INTERNATIONAL MONETARY FUND

IMF Country Report No. 17/166

PERU

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; AND STAFF REPORT

June 2017

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 2017 Article IV consultation with Peru, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its June 16, 2017 consideration of the staff report that concluded the Article IV consultation with Peru.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on June 16, 2017 following discussions that ended on May 16, 2017, 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 1, 2017.
- 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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INTERNATIONAL MONETARY FUND
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Press Release No. 17/252
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June 28, 2017

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2017 Article IV Consultation with Peru

On June 16, 2017, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Peru.

With average growth of over 5¼ percent since 2000, Peru has significantly reduced unemployment and poverty. Inflation is in low single digits, the fiscal position has strengthened, and dollarization has declined markedly. In the context of the commodity boom, sound macroeconomic management and structural reforms have played an essential role in this improvement.

The current juncture is, however, a difficult one, given domestic headwinds and challenging external conditions. The Odebrecht corruption scandal that broke in December 2016 is weighing on investment and confidence. And one of the worst flooding and landslides in over 50 years (related to el Niño) has affected a significant part of the population, caused widespread infrastructure damage, and raised domestic food prices. On the external side, although commodity prices have recovered somewhat since late 2016, they remain significantly lower than during the commodity boom.

While slowing in the short term given sizable domestic shocks and a smaller contribution from new export projects, growth is expected to remain high relative to the region. In particular, GDP growth is projected to slow to about 2.7 percent in 2017 (supported by a significant fiscal stimulus) before bouncing back to over 3¾ percent in 2018, as reconstruction spending filters through the economy and projects delayed due to the Odebrecht scandal start to catch-up. Inflation should gradually return to the target range as weather-related factors abate and food price inflation declines.

[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.

Executive Board Assessment[2]

Executive Directors commended the authorities for steadfast implementation of sound macroeconomic policies and reforms which have helped Peru achieve high growth and significant improvement in social indicators over the past two decades. Directors noted, however, that recent external and domestic challenges, including those arising from lower commodity prices, the Oderbrecht scandal, and the devastating floods, are expected to adversely affect the economy in the near term. They praised the authorities for their immediate countercyclical response to these shocks, and concurred that continued sound macroeconomic management and strong structural reforms are key to sustaining growth and enabling Peru to reach its goal of high-income status in the long run.

Directors supported the short-term fiscal stimulus plan to address flood-related reconstruction needs, stressing that such spending should be underpinned by strong public investment management. They took note of the transparency gains in the modified structural balance fiscal rule, and advised the authorities to remain vigilant given the new rule's potential for procyclicality. Directors welcomed the authorities' commitment to gradual medium-term fiscal consolidation and supported their plan to establish a medium-term budget framework as a tool to enhance fiscal discipline and the predictability of the budget process. They encouraged the authorities to push forward with their efforts to raise the tax-to-GDP ratio, particularly by strengthening tax administration and reducing VAT exemptions and economic informality. They also welcomed the recent reforms to the frameworks for public investment and public-private partnerships, which would help address the infrastructure gap.

Directors considered the accommodative monetary policy stance to be appropriate at the current juncture. They encouraged the authorities to continue to make decisions depending on data and to monitor inflation expectations closely. Directors stressed that clear communication of the temporary nature of existing price shocks and the inflation outlook would be essential to anchor inflation expectations. They welcomed the increased exchange rate flexibility and recommended that future interventions be limited to cases of disorderly market conditions.

Directors observed that the financial sector remains stable, while noting the need for continued focus on reducing dollarization to further mitigate currency mismatches and balance sheet vulnerabilities. They encouraged further action to formalize the financial stability council and to broaden the financial supervisory perimeter. While emphasizing that financial stability should remain a priority, Directors highlighted the importance of enhancing financial deepening and inclusion.

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Directors emphasized that implementation of strong structural reforms is critical to raise growth potential and achieve the high-income status. Along with efforts to close the infrastructure gap, they called for further efforts to increase labor market flexibility, reduce economic informality, and improve business environment and fight corruption. Directors also emphasized the need for stronger implementation of anti-corruption and AML/CFT measures.

Table. Peru: Selected Economic Indicators

	2011	2012	2013	2014	2015	Projections 2016	2017	2018
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	94.0	...	...	...
Poverty rate (total) 1/	27.8	25.8	23.9	22.7	21.8	20.7	...	...
Unemployment rate	7.7	6.8	5.9	5.9	6.5	6.7	...	...
	(Annual percentage change; unless otherwise indicated)							
Production and prices								
Real GDP	6.5	6.0	5.8	2.4	3.3	3.9	2.7	3.8
Real domestic demand	7.7	7.3	7.3	2.2	3.1	0.9	2.4	3.7
Consumer Prices (end of period)	4.7	2.6	2.9	3.2	4.4	3.2	2.9	2.5
Consumer Prices (period average)	3.4	3.7	2.8	3.2	3.5	3.6	3.1	2.6
External sector								
Exports	29.5	2.2	-9.6	-7.8	-12.9	7.6	12.9	4.5
Imports	28.9	10.4	3.3	-3.1	-9.0	-5.9	6.3	5.0
Terms of trade (deterioration -)	7.0	-2.3	-5.2	-5.4	-6.4	-0.7	5.0	-0.8
Real effective exchange rate (depreciation -)	-1.4	8.1	-0.2	-1.6	0.8	-2.3	...	...
Money and credit 1/ 2/								
Broad money	15.1	12.5	15.3	9.5	11.6	4.3	5.2	7.8
Net credit to the private sector	21.6	13.3	18.3	13.2	14.0	5.0	5.2	6.5
	(In percent of GDP; unless otherwise indicated)							
Public sector								
NFPS Revenue	27.5	28.3	28.4	28.0	25.1	23.2	23.1	23.2
NFPS Primary Expenditure	24.2	24.8	26.4	27.1	26.0	24.7	24.8	25.3
NFPS Primary Balance	3.3	3.5	2.0	0.9	-1.0	-1.5	-1.7	-2.1
NFPS Overall Balance	2.1	2.4	0.9	-0.2	-2.0	-2.6	-3.0	-3.5
External Sector								
External current account balance	-1.9	-2.7	-4.4	-4.4	-4.8	-2.7	-2.1	-2.1
Gross reserves								
In millions of U.S. dollars	48,859	64,049	65,710	62,353	61,530	61,731	61,731	62,931
Percent of short-term external debt 3/	559	496	536	534	523	450	410	604
Percent of foreign currency deposits at banks	228	300	274	258	224	230	233	236
Debt								
Total external debt	25.9	27.8	27.2	30.6	34.6	33.5	30.0	28.8
NFPS Gross debt (including Repayment Certificates)	23.3	21.6	20.8	20.7	24.0	24.4	25.2	26.4
External	11.5	10.0	9.0	8.7	11.1	10.3	9.9	10.6
Domestic	11.8	11.6	11.8	12.0	12.9	14.1	15.3	15.7
Savings and investment								
Gross domestic investment	24.9	24.7	26.5	24.9	24.6	22.8	22.2	22.2
Public sector 4/	4.9	5.5	5.9	5.5	5.0	4.8	5.2	5.6
Private sector	19.3	20.7	21.2	20.1	19.3	17.7	16.7	16.5
National savings	23.0	22.0	22.0	20.5	19.8	20.1	20.1	20.1
Public sector 5/	7.5	8.2	7.2	6.0	3.8	2.7	2.7	2.7
Private sector	15.5	13.7	14.8	14.4	16.1	17.4	17.3	17.4
Memorandum items								
Nominal GDP (S/. billions)	464.8	498.5	534.7	576.3	612.8	658.7	703.9	747.8
GDP per capita (in US$)	5,731	6,396	6,629	6,586	6,168	6,199	6,568	6,872

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 2017 ARTICLE IV CONSULTATION

June 1, 2017

KEY ISSUES

Context. With average growth of over 5¼ percent since 2000, Peru has significantly reduced unemployment and poverty. Inflation is in low single digits, the fiscal position has strengthened, and dollarization has declined markedly. In the context of a commodity boom, sound macroeconomic management and structural reforms have played an essential role in this improvement. With lower commodity prices now, consolidating these gains and further reforms—including financial deepening and labor reforms—will be critical in helping Peru reach its target of high-income status. The government has introduced several structural reforms aimed at modernizing the economy, increasing formality, and lifting potential growth. But the current juncture is a difficult one given domestic headwinds and challenging external conditions. These include the Odebrecht scandal, one of the worst flooding and landslides in over 50 years, the lack of a majority in Congress, and significant uncertainty surrounding the U.S. outlook and how much protectionist pressures will rise globally.

Outlook and Risks. Growth is expected to weaken in 2017 to 2.7 given the impact of the Odebrecht scandal and notwithstanding a stimulus plan. A bounceback should take place in 2018–19, reflecting reconstruction spending, public investment projects, and a recovery in private sector investment, after which growth is expected to converge to potential of 3¾ percent in the medium term. Especially in 2017, risks to the outlook are tilted to the downside, with potential for larger than expected flood-related damage, further delays in implementing investment projects, and new spillovers from the Odebrecht investigation. There is some upside potential in the medium term, however, if reforms are implemented faster, or commodity prices are higher, than in the baseline.

Policy Advice. In the context of domestic headwinds and challenging external conditions, a combination of countercyclical policies and structural reforms is appropriate. In the short term, agile fiscal and monetary policies will help the economy tackle reconstruction needs, while preserving Peru's strong fiscal and inflation anchors. Structural reforms constitute an essential complement to these short-term actions, as lifting potential growth hinges on efforts aimed at closing infrastructure gaps, diversifying the production base, reducing economic informality, deepening financial intermediation, and improving governance, including by fighting corruption and strengthening institutions.

Approved By
Krishna Srinivasan (WHD) and Zeine Zeidane (SPR)

Discussions took place in Lima and Cusco during May 2–16, 2017. The staff team comprised Ravi Balakrishnan (Head), Francisco Roch, Pedro Rodriguez (all WHD), Greetje Everaert (SPR) and Yen Mooi (MCM). Adrian Robles and Irina Sirbu (WHD) provided assistance. Virginia Alonso Albarran (FAD), Raphael Espinoza (RES), and Miguel Segoviano (MCM) contributed to specific sections of the report. Staff met with the Prime Minister, Fernando Zavala, the Minister of Economy and Finance, Alfredo Thorne, the Minister of Labor, Alfonso Grados, the Central Bank Governor, Julio Velarde, other senior government officials, and representatives of the private sector and civil society. Mr. Estrella (OED) also participated in the discussions.

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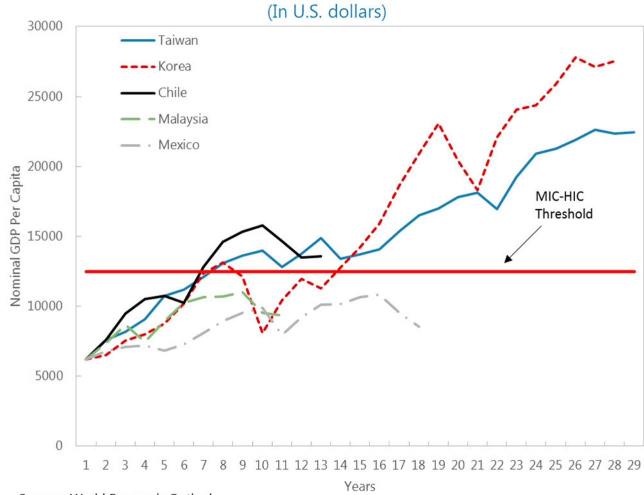
CONTEXT

1. After sustained improvements in macroeconomic and social indicators since the turn of the century, Peru is looking ahead to the challenge of becoming a high-income nation. With average growth of over 5¼ percent since 2000, Peru has significantly reduced unemployment and poverty. Inflation is in low single digits, the fiscal position has strengthened, and dollarization has declined markedly. In the context of a commodity boom, sound macroeconomic management and structural reforms have played an essential role in this improvement. These reforms have largely been in line with past Fund advice (Annex I). Consolidating these gains and pursuing further reforms will be critical in helping Peru reach high-income status. Given the experience of other countries, care will be needed to avoid being stuck in a "middle income trap". Importantly, even if high-income status is attainable, international experience suggests that it will take time (chart).

GDP Per Capita Since Reaching Peru's 2016 Level of Income

(In U.S. dollars)



Sources: World Economic Outlook.

2. The government has introduced several structural reforms to modernize the economy and lift potential growth. They include: (i) a new institutional framework for public and public-private infrastructure investment; (i) improving the business climate by cutting administrative procedures and promoting the digitalization of processes; (iii) a new tax regime for small and medium enterprises; and (iv) enhancing fiscal transparency via a new fiscal rule.[1] The government has also set up a Social Protection Commission tasked with delivering a comprehensive and fiscally sustainable reform of the social security system. The aim of this is to increase coverage while reducing informality.

3. The current juncture is, however, a difficult one given domestic and external headwinds. The Odebrecht corruption scandal that broke in December 2016 is weighing on investment and confidence. This is combined with the worst flooding and landslides in over 50 years (related to El Niño). At the same time, the government does not hold a majority in Congress, potentially posing challenges in passing key reforms going forward. On the external side, although commodity prices have recovered somewhat since late 2016, they remain significantly lower than during the commodity boom. There also remains significant uncertainty about the U.S. outlook and how much protectionist pressures will rise globally.

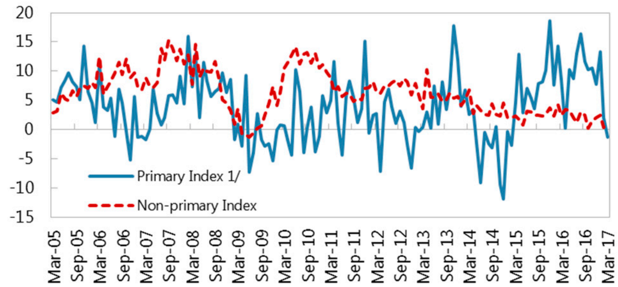
[1] Annex I provides a detailed comparison of the new and previous fiscal frameworks.

