Foreign Currency Liquidity. Since August 2006, the BCRP is including the full amount of the liquidity requirements in the reserve template both under official reserve assets and as a contingent net drain (as specified in Section III of the Data Template). Peru disseminates quarterly data on external debt with an eight week lag on the National Summary Data Page with a hyperlink to the Fund’s website.

Peru: Table of Common Indicators Required for Surveillance
(As of March 31, 2016)

	Date of Latest Observation	Date Received	Frequency of data[7]	Frequency of Reporting[7]	Frequency of Publication[7]	Memo Items: Data Quality – Methodological Soundness[8]	Memo Items: Data Quality Accuracy and Reliability[9]
Exchange Rates	03/30/16	03/31/16	D	M	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	12/31/15	03/09/16	D	M	W		
Reserve/Base Money	12/31/15	03/09/16	W	M	W	O, LO, LO, LO	O, O, O, O, O
Broad Money	12/31/15	03/09/16	W	M	W		
Central Bank Balance Sheet	12/31/15	03/09/16	W	M	W		
Consolidated Balance Sheet of the Banking System	12/31/15	03/09/16	W	M	W		
Interest Rates[2]	12/31/15	03/09/16	D	M	D		
Consumer Price Index	03/30/16	04/01/16	M	M	M	O, LO, LO, LO	LO, LO, O, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – CG and GG[4]	Q4 2015	03/12/16	Q	Q	Q	O, LO, O, O	O, O, O, LO, O
Stocks of CG Debt[5]	Q4 2015	03/12/16	Q	Q	Q		
International Investment Position[6]	Q4 2015	02/20/16	Q	Q	Q		
External Current Account Balance	Q4 2015	02/20/16	Q	Q	Q	O, LO, LO, LO	LO, LO, O, O, O
Exports and Imports of Goods and Services	Q4 2015	02/20/16	M	M	M		
GDP/GNP	Q4 2015	3/05/16	Q	Q	Q	LO, LO, LO, LO	LNO, LNO, LNO, LO, LO
Gross External Debt	Q4 2015	02/20/16	Q	Q	Q		

[1] Every Friday the central bank disseminates daily net international reserves, and weekly International Reserve Assets and Reserve Liabilities.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Central government (CG) and general government (GG) revenue and expenditure data are available monthly; and the composition of financing are available quarterly. Financing comprises of foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including type of instrument, maturity and type of creditor.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

[8] Reflects the assessment provided in the data ROSC published in October 2003 and *based* on the findings of the mission that took place during February 12–26, 2003 for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning (respectively) concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), not observed (NO), or not available (NA).

[9] Same as footnote 7, except referring to international standards concerning (respectively) source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.