RECENT DEVELOPMENTS

4. The economy has been primarily driven by mineral exports and weather-related factors have taken their toll in early 2017:

- *Growth reached 3.9 percent in 2016, strengthening for the second consecutive year, but slowed sharply in 2017Q1* (Figure 1). Exports grew by nearly 10 percent in real terms in 2016, primarily driven by higher mining and hydrocarbon production. Domestic demand, however, grew by less than 1 percent, with credit growth slowing down and private investment declining for the third consecutive year—although part of this reflects the winding down of investment in copper megaprojects. This asymmetry was also evident on the production side—with primary sectors growing by almost 10 percent and nonprimary sectors by around 2¼ percent (chart). The flooding and landslides reduced growth to 2.1 percent (yoy) in 2017Q1 and the current output gap is estimated to be around -1 percent.

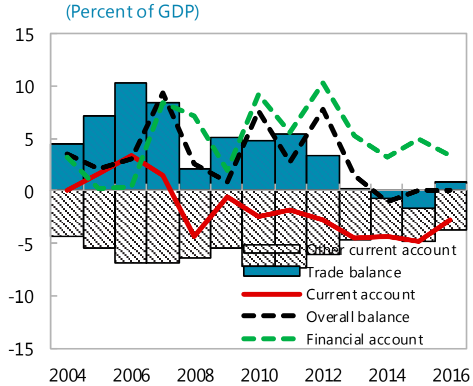
Peru: Real GDP Decomposition
(In percent, year-over-year changes)



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

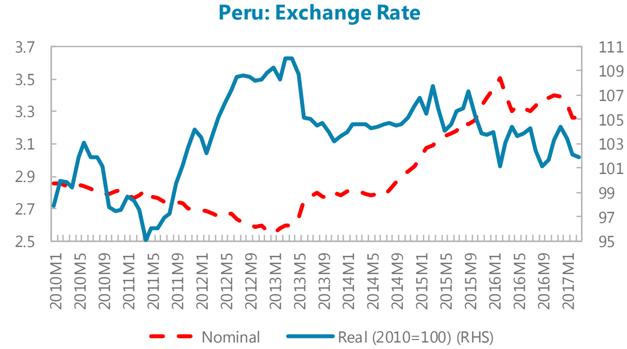
- *Growing exports and subdued domestic demand have translated into an improvement of the current account (Figure 2), and Peru's external position is assessed to be broadly consistent with fundamentals and appropriate policy settings (Annex II)*. The current account deficit fell to around 2¾ percent of GDP in 2016 and the trade balance posted a surplus of nearly one percent of GDP (chart). With the current account norm broadly unchanged in 2016, this improvement narrowed the current account gap compared to 2015, resulting in the exchange rate overvaluation disappearing. The central bank (BCRP) took advantage of the stronger external conditions to

Peru: Balance of Payments
(Percent of GDP)



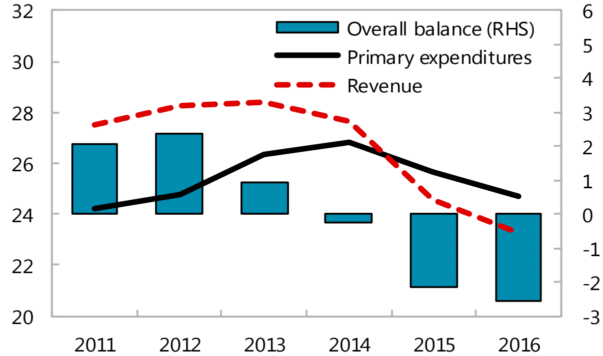
Sources: National authorities; Haver Analytics, and Fund staff estimates.

Peru: Exchange Rate



gradually unwind its stock of foreign exchange (FX) swaps through the year, while reducing intervention in the spot market compared to previous years. Hence, gross international reserves remained broadly unchanged and well above adequacy metrics. While the sol appreciated 1½ percent yoy against the U.S. dollar, the real effective exchange rate was quite stable in 2016 (chart). Appreciation pressures continued in early 2017, with BCRP intervention increasing international reserves.[2]

Fiscal Balance and Key Components
(percent of GDP)

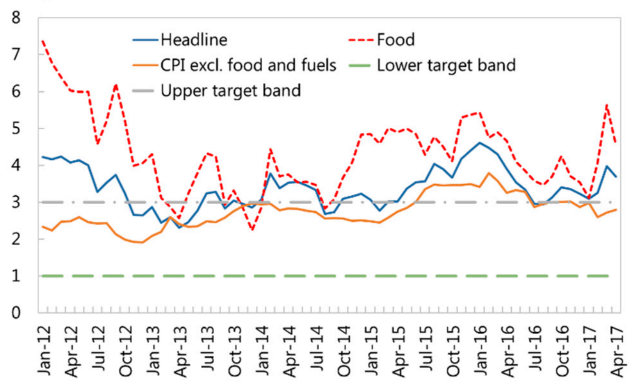


Sources: National authorities; and Fund staff estimates.

- *The deficit of the nonfinancial public sector widened to 2.6 percent of GDP in 2016, a 15-year high* (chart, Figure 3). This mainly reflected weaker consumption taxes (which grew just two percent for the year) and a significant increase in tax refunds to mining companies (associated with past investment in copper megaprojects). These trends continued into early 2017, which also showed weakening income tax growth (a decline of five percent yoy to March).

- *Headline inflation has spiked up close to the peak of early 2016, but core has returned to within the central bank's target band of 1–3 percent.* While weather-related food price increases have kept inflation above the target range in recent months, core inflation (excluding food and fuel) dipped below 3 percent in December and has stayed there since, partly reflecting sol appreciation (chart).

Inflation Developments
(In percent)



Sources: BCRP and IMF staff estimates.

5. **Spillovers from U.S. developments since the November 2016 election have been relatively mild so far** (Figure 4)**.** Peru has small trade and FDI exposures to the U.S. relative to other countries in the region, and both sovereign and corporate spreads have narrowed since the U.S. election, likely reflecting the increase in commodity prices.

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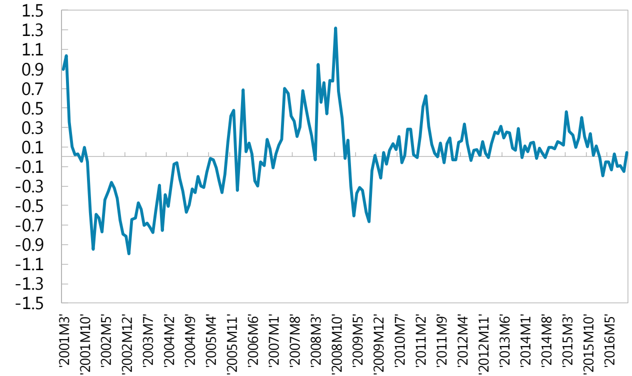
[2] Regarding capital flow management measures (CFMs), foreign exchange derivative transaction limits and taxes on related nonresident gains were relaxed in May 2017 and April 2015, respectively. Relaxation given receding inflows is in line with the Fund's institutional view on capital flows.

6. Banking and corporate indicators remain solid, while financial conditions are neutral with respect to growth. Bank capitalization continued to increase in 2016 (surpassing 15 percent), and profitability remains high (ROA of 2 percent) despite some increase in nonperforming loans (Annex III). Corporate leverage has increased, especially for large firms, but debt at risk (defined as having an interest coverage ratio below 1.5) has halved since 2014. Both loan and deposit dollarization of the banking sector continued to decline in 2016. At around 45 percent, deposit dollarization remains high, but loan dollarization has now fallen below 30 percent. Credit growth moderated steadily through 2016 and in early 2017 (Figure 5). With financial conditions (measured by a Financial Conditions Index) having been neutral in 2016 (chart), the credit slowdown appears to be primarily driven by macroeconomic conditions rather than financial shocks.[3] Pressures in FX and capital markets receded following spikes in early 2016, while balance sheet indicators remain solid (Figures 6 and 7).

A TVP-FAVAR Financial Conditions Index

(Index, 0=neutral, +/-=tight/loose)



Source: IMF staff estimates.

7. The authorities have reacted rapidly to changes in domestic and external conditions. In response to the Odebrecht scandal and floods, the Ministry of Economy and Finance (MEF) has invoked the escape clause of the new fiscal rule and put together a package aimed at supporting growth, including: (i) a fiscal package of 1.3 percent of GDP in 2017 targeted at reconstruction needs and public investment; (ii) an exemption to employers from healthcare contributions (nine percent of monthly wages) when they hire new young entrants to the labor market; (iii) initiatives to support affordable housing developments, and (iv) easing SMEs’ access to financing. To support credit conditions in an environment characterized by higher international interest rates, the BCRP has reduced reserve requirements several times since December 2016 and cut the policy rate by 25 basis points for the first time in 15 months in May 2017.[4] Various anti-corruption measures have been put in place (Box 1).

[3] The FCI is purged of cyclical influences and the direct effects of monetary policy decisions, and represents a common element of a set of over thirty financial indicators. The method combines the estimation of time-varying parameter vector-autoregressions (TVP-VAR) with recent developments in factor analysis for large data sets.

[4] The marginal reserve requirement rate has been reduced from 70 to 44 percent for FX liabilities and from 6½ to 5 percent for domestic liabilities.

Box 1. Odebrecht Corruption Case

Investigations by the Brazilian Federal Prosecution Service, the U.S. Department of Justice, and the Swiss Office of the Attorney General revealed, in late 2016, that the Brazilian construction company Odebrecht paid approximately $29 million in corrupt payments to government officials in Peru to secure public work contracts during 2005–2014. Peru's judicial system has continued the investigations, leading to the incarceration of former government officials and to the extradition request for former President Toledo.

As a consequence, projects related to this and other Brazilian construction companies have stalled. The most prominent example has been the Peruvian Southern Gas Pipeline, which registered no investment in 2017Q1, sharply contrasting with the $405 million spent in 2016Q1. On balance, the authorities estimate that the associated project delays will reduce growth by about 0.3 p.p. in 2017, but assess that exposures of the financial sector to Brazilian construction companies (and related domestic companies) are moderate.

The government started implementing anticorruption measures even before the revelations of the Odebrecht investigation. In October 2016, they passed a law dubbed "Civil Death", which extended bans for corrupt public officials. In early December 2016, the government received the recommendations of the Presidential Commission of Integrity, a subset of which was approved shortly after (e.g., declaration of interests by high-ranking government officials, introduction of anticorruption clauses in contracts for large public projects). Additional steps were also taken following the revelations. These include designating a special investigative team focused solely on the Odebrecht investigation, and barring any company that has admitted/been convicted of corruption from new bids on government projects as well as ringfencing their assets in Peru (hence safeguarding the State's interests).

OUTLOOK AND RISKS

8. **Notwithstanding fiscal support, growth is expected to slow down to 2.7 percent in 2017, with inflation converging to the central bank's 1–3 percent target band.** With the expansion of copper mines largely completed, the contribution of exports to economic growth is projected to decline from nearly 2½ percentage points in 2016 to just over ½ percent in 2017. The slowdown in credit growth is consistent with still negative private investment growth and decelerating consumption. Nonetheless, a planned increase in government investment, combined with the announced stimulus plan—likely also implying a moderately supportive financial conditions index—and the emergency reconstruction funds, are expected to offset part of this decline, with the government contribution to growth increasing by nearly 1 percentage point. Inflation should gradually return to the central bank target, as weather related factors that have pushed food inflation up abate. The fiscal deficit is expected to reach three percent of GDP in 2017, with the significant expenditure increase partially offset by higher-than-budgeted revenues. The latter stem from more favorable commodity prices and other factors (e.g., a tax amnesty for repatriation of profits). Given the higher commodity baseline and a softening of activity, the 2017 current account deficit is expected to narrow to about 2 percent of GDP (for the first time since 2011).

9. **After a bounceback in 2018–19, growth is projected to converge to its potential of 3¾ percent in the medium term and the fiscal deficit to narrow.** The modest bounceback is predicated on reconstruction spending, public investment projects, and a recovery in private sector

investment—partly reflecting a catch-up effect of projects delayed by the Odebrecht case and a corresponding pick up in credit growth. The financial conditions index is projected to be neutral. With the output gap closing by around 2020, the economy is projected to return to its potential growth rate (Box 2). In parallel, the government is forecast to accelerate its consolidation towards the (one percent deficit) target in the fiscal rule and—as private investment starts to recover—the current account deficit is expected to climb back up to around 2¾ percent of GDP, but remain mainly financed by FDI.

10. Risks are tilted on the downside, particularly in 2017. On the external front, increased global spillovers from a rise in protectionism, a slowdown in China, or a more rapid increase in international interest rates could adversely affect Peru via weaker growth of exports and tighter financing conditions. Risks appear greater on the domestic front, and stem from additional delays in executing investment projects and larger than expected flood-related damages (Annex IV).

11. But there are also upside risks. Higher infrastructure spending in systemically important countries could translate into higher commodity prices, improving Peru's terms of trade, which has historically been linked to increases in productivity and growth. In addition, there is still significant untapped potential in the mining sector and structural reforms could proceed at a faster pace if the authorities' reform program gains greater traction than assumed in staff's baseline (e.g., if the recommendations of the Social Protection Commission lead to meaningful labor market reform). This could have a sizable impact on productivity, increasing potential growth to 4–4½ percent.

Box 2. Potential Output

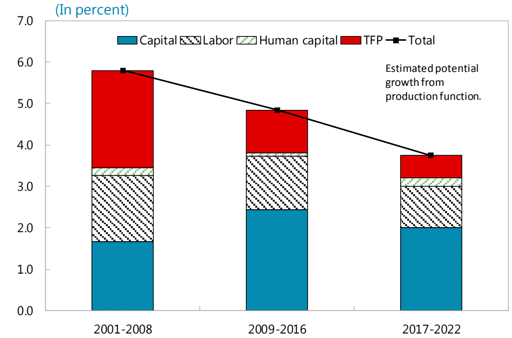
Potential growth has been declining since the end of the commodity boom. Results are relatively robust across different methodologies, including a production function approach, a Hodrick-Prescott filter (HPF), and a multivariate filter (MVF) which incorporates information on inflation (through a Phillips' curve) and unemployment rates. For the period 2001–08, before the Great Recession, Peru's potential output grew at an average rate of 5.7 percent. Post-crisis, the estimate is lower at 5 percent. The production function approach shows that the main drivers of fluctuations in potential growth were TFP and capital accumulation.

Estimates of Potential Growth

	2001-2008	2009-2016	2016	2022 (proj.)
Hodrick-Prescott	5.54	5.05	3.61	-
Multivariate Filter	5.83	5.25	3.94	-
Production Function	5.82	4.83	3.79	3.75
Average	5.73	5.04	3.78	3.75

Source: Fund staff estimates.

Peru. Contributions to Growth
(In percent)

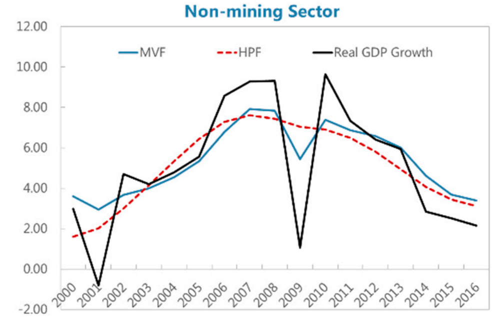


Source: Fund staff estimates.

Peru's non-mining and mining sectors have experienced different potential growth dynamics. As in Blagrave and Santoro (2016), for the non-mining sector the same MVF discussed above is applied. In contrast, for the mining sector it is assumed that the structural price of oil, i.e. long-lasting price changes, affects potential output, while changes in the cyclical component of oil prices affect only the output gap. The MVF follows closely the trend growth estimates from a standard HPF. The results suggest that potential growth in the non-mining sector has slowed significantly since 2009, and is estimated at around 3.4 percent. In contrast, the estimates for the mining sector show a progressive increase since 2004, and have been around 5 percent during the last 6 years.

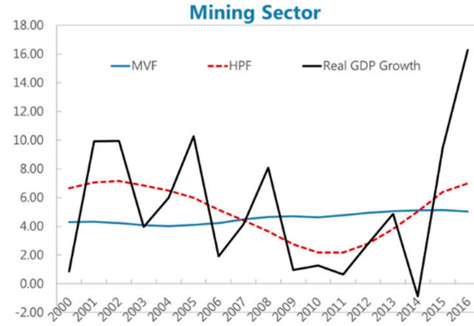
Staff's baseline scenario estimates potential growth in the medium term at about 3¾ percent. Specifically, for 2017–22, it is assumed that: (i) capital accumulates at the rate of investment growth in staff's baseline macroeconomic outlook; (ii) employment grows in line with population forecasts and no change in the labor force participation rate; and (iii) human capital growth remains at its historical rate of 0.3 percent. Predicted TFP values come from a TFP regression model based on changes in the terms of trade and an index of structural reforms. World Economic Outlook (WEO) terms of trade projections are used. Given ongoing reforms to reduce bureaucracy and informality, and increase capacity and efficiency at the agencies managing the public investment system and PPPs, structural reforms are assumed to proceed at a similar pace to during the mid-2000s, still significantly below the 20 b.p. increase in the structural reform index during the 1990s.

Non-mining Sector



Source: Fund staff estimates.

Mining Sector



Source: Fund staff estimates.

Given lower commodity prices, increasing potential growth above 4 percent in the medium term would require undertaking significant reforms to boost investment and productivity. Such a scenario would include Peru reaching Chile's level of the structural reform index by 2022, helping investment grow at a similar pace to during the commodity boom period and TFP increase at around double the rate assumed in the baseline.

POLICY DISCUSSIONS

In the context of domestic headwinds and challenging external conditions, a combination of countercyclical policies and structural reforms is appropriate. In the short term, agile fiscal and monetary policies will help the economy absorb reconstruction needs, while preserving Peru's strong fiscal and inflation anchors. Structural reforms constitute an essential complement to these short-term actions, as lifting potential growth and transitioning towards high-income status hinges on closing infrastructure gaps, diversifying the production base, reducing economic informality, deepening financial intermediation, and improving governance, including by fighting corruption and strengthening institutions.

A. Tackling Multiple Fiscal Objectives

12. A moderate and temporary fiscal loosening is justified at the current juncture. Due to prudent fiscal policy in the past and low net public debt—even before excluding large nonfinancial assets—(Annex V) the government has ample fiscal space to address flood-related reconstruction needs. The fiscal stimulus plan—which raises the deficit to 3½ percent in 2018 before starting a process of gradual consolidation—is appropriate given the existing output gap and the expected deterioration in domestic demand. However, the success of this plan depends on executing a high level of investment spending, which has historically proven to be difficult in Peru. In this regard, staff welcomes recent government efforts to raise execution rates, including by effecting annual transfers to subnational governments earlier in the year (by the end of the first quarter).

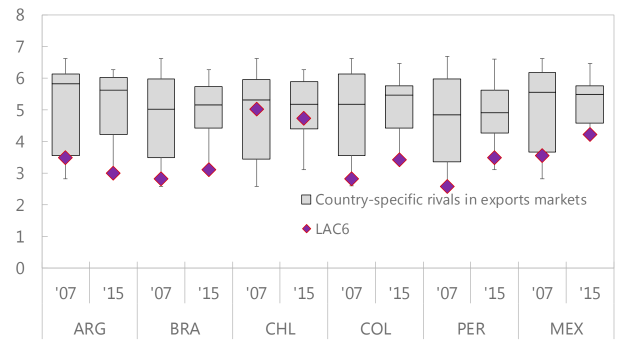
13. Over the medium term, the authorities are prioritizing improving fiscal transparency and consolidation. In line with the new fiscal rule, the authorities envisage a gradual consolidation towards the 1 percent deficit target by 2021. They plan to make use of assets such as those in the Fiscal Stabilization Fund to maintain public debt comfortably below the 30 percent of GDP ceiling. With support from Fund TA, the government is moving towards establishing a medium term budgetary framework (MTBF), which includes 3-year expenditure envelopes through a coordinated process at the Cabinet level.

14. While the move away from a structural balance rule is against previous IMF advice, it does have some advantages. Cross-country experience with structural deficit rules has been mixed (Ardanaz, Corbacho, Gonzales, and Tolsa (2015)). Indeed, headline deficit targets are more transparent and the new rule maintains key checks and balances embedded in the previous rule to ensure that fiscal policy is conducted responsibly (e.g. the Fiscal Council). It is also still informed by structural balance trends and contains necessary escape clauses. The latter have been appropriately called upon currently to finance reconstruction needs. Staff did caution, however, that a combination of the predetermined (and likely binding) adjustment path embedded in the new fiscal framework, along with possible volatility on fiscal revenues, could add procyclicality to the fiscal accounts.

15. The authorities have indicated that tackling Peru's infrastructure gap will be a priority. Their estimates put the infrastructure spending gap for the period 2016–25 at about 25 percent of 2016 GDP, with the main needs in transport, energy, telecommunications, health, and water. To tackle this challenge, the new government has reformed the system of public investment, by creating the National System for the Multiannual Programming and Management of Investments (Invierte.pe). The new system is expected to cover the phases of the investment cycle in a more complete manner than its predecessor.

16. Staff agreed on the infrastructure needs, and recommended continued efforts to improve revenue collection. Regarding infrastructure gaps, staff noted that the quality of infrastructure compared unfavorably with that of trade competitors (chart) and the government's focus on this is welcome, including by reforming the system of public investment. Staff recommended keeping a focus on enhancing capacity to implement projects at the subnational level and raising the tax to GDP ratio. Given lower commodity revenues, the latter has fallen to around 14 percent of GDP, below the regional average. Potential measures which the authorities are actively working on include streamlining tax administration and reducing VAT exemptions and informality.

LAC6 and Trade Rivals Comparison
(Quality of infrastructure, 2007-2015, Index: 7 = best)



Sources: April 2016 IMF Regional Economic Outlook, Western Hemisphere.
Note: The box-and-whiskers plot shows the full range (whiskers) and interquartile range and median (box) for country specific trade rivals.

17. Staff welcomed the authorities plan to establish a medium-term budgeting framework but suggested improving the Public-Private-Partnership (PPP) framework and introducing a comprehensive approach to monitoring fiscal risks. Staff noted that an MTBF could improve consistency between the annual budget and macro-fiscal aggregates. This would enhance fiscal discipline, costing of policies, and predictability of the budget process.[5] It could also build off the existing *Marco Macroeconómico Multianual*, which already provided a medium-term fiscal framework that set the macroeconomic scenario, revenue projections and main aggregates of expenditure to reach the fiscal targets. Regarding PPPs, while Peru's framework is considered relatively good by international standards, efforts to enhance capacity at Proinversión (the investment promotion agency in charge of PPPs) are welcome. There is scope, however, to improve certain facets, for example the procurement phase given a high level of contract renegotiations and cost overruns (see Annex VI). In line with previous FAD TA, staff recommended publishing an annual comprehensive fiscal risks statement, covering contingent liabilities and risks associated with investment plans.[6] This would be especially important given the objective of ramping up infrastructure spending.

[5] While there is no a one-size-fits-all model for MTBFs, good examples include Australia, Canada, Sweden and the UK. See selected issues paper for further details.

[6] While the TA recommendations are quite specific regarding the ideal coverage and structure for Peru, the risk statements of Australia and New Zealand may also provide useful guidance.

B. Striking the Right Monetary Policy Balance

18. The next monetary policy steps need to be considered carefully and communication will be key. With the output gap widening, temporary weather-related price pressures expected to abate quickly, and core inflation remaining within the target range, staff supported the BCRP's recent reduction of the policy rate. Looking ahead, fiscal policy has the advantage of facilitating both a demand and supply response (e.g. reconstruction of housing and infrastructure). Given the availability of fiscal space, this suggested fiscal policy should be the first line of defense if flood damage turns out to be higher than expected. Monetary policy could provide a useful complement if demand conditions deteriorated further, but the BCRP would need to continue to remain data dependent and monitor inflation expectations closely for any signs of a persistent drift above the target range. Clear communication regarding the temporary nature of existing price shocks and the inflation outlook would be essential to continue anchoring inflation expectations.

Peru. Inflation Expectations 1/

	2017	2018
Private sector		
Financial system	2.9	2.7
Economic analysts	3.0	2.9
Nonfinancial corp.	3.0	3.0
Concensus Forecast 2/	2.9	2.6
IMF Forecast	2.9	2.5

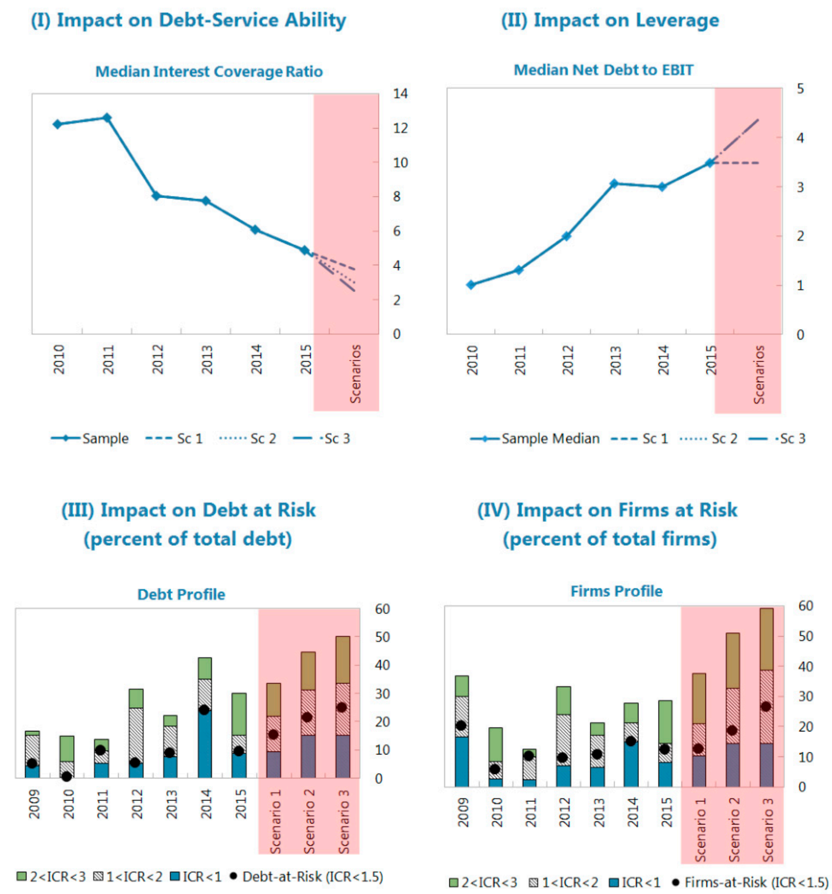
Sources: BCRP; Concensus Economics; and IMF staff calculations.
1/ End of period
2/ Corresponds to March 2017 survey.

19. Staff welcomed the increased exchange rate flexibility and the unwinding of the BCRP's FX intervention instruments. Staff argued that exchange rate flexibility is important, as demonstrated by the increased resilience in Latin America of domestic demand to recent current account adjustment under flexible exchange rate regimes. Regarding credit dollarization, staff pointed out that the decline over the last two years would help limit the adverse impact (via balance sheet effects) of exchange rate movements on domestic demand and financial sector soundness. Staff highlighted the smooth unwinding of the BCRP's FX intervention instruments (swaps), and its beneficial impact in terms of fostering a market-determined exchange rate. But staff also reiterated that future interventions should be limited to cases of disorderly market conditions. This would help further develop the market for hedging instruments.

C. Fostering Financial Stability and Development

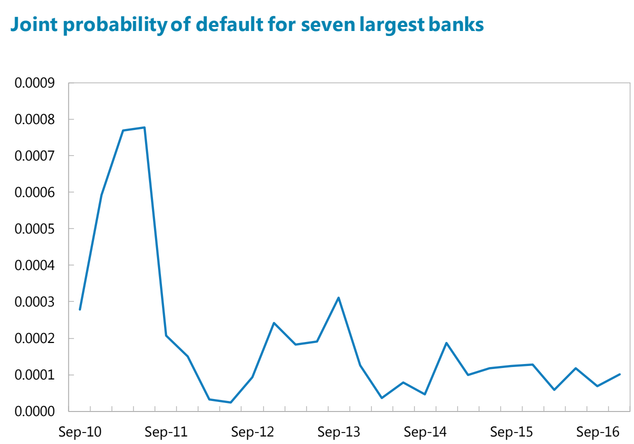
20. While corporate leverage has increased, sensitivity analysis suggests that vulnerabilities are relatively low (panel chart)**.**[7] Based on a limited sample of 54 firms, the share of debt-at-risk rises to 15 percent when a 30 percent currency depreciation is applied (Scenario 1). Assuming a 20 percent earnings fall in addition (Scenario 2), debt-at-risk rises by a further 6 percentage points. Adding an increase in interest rate expenses of 30 percent (Scenario 3) further increases debt-at-risk to a quarter of total debt. In all three scenarios, the median interest coverage ratio falls but remains above 2, and this is without applying any natural or financial hedges.

[7] The assumption of a 30 percent depreciation is double the depreciation in 2015; a 20 percent earnings fall is 10 times the standard deviation of nominal GDP growth in the last five years; and a 25 percent increase in interest expenses is the average of the rolling 12-month standard deviation of corporate loan interest rates in the last five years.



Source: IMF staff calculations.

21. Peru's financial system remains sound, with stability risks mainly arising from adverse economic developments and substantial exchange rate depreciation (Annex III)**.** Banks—90 percent of the system's assets (excluding pensions and insurance)—exhibit high profitability and capitalization ratios, and low ratios of nonperforming loans. The rest of the system—composed of smaller nonbank institutions—is also sound, but with more variability across institutions.[8] Nevertheless, the financial cooperatives segment is rapidly growing and would require greater oversight to contain any potential risks. While dollarization has declined, it remains a structural risk. The BCRP and SBS solvency stress tests indicate that the largest risks stem from decelerating economic growth and a large and sudden depreciation of the currency,



Source: Fund staff calculations

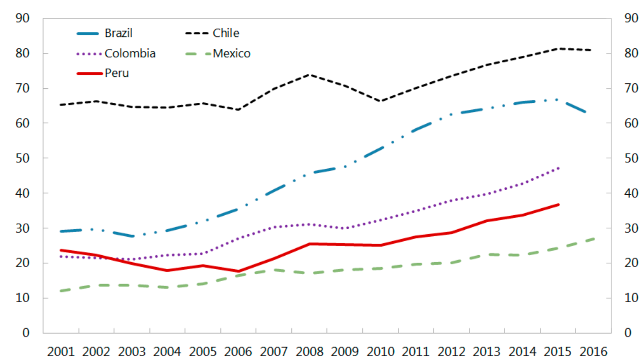
[8] BCRP's (November 2016) Financial Stability Report reports that some small nonbank institutions face difficulties due to their small scale of operations and weaker credit quality. Nonetheless, they do not represent a systemic risk.

although buffers appear sufficiently strong to withstand a stress scenario. Systemic risk also appears contained, with the joint probability of distress of the seven largest banks declining since its peak in 2010 and remaining at a low level (chart).[9] Staff noted that the incoming FSAP will constitute a valuable opportunity to examine stress tests and macrofinancial linkages in more detail.

22. Staff argued for a focus on further mitigating FX-related vulnerabilities to guard against stability risks, and discussed next steps regarding financial dedollarization. Staff noted that the targets on banks' share of FX loans, and resulting higher reserve requirements if these were not met, have been helpful in reducing credit dollarization. This has helped strengthen the resilience of specific institutions to exchange rate shocks and reduced systemic risks. Staff inquired about the recent strategy behind changes in FX reserve requirements, and recommended that future changes be clearly tied to the dedollarization process or stopping adverse macrofinancial feedback loops from developing. Regarding the prospects for rolling over the maturing dedollarization repos, staff stressed that these repos should remain a temporary strategy, and that the BCRP should continually monitor the associated impact on reserves and on the banking sector. Moreover, other strategies could be considered, such as increasing FX provisions for FX loans to unhedged borrowers. Regarding other potential risks, staff encouraged the development and publication of a national house price index and welcomed IMF TA in this regard.

23. While financial stability should remain a priority, perhaps the biggest challenges (and rewards) are associated with financial sector development. Tremendous progress has been made in branch penetration, which quadrupled over the last decade. But overall financial depth remains low, relative to fundamentals and the region (chart and Box 3). Financial inclusion is also low—the Global Findex (2014) shows that only about 30 percent of the Peruvian population aged over 15 has a bank account, below regional (51 percent) and income peers (58 percent). Notwithstanding recent reforms in the stock market, capital markets lack depth and liquidity.

Credit to Private Sector
(Percent of GDP)



Sources: IMF International Financial Statistics; WEO Database; and Fund staff calculations.

24. Staff recommended measures to aid financial deepening while preserving financial stability. Staff welcomed private initiatives to develop mobile payment platforms (*Billetera Móvil*). But staff also cautioned that the supervision perimeter would need to keep up with financial development, and argued that further efforts to reduce informality and increase literacy and financial education would be important complements. Staff also recommended to study possible reforms to deepen financial integration within the Pacific Alliance, which could help increase capital market liquidity and expand investment options for pension funds. The 2018 FSAP will likely cover

[9] Calculated as the probability that all seven banks are simultaneously in distress, where distress is defined as unexpected losses exceeding 7.5 percent of capital.

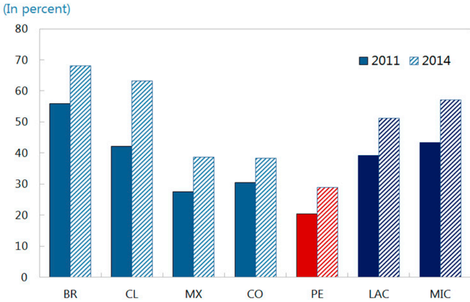
other key developmental issues, such as banking sector concentration, capital market development, payment systems competition, and pension reform.

25. Peru's developed macroprudential toolkit could be complemented by creating a Financial Stability Council. Following the Great Recession, the BCRP, MEF, and SBS have met on a regular informal basis. But the group has no formal mandate for financial stability, which could lead to collective action problems in the event of a crisis. The group could be converted into a formalized setup, while maintaining the mandates and operational autonomy for the individual agencies. While there is no one-size-fits-all and there are various models to achieve this (e.g. New Zealand, the U.K, and Germany), key features include a clear mandate that sets out well-defined objectives, strong accountability, and mechanisms to foster cooperation among agencies. Given that multiple agencies have roles in preserving financial stability, a coordinated council would help to strengthen the institutional framework, raise awareness about potential risks, facilitate consensus building, and identify overlaps and gaps in monitoring vulnerabilities. The upcoming FSAP would provide an opportunity to examine these issues in greater detail.

Box 3. Financial Deepening

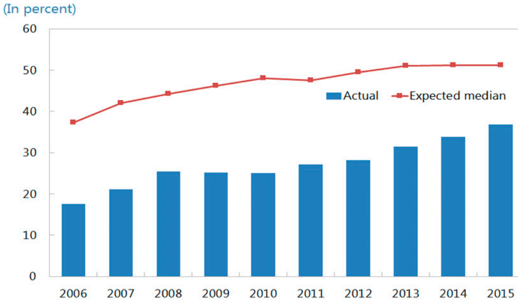
Peru's private credit to GDP at around 40 percent of GDP is one of the lowest in the region, and below the expected level for a country at Peru's income and population.[1] Studies also show that Peru has a negative gap in the depth and efficiency of financial institutions, as well as in the financial inclusion of households (for example, the level of account ownership of individuals remains low relative to comparator countries). [2]

Account at a financial institution, share of adults
(In percent)



Source: World Bank Global Findex (2014)

Private credit to GDP
(In percent)



Source: World Bank FinStats

Panel regression analysis using detailed institutional-level data finds that informality and illiteracy are barriers to financial deepening. Regions with higher levels of informality and illiteracy see less branch penetration of both banks and non-banks alike. However, once present in a region, banks and non-banks serve different segments of the population, with the non-banks playing an important role in providing financial services for the lower end of the market (see Selected Issues Paper for further details).

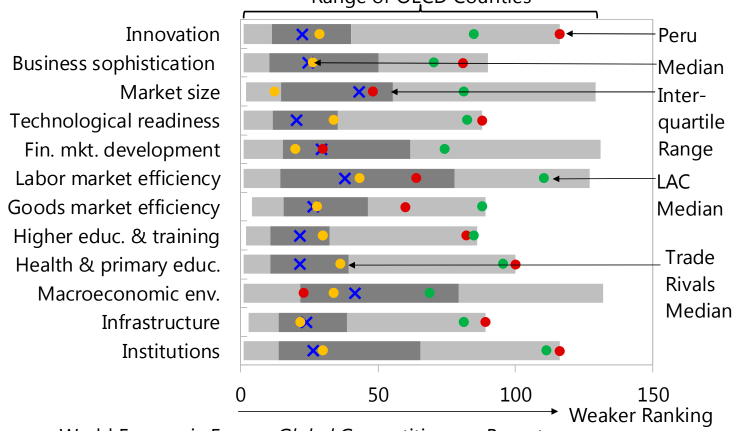
High levels of informality could be linked to a stronger preference for cash transactions, as well as the lack of proper documentation to fulfill know-your-customer requirements at formal financial institutions. The lack of financial literacy was cited as a major obstacle to financial inclusion in Peru, in a survey by the Center for Financial Inclusion (2013). The survey also cites the high cost of service delivery in remote and poor areas, which are also areas with higher levels of informality.

[1] Source: World Bank FinStats, which produces financial benchmarks based on a regression analysis controlling for structural factors.
[2] See for instance IMF WP/15/206.

D. Increasing Potential Growth Through Structural Reforms

26. A multifaceted approach is needed to increase potential growth. The 2016–17 Global Competitiveness Report (GCR) suggests that Peru is more competitive relative to other Latin American countries, and, indeed, it has achieved a rapid expansion in some nontraditional exports (e.g., fruits and vegetables) and a steady drop in product concentration (special feature, Annex II). Nonetheless, Peru still lags trade rivals and OECD countries in many areas (chart). Key areas for improvement in the journey to high-income status include education, infrastructure, innovation, and institutions. Regarding the latter and especially given the Odebrecht scandal (see Box 1), strengthening the anti-corruption legal framework and institutions, and adopting international best practices for the Office of the Comptroller General in verifying asset declarations seem particularly important. Effective implementation of AML/CFT measures in line with the international standards, for example enhanced due diligence for politically exposed persons, would also help to prevent the misuse of the financial system by corrupt officials.

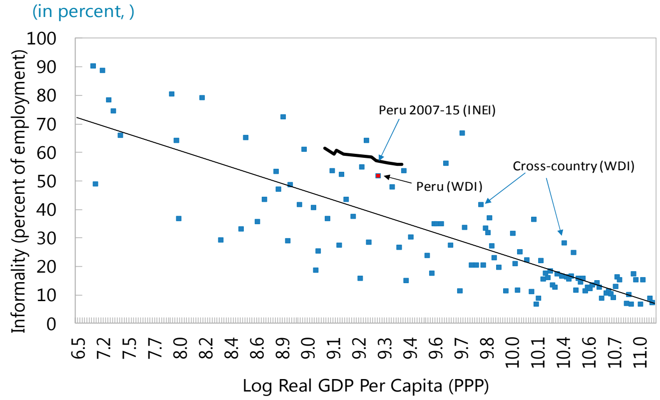
Competitiveness Indicators
(Ranking among 140 countries)



Source: World Economic Forum, *Global Competitiveness Report.*

27. The authorities are rightly focusing on high levels of informality as a key impediment. The GCR executive opinion survey pointed to labor market regulations as a serious problem.[10] And these are linked to high levels of informality in Peru relative to other countries of similar per capita income (chart) although other factors such as education levels, the tax regime, access to public services, and enforcement of laws have also played a role. Simulation exercises suggest that the growth gains from labor market reform can be significant (Box 4). The Social Protection Commission has an important mandate in this regard.

Informality and GDP per Capita
(in percent,)



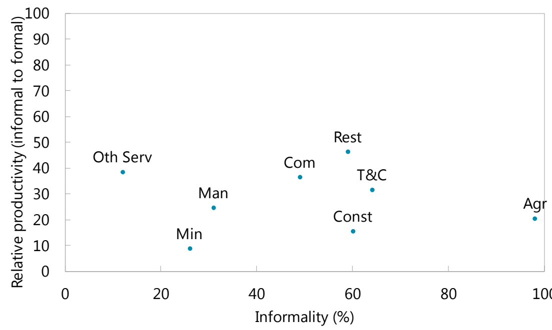
Sources: WDI, INEI, and IMF staff estimates.
Note: Cross-country WDI is for 2012 and reflects the share of self-employment in total employment. INEI data reflects the measure of informality by Peru's statistical agency.

[10] Dismissals for economic reasons are severely limited as they require authorization from the Ministry or Labor or the Courts. And dismissal outside of economic reasons must be through negotiated compensation.

Box 4. Growth Gains from Labor Market Reforms

The productivity differential between the informal and formal sectors in Peru is quite marked—with productivity in the former at less than 50 percent of the productivity in the latter in all sectors, and in some much less. Furthermore, Peru has a relatively inefficient labor allocation across sectors—measured by the negative covariance between each sector's employment share and labor productivity. This opens the possibility of large efficiency gains if labor were to move from the informal to the formal sector. While workers in the formal and informal sectors are not fully interchangeable (e.g., there are differences in human capital), the higher economies of scale and capital/labor ratios in the formal sector suggest, nonetheless, the reforms that achieve a reallocation of labor are likely to be growth enhancing.

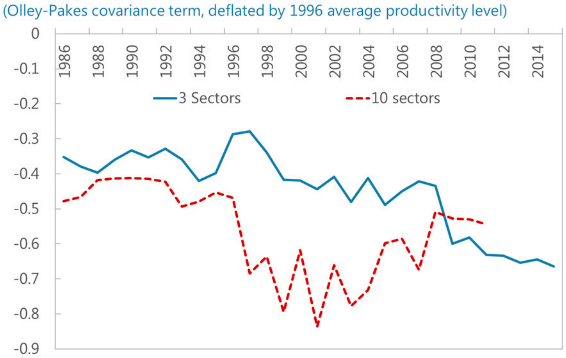
Peru. Informality and Productivity per Sector, 2014
(in percent)



Sources: INEI, and IMF staff estimates.

Achieving significant reductions in informality will require further structural reforms. Informality will likely gradually decline as GDP per capita in Peru continues increasing, but making a significant dent will likely necessitate labor market reforms—such as relaxing policies that push labor costs above productivity growth, or reducing labor taxes and firing costs. Regarding the first type of reform, using the analytical framework developed in Loayza (2016) suggests that a reform scenario in which labor productivity in the formal sector grows faster than labor costs could lead to informality in Peru declining by around 30 percentage points by 2030, relative to a nonreform scenario. Regarding the second type of reform, adapting the framework developed in Anand and Khera (2016) and Munkacsi and Saxegaard (2017) suggests that a combination of product and labor market reforms in Peru could lead to a significant positive impact on GDP in the long run. However, the presence of some short-run job destruction argues for combining these reforms with social transfers and active labor market policies (see Munkacsi, Roch, and Rodriguez (2017, forthcoming)).

Peru. Efficiency of Labor Allocation Over Time, 1986-2015
(Olley-Pakes covariance term, deflated by 1996 average productivity level)



Sources: Timmer, de Vries, and de Vries (2015 database), WBDI; and staff estimates

E. Authorities' Views

28. The authorities project stronger growth than staff. The MEF stressed the significant short term fiscal impulse and the efforts to increase the execution rate of public investment projects—including through accelerating budget transfers to the regions. Moreover, the authorities envisage that a catch-up in the implementation of large PPP projects delayed in 2017 will lead to a fast recovery of private investment in 2018–19. They argued that their efforts to reduce the infrastructure gap and informality will help the economy achieve a potential growth in the order of 4 to 5 percent in the medium term.

29. The authorities reiterated the advantages of the new fiscal rule. They stressed that the new rule was easier to communicate and would help maintain debt low. Furthermore, they noted the incentives that this rule would provide for further tax reform—e.g., expanding the tax base—which would help mitigate the impact of lower commodity prices on fiscal revenues.

30. The BCRP agreed that monetary policy should remain vigilant regarding the future path of inflation. The decision to cut the policy rate with inflation above the target range was made right after the reversal of the adverse supply shocks started, highlighting the transitory nature of inflation deviations from the target range. The BCRP emphasized that, given the negative output gap and the further expected reversal in food prices, a moderate expansionary monetary stance is consistent with a declining path of inflation towards its target range. Additionally, the BCRP indicated that further reductions of its policy rates would be data dependent.

31. The authorities saw merit in several of staff's recommendations, but indicated that further analysis regarding modalities may be needed.

- *Fiscal risks statement*. The authorities agreed that a more comprehensive mapping and assessment of risks may be useful given the efforts to ramp up investment spending. The MEF noted that the incoming Multiannual Macroeconomic Framework will contain a separate section on contingent liabilities, and will ponder in the coming months whether a broader risk exercise is feasible given competing priorities—e.g., MTB, 2018 budget preparation, and assessment of the recommendations of the social protection commission.

- *Financial stability committee*. The authorities noted that improved information sharing would be a key advantage of this institutional arrangement, but raised concerns regarding the potential loss of independence of participating agencies. The SBS indicated its preference for a coordinating committee, while the BCRP was more inclined towards a risk assessment committee as a mechanism for more effective information disclosing.

- *Dedollarization strategy*. The BCRP and SBS saw little need for new dedollarization measures given the already comprehensive framework in this area. Similarly, the BCRP was not concerned with the recent reduction in FX reserve requirements causing a reversal in recent dedollarization gains, noting that quantitative limits on FX credit growth remain in place, and that the reduction reflects a normalization from earlier peaks. The BCRP agreed with staff's exchange rate assessment but continued to see merit in leaning against the wind and smoothing effects of temporary volatility.

STAFF APPRAISAL

32. Peru is looking ahead to tackle the challenge of becoming a high-income nation, but the current juncture is a difficult one. With average growth of over 5¼ percent since 2000, Peru has significantly reduced unemployment and poverty. Inflation is in low single digits, fiscal buffers are ample, and dollarization has declined markedly. In the context of a commodity boom, sound macroeconomic management and structural reforms have played an essential role in this improvement. With lower commodity prices now, consolidating these gains and further reforms will be critical in helping Peru reach its target of high-income status. But the current juncture is a difficult one given domestic headwinds—the Odebrecht scandal and the worst flooding and landslides in over 50 years—and challenging external conditions.

33. The domestic headwinds presage weaker growth in 2017 before a bounceback given policy stimulus. Growth is expected to decline to slightly below 2¾ percent in 2017 given the impact of the Odebrecht scandal and the floods, notwithstanding the stimulus plan. A bounceback should take place in 2018–19, reflecting reconstruction spending, public investment projects, and a recovery in private sector investment before growth converges to potential of 3¾ percent in the medium term. Especially in 2017, risks to the outlook are tilted to the downside, with potential for delays in implementing investment projects and reconstruction spending. Headline inflation is expected to gradually decline and return to the BCRP's target range as weather-related food price increases dissipate.

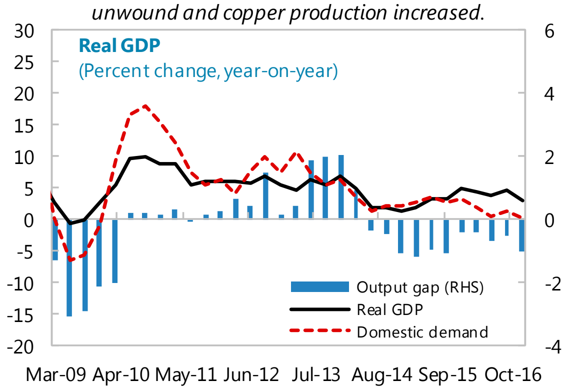
34. The short term macroeconomic policy mix remains appropriate. Countercyclical fiscal policy is rightly being used as the first line of defense to support reconstruction and economic activity, while the government is financing the added fiscal impulse with its fiscal buffers, helping it maintain public debt below the 30 percent of GDP ceiling. The recent monetary easing is supported by evidence of a reversal of the adverse supply shocks and a widening output gap. Looking ahead, monetary policy should remain data dependent. The real exchange rate remains broadly in line with fundamentals. While the BCRP has intervened in the FX market over the last year, the bulk of the intervention was to unwind previous operations and/or to mitigate excessive short term volatility, given Peru remains still partially dollarized. Future interventions should be limited to cases of disorderly market conditions.

35. The medium-term economic strategy targets the right areas, but could benefit from a more ambitious structural reform agenda and a further focus on risks. Gradual fiscal consolidation, domestic revenue mobilization, closing the infrastructure gap, reducing economic informality, and implementing anti-corruption and AML/CFT measures should help Peru maintain its sound fiscal buffers, sustain robust growth, and support further poverty reduction. Nonetheless, reforms to increase labor market flexibility, enhance financial deepening and inclusion, and further actions to strengthen institutions will likely be needed to significantly increase potential growth, especially in the context of lower commodity prices. Introducing a comprehensive fiscal risks statement, continuing to focus on FX risks, creating a financial stability council, extending the financial supervisory perimeter, and developing/publishing a national house price index would help the comprehensive monitoring of future vulnerabilities, should they arise.

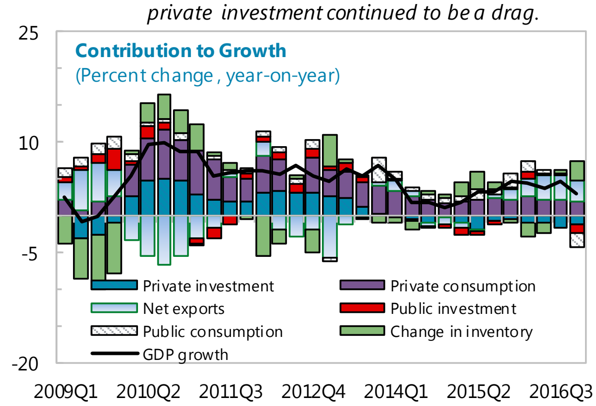
36. Staff would like to express their appreciation to the new administration for a constructive engagement. It is recommended that the next Article IV consultation take place on the 12-month cycle.

Figure 1. Real Sector Developments

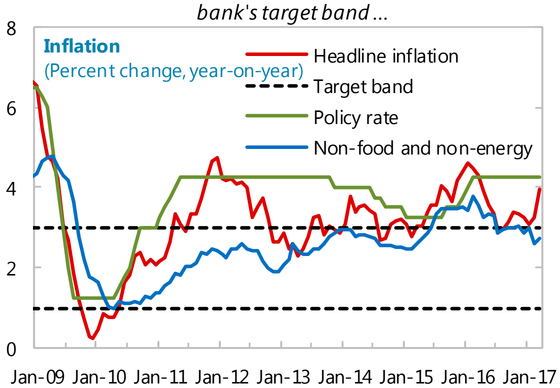
Economic growth strengthened in 2016, as supply shocks unwound and copper production increased.



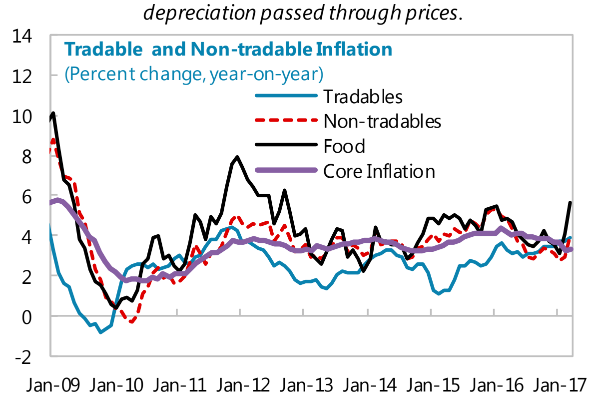
Exports and consumption helped sustain growth, while private investment continued to be a drag.



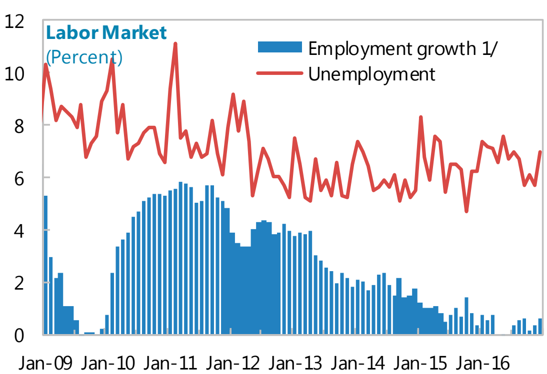
Inflation has remained above the upper limit of the central bank's target band…



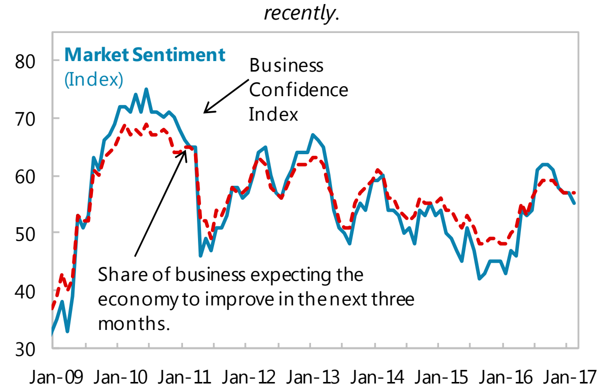
…as food and energy price inflation picked up, and exchange rate depreciation passed through prices.



Employment growth has remained moderate…

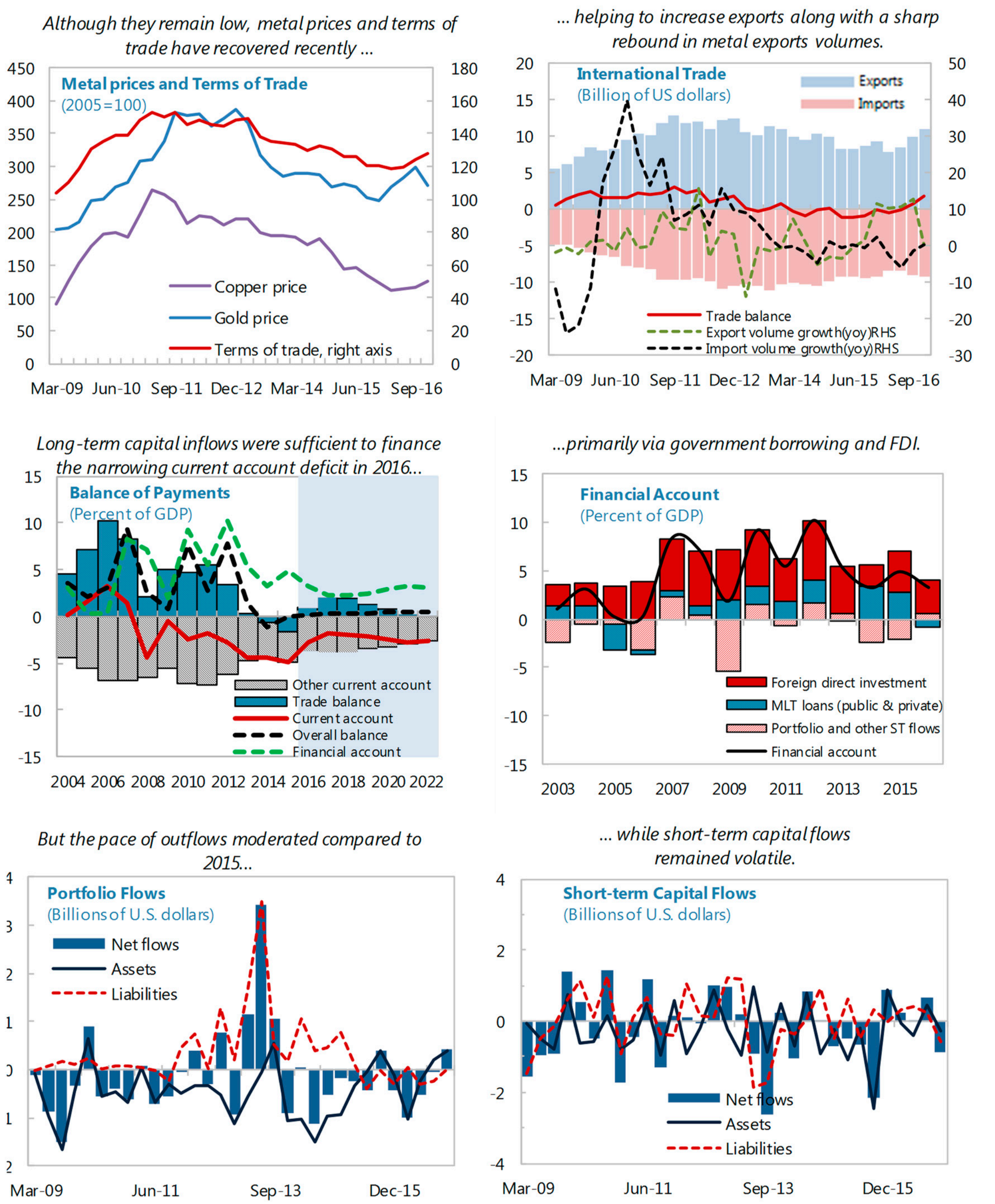


…while market sentiment improved but has weakened recently.



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

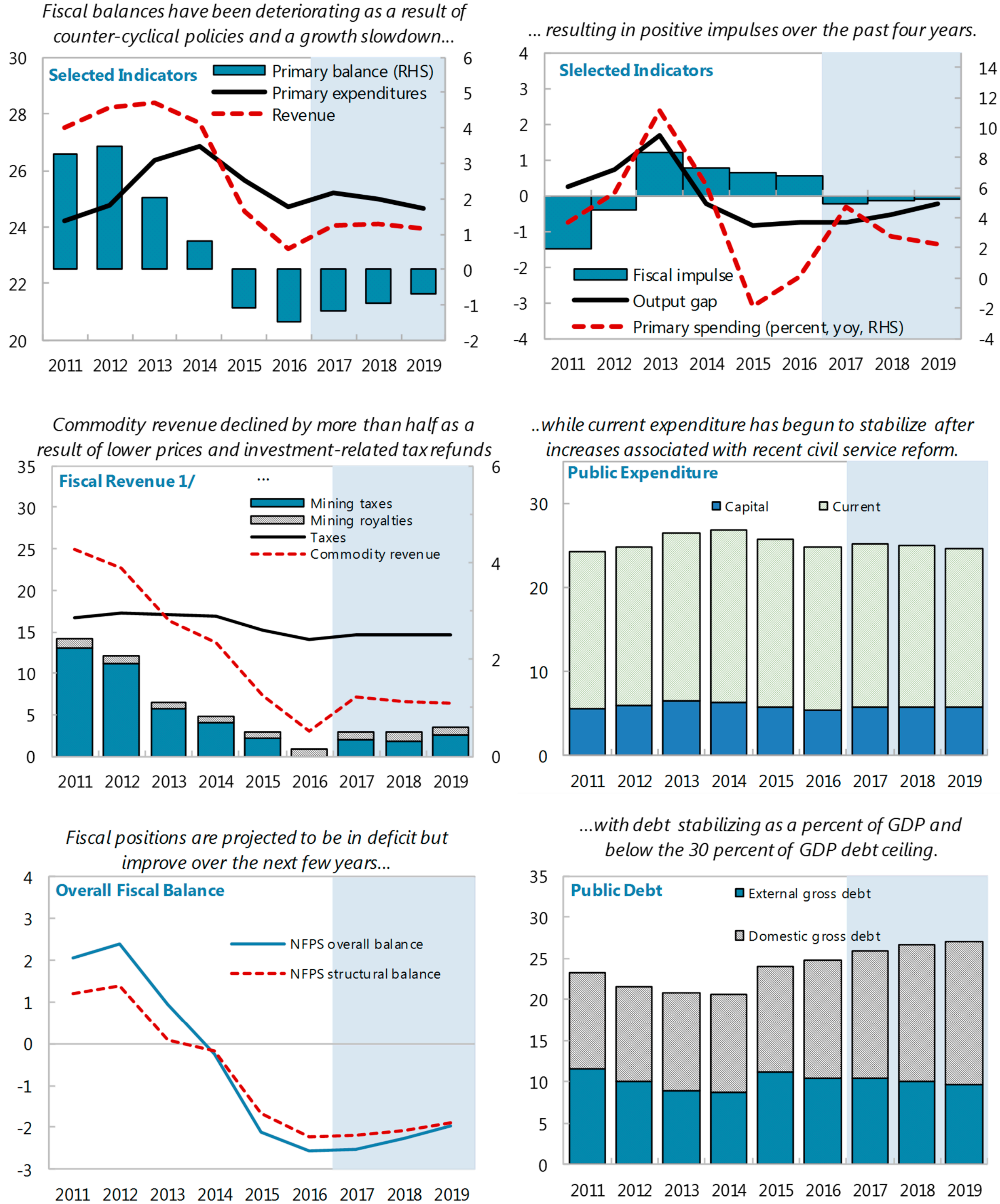
Figure 2. External Sector Developments



Sources: National authorities; and Fund staff estimates.

Figure 3. Fiscal Sector Developments

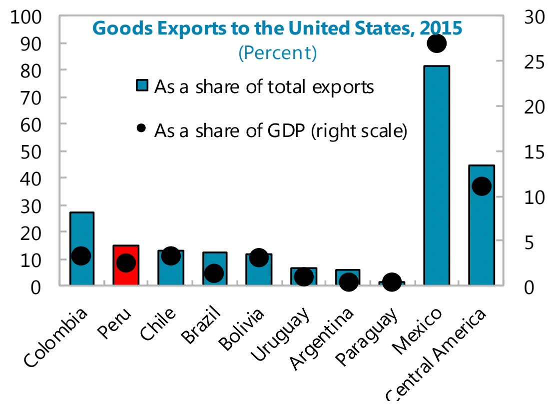
(Percent of GDP)



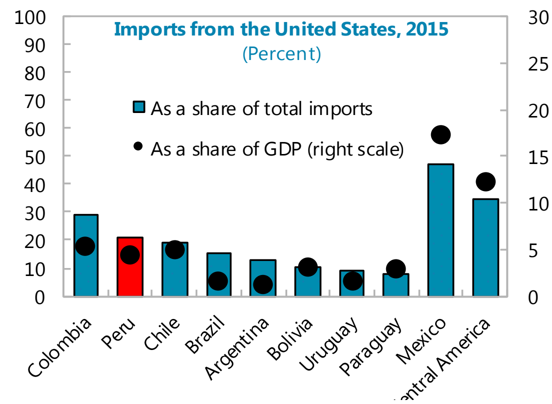
Sources: National authorities; and Fund staff estimates.
1/ Net of restitutions.

Figure 4. U.S. Exposures and Spillovers

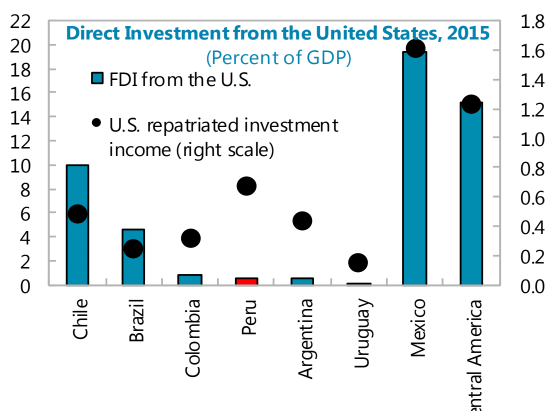
Export exposures to the US are moderate, with goods exports at around 2.5 percent of GDP...



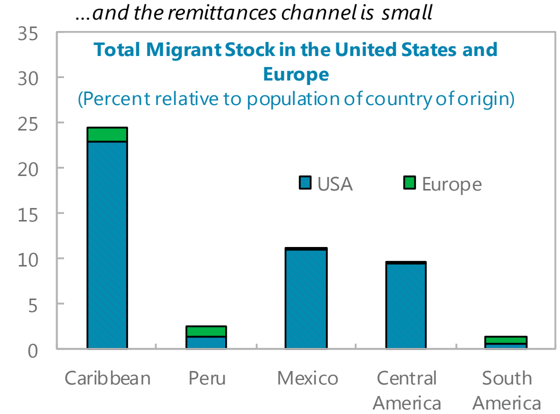
...and imports slightly over 4 percent of GDP.



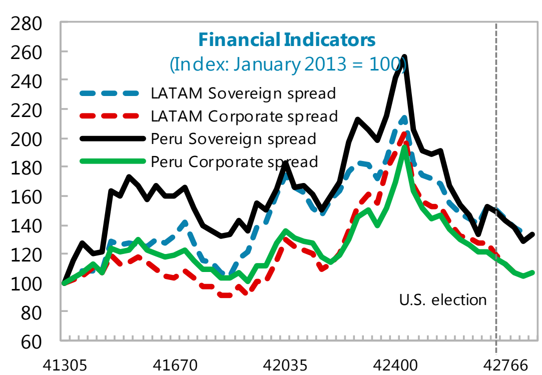
FDI exposures are limited...



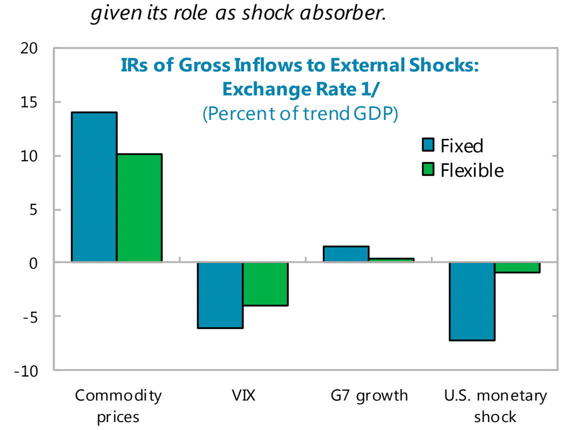
...and the remittances channel is small



With higher commodity prices, sovereign spreads have actually declined after the U.S election.



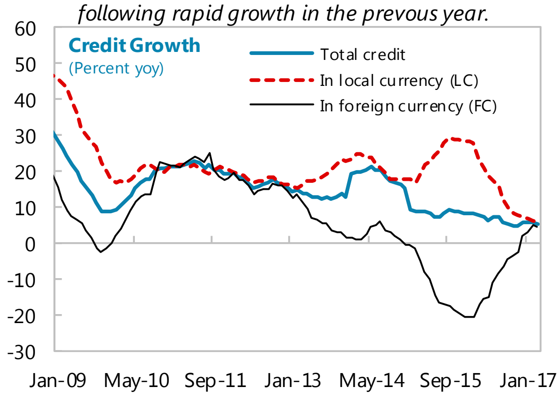
Nonetheless, it will be important to maintain a flexible exchange rate regime going forward, given its role as shock absorber.



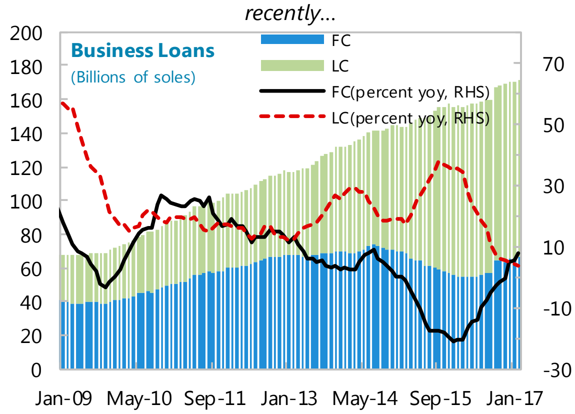
Source: IMF staff calculations.
Central American countries include: Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, Panama, Mexico
1/ Impulse responses.

Figure 5. Financial Sector Developments

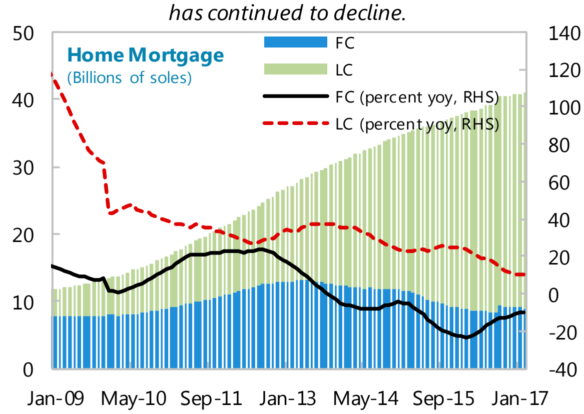
Private sector credit growth slowed down following rapid growth in the prevous year.



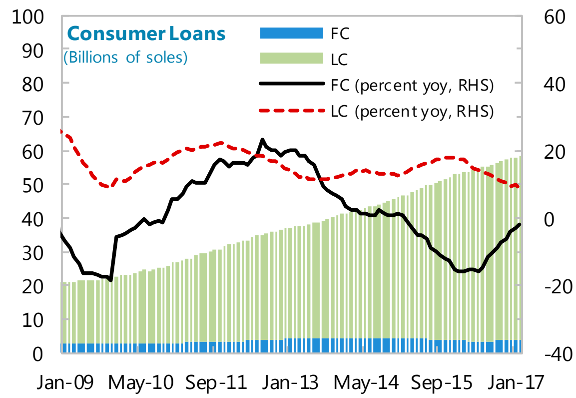
The share of corporate loans in dollars has stabilized recently...



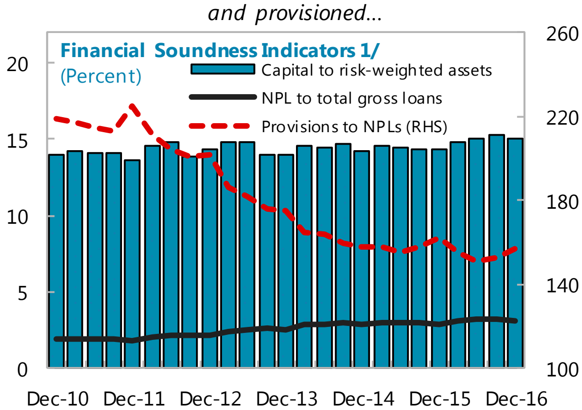
... but the share of dollar-denominated mortgage loans has continued to decline.



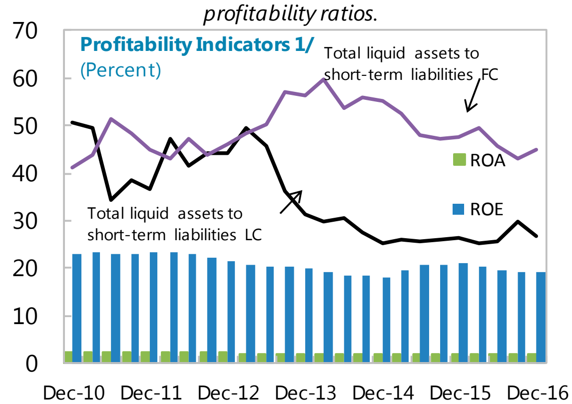
Dollarization of consumer loans remains low.



Deposit-taking institutions are well-capitalized and provisioned...



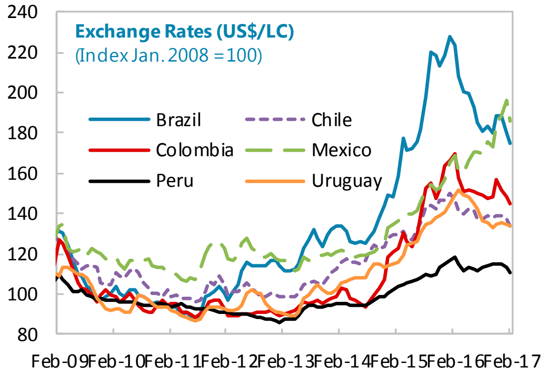
...with adequate liquidity and comfortable profitability ratios.



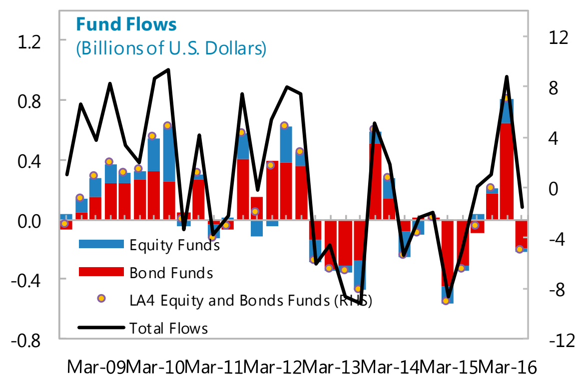
Sources: National authorities; and Fund staff estimates.
1/ Data corresponds to depository corporations. Last data available is for June-2016.

Figure 6. FX and Capital Market Developments

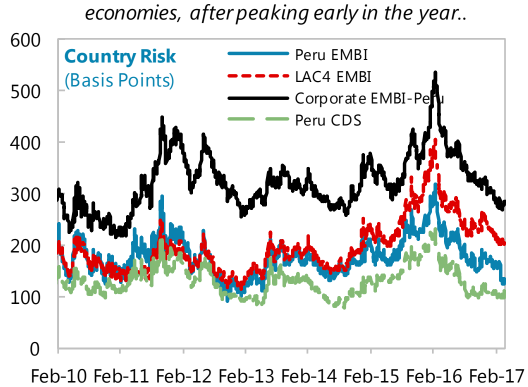
The sol stabilized in 2016...



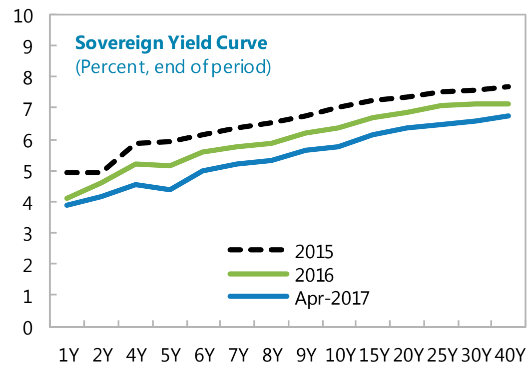
...while bond and equity flows recovered.



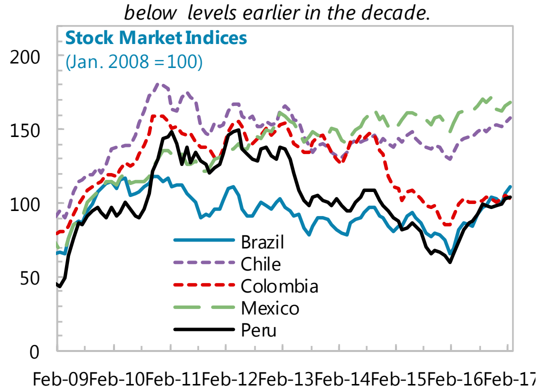
Spreads declined, in line with other regional economies, after peaking early in the year..



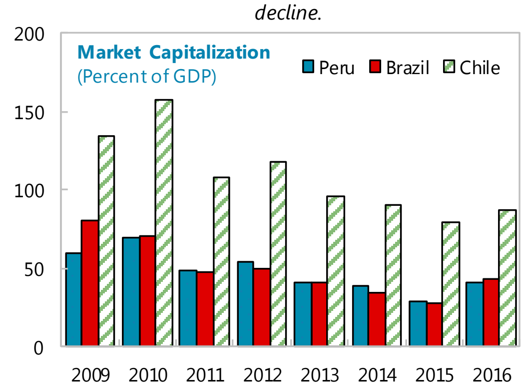
...and the sovereign bond yield curve has shifted downward.



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

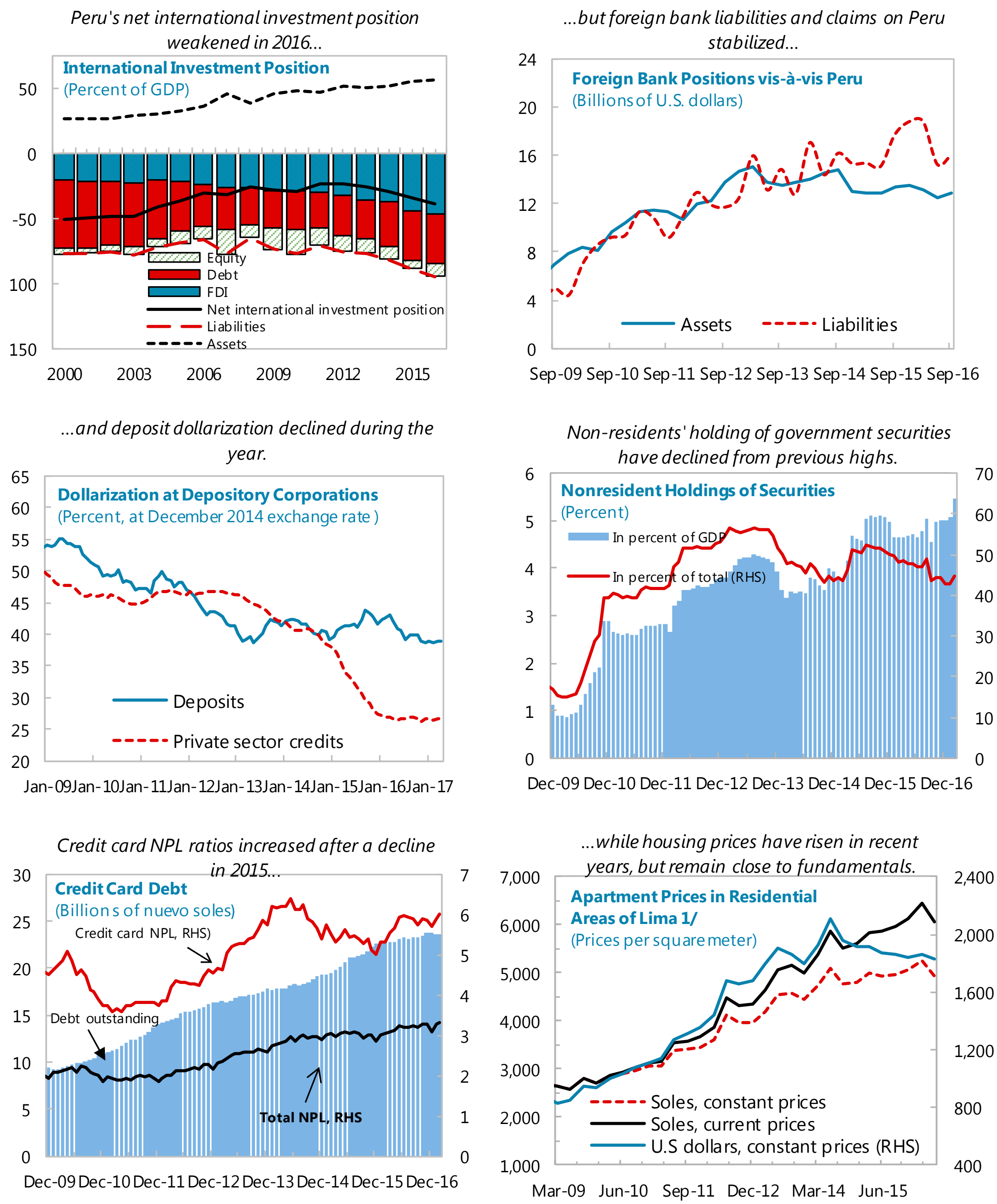


Market capitalization recovered after three years of decline.



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

Figure 7. Balance Sheet Indicators

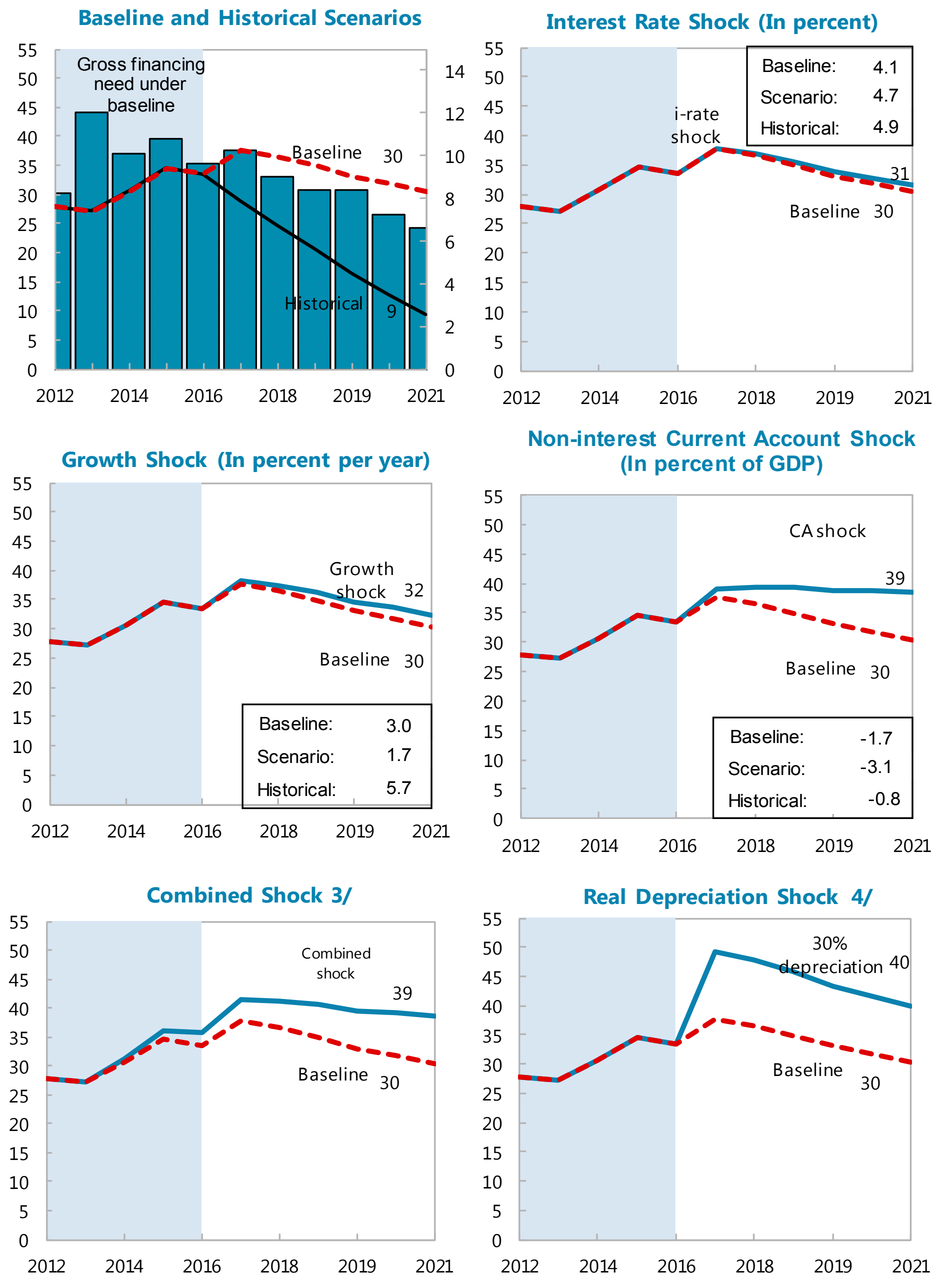


Sources: National authorities; Association of Banks; Bank for International Settlements; and Fund staff estimates.

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

Figure 8. 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

	2012	2013	2014	2015	Prel. 2016	Proj. 2017	2018	2019	2020	2021	2022
Social Indicators											
Life expectancy at birth (years) 1/	74.0	74.2	74.4	74.6	...	...	...	...	...	...	...
Infant mortality (per thousand live births)	17.0	16.0	17.0	17.6	...	...	...	...	...	...	...
Adult literacy rate 1/	93.8	93.8	93.7	94.0	...	...	...	...	...	...	...
Poverty rate (total)	25.8	23.9	22.7	21.8	20.7	...	...	...	...	...	...
Unemployment rate	6.8	5.9	5.9	6.5	6.7	...	...	...	...	...	...
	(Annual percentage change; unless otherwise indicated)										
Production and prices											
Real GDP	6.0	5.8	2.4	3.3	3.9	2.7	3.8	4.0	3.9	3.8	3.8
Real domestic demand	7.3	7.3	2.2	3.1	0.9	2.4	3.7	4.7	4.5	4.2	3.9
Output gap (percent of potential GDP)	0.7	1.7	-0.2	-0.8	-0.8	-1.1	-0.8	-0.3	0.0	0.0	0.0
Consumer prices (end of period)	2.6	2.9	3.2	4.4	3.2	2.9	2.5	2.5	2.4	2.2	2.0
Consumer prices (period average)	3.7	2.8	3.2	3.5	3.6	3.1	2.6	2.5	2.4	2.3	2.3
External sector											
Exports	2.2	-9.6	-7.8	-12.9	7.6	12.9	4.5	2.7	3.2	3.2	3.1
Imports	10.4	3.3	-3.1	-9.0	-5.9	6.3	5.0	6.5	6.6	6.2	4.4
Terms of trade (deterioration -)	-2.3	-5.2	-5.4	-6.4	-0.7	5.0	-0.8	-1.1	-1.0	-1.2	0.7
Real effective exchange rate (depreciation -)	8.1	-0.2	-1.6	0.8	-2.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Money and credit 2/ 3/											
Broad money	12.5	15.3	9.5	11.6	4.3	5.2	7.8	7.8	7.6	7.6	7.7
Net credit to the private sector	13.3	18.3	13.2	14.0	5.0	5.2	6.5	6.6	6.5	6.6	6.7
	(In percent of GDP; unless otherwise indicated)										
Public sector											
NFPS revenue	28.3	28.4	28.0	25.1	23.2	23.1	23.2	23.4	23.6	23.8	23.8
NFPS primary expenditure	24.8	26.4	27.1	26.0	24.7	24.8	25.3	24.9	24.1	23.5	23.3
NFPS primary balance	3.5	2.0	0.9	-1.0	-1.5	-1.7	-2.1	-1.5	-0.5	0.3	0.4
NFPS overall balance	2.4	0.9	-0.2	-2.0	-2.6	-3.0	-3.5	-2.9	-1.9	-1.0	-1.0
NFPS structural primary balance 5/	2.0	0.8	0.1	-0.5	-1.2	-1.3	-1.9	-1.4	-0.5	0.3	0.4
External sector											
External current account balance	-2.7	-4.4	-4.4	-4.8	-2.7	-2.1	-2.1	-2.4	-2.7	-2.8	-2.8
Gross reserves											
In millions of U.S. dollars	64,049	65,710	62,353	61,530	61,731	61,731	62,931	62,931	63,431	63,631	63,831
Percent of short-term external debt 4/	496	536	534	523	450	410	604	586	667	701	712
Percent of foreign currency deposits at banks	300	274	258	224	230	233	236	235	237	239	243
Debt											
Total external debt	27.8	27.2	30.6	34.6	33.5	30.0	28.8	26.4	25.1	23.8	22.4
Gross non-financial public sector debt (incl. repayment certificates)	21.6	20.8	20.7	24.0	24.4	25.2	26.4	27.0	26.8	26.3	25.7
External	10.0	9.0	8.7	11.1	10.3	9.9	10.6	9.9	10.0	9.8	9.5
Domestic	11.6	11.8	12.0	12.9	14.1	15.3	15.7	17.1	16.8	16.4	16.2
Savings and investment											
Gross domestic investment	24.7	26.5	24.9	24.6	22.8	22.2	22.2	23.0	23.8	24.4	24.4
Public sector (incl. repayment certificates)	5.5	5.9	5.5	5.0	4.8	5.2	5.6	5.6	5.3	5.1	5.1
Private sector (incl. inventories)	19.2	20.6	19.4	19.6	18.1	17.0	16.5	17.4	18.5	19.3	19.3
National savings	22.0	22.0	20.5	19.8	20.1	20.1	20.1	20.6	21.0	21.6	21.5
Public sector	8.2	7.2	6.0	3.8	2.7	2.7	2.7	3.3	4.0	4.6	4.3
Private sector	13.7	14.8	14.4	16.1	17.4	17.3	17.4	17.2	17.1	17.0	17.2
Memorandum items											
Nominal GDP (S/. billions)	498.5	534.7	576.3	612.8	658.7	703.9	747.8	796.0	845.9	897.6	952.3
GDP per capita (in US$)	6,396	6,629	6,586	6,168	6,199	6,568	6,872	7,218	7,566	7,920	8,305

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

					Prel.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	(In millions of soles; unless otherwise indicated)										
Revenues	**140,842**	**151,932**	**161,274**	**153,579**	**152,842**	**162,323**	**173,627**	**185,968**	**199,399**	**214,064**	**226,198**
Taxes	86,097	91,617	97,646	92,788	92,221	96,605	103,895	112,016	121,072	131,198	138,548
Other	54,745	60,315	63,628	60,791	60,621	65,719	69,732	73,953	78,326	82,867	87,651
Primary expenditures 1/	**123,413**	**140,984**	**156,179**	**159,623**	**162,755**	**174,461**	**189,471**	**197,970**	**203,698**	**210,925**	**222,311**
Current	93,507	106,446	118,655	123,024	127,177	133,561	142,185	147,451	152,949	159,675	168,561
Capital	29,906	34,538	37,525	36,599	35,578	40,899	47,285	50,519	50,749	51,250	53,750
Primary balance	**17,429**	**10,948**	**5,095**	**-6,044**	**-9,913**	**-12,137**	**-15,843**	**-12,002**	**-4,300**	**3,139**	**3,887**
Interest	5,577	6,005	6,206	6,346	7,137	8,635	10,410	11,094	11,653	12,393	13,072
Overall balance	**11,852**	**4,944**	**-1,111**	**-12,390**	**-17,050**	**-20,772**	**-26,253**	**-23,096**	**-15,953**	**-9,254**	**-9,185**
External financing	-1,385	-4,386	-843	10,064	1,033	996	9,968	-838	5,189	3,727	2,575
Domestic financing	-10,468	-558	1,954	2,327	16,017	19,776	16,285	23,934	10,764	5,527	6,610
Public Gross Debt 2/	**107,704**	**111,009**	**119,252**	**147,291**	**160,861**	**177,361**	**197,070**	**215,299**	**226,447**	**235,863**	**245,048**
External	49,719	48,084	50,373	68,006	67,976	69,425	79,584	78,953	84,424	88,313	90,888
Domestic	53,925	58,961	65,013	74,825	88,841	104,191	114,042	133,202	139,179	145,006	151,916
Repayment Certificates	3,983	3,964	3,866	4,460	4,044	3,744	3,444	3,144	2,844	2,544	2,244
Public Assets	**76,999**	**85,404**	**90,618**	**99,497**	**100,795**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
	(In percent of GDP; unless otherwise indicated)										
Revenues	**28.3**	**28.4**	**28.0**	**25.1**	**23.2**	**23.1**	**23.2**	**23.4**	**23.6**	**23.8**	**23.8**
Taxes	17.3	17.1	16.9	15.1	14.0	13.7	13.9	14.1	14.3	14.6	14.5
Other	11.0	11.3	11.0	9.9	9.2	9.3	9.3	9.3	9.3	9.2	9.2
Primary expenditures 1/	**24.8**	**26.4**	**27.1**	**26.0**	**24.7**	**24.8**	**25.3**	**24.9**	**24.1**	**23.5**	**23.3**
Current	18.8	19.9	20.6	20.1	19.3	19.0	19.0	18.5	18.1	17.8	17.7
Capital	6.0	6.5	6.5	6.0	5.4	5.8	6.3	6.3	6.0	5.7	5.6
Primary balance	**3.5**	**2.0**	**0.9**	**-1.0**	**-1.5**	**-1.7**	**-2.1**	**-1.5**	**-0.5**	**0.3**	**0.4**
Interest	1.1	1.1	1.1	1.0	1.1	1.2	1.4	1.4	1.4	1.4	1.4
Overall balance	**2.4**	**0.9**	**-0.2**	**-2.0**	**-2.6**	**-3.0**	**-3.5**	**-2.9**	**-1.9**	**-1.0**	**-1.0**
External financing	-0.3	-0.8	-0.1	1.6	0.2	0.1	1.3	-0.1	0.6	0.4	0.3
Domestic financing	-2.1	-0.1	0.3	0.4	2.4	2.8	2.2	3.0	1.3	0.6	0.7
Public Gross Debt 2/	**21.6**	**20.8**	**20.7**	**24.0**	**24.4**	**25.2**	**26.4**	**27.0**	**26.8**	**26.3**	**25.7**
External	10.0	9.0	8.7	11.1	10.3	9.9	10.6	9.9	10.0	9.8	9.5
Domestic	10.8	11.0	11.3	12.2	13.5	14.8	15.3	16.7	16.5	16.2	16.0
Repayment Certificates	0.8	0.7	0.7	0.7	0.6	0.5	0.5	0.4	0.3	0.3	0.2
Public Assets	**15.4**	**16.0**	**15.7**	**16.2**	**15.3**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
Of which: Treasury Deposits and Fiscal Stabilization Fund	8.3	8.3	8.2	9.4	9.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Public Net Debt	**6.2**	**4.8**	**5.0**	**7.8**	**9.1**	**…**	**…**	**…**	**…**	**…**	
Memorandum items											
Commodity related revenues 3/	3.9	2.8	2.4	1.3	0.4	1.1	1.0	1.0	1.0	0.9	0.9
Output gap (percent of potential GDP)	0.7	1.7	-0.2	-0.8	-0.8	-1.1	-0.8	-0.3	0.0	0.0	0.0
SPNF non-commodity structural balance	-1.8	-2.5	-2.9	-2.8	-2.8	-3.7	-4.3	-3.8	-2.8	-2.0	-1.0
SPNF non-commodity primary structural balance	-0.6	-1.3	-1.8	-1.7	-1.7	-2.5	-2.9	-2.4	-1.4	-0.6	0.4
NFPS structural balance 4/	0.9	-0.3	-1.0	-1.5	-2.2	-2.6	-3.3	-2.8	-1.9	-1.1	-1.0
NFPS structural primary balance 4/	2.0	0.8	0.1	-0.5	-1.2	-1.3	-1.9	-1.4	-0.5	0.3	0.4
Fiscal impulse (+ = expansionary)	-0.4	1.2	0.7	0.6	0.7	0.2	0.5	-0.4	-0.9	-0.8	-0.1

Sources: National Authorities; and Fund staff estimates.

1/ Official data excludes expense accrued during the period by Repayment Certificates (CRPAOs) and Petroleum Price Stabilization Fund (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 Petroleum 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

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

(In percent of GDP; unless otherwise indicated)

					Prel.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	**22.8**	**22.8**	**22.3**	**20.0**	**18.7**	**18.6**	**18.7**	**18.8**	**19.1**	**19.3**	**19.2**
Taxes	17.3	17.1	16.9	15.1	14.0	13.7	13.9	14.1	14.3	14.6	14.5
Social Contributions	2.1	2.1	2.2	2.0	2.2	2.3	2.3	2.3	2.3	2.2	2.2
Grants	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other revenue	3.3	3.4	3.1	2.8	2.4	2.4	2.4	2.4	2.4	2.4	2.4
Expense 2/	**14.9**	**15.8**	**16.6**	**16.8**	**16.3**	**16.3**	**16.5**	**16.0**	**15.6**	**15.4**	**15.3**
Compensation of employees	5.0	5.4	6.0	6.2	6.0	6.0	6.2	6.0	5.8	5.7	5.6
Use of goods and services	5.7	6.4	6.0	6.5	6.1	6.1	6.1	6.0	5.8	5.7	5.8
Consumption of fixed capital 2/	5.8	6.3	6.0	5.4	4.7	5.0	5.6	5.6	5.3	5.0	4.9
Interest	1.1	1.1	1.0	1.0	1.0	1.2	1.3	1.3	1.3	1.3	1.3
Social benefits	2.0	2.0	1.9	2.0	2.1	2.1	2.1	2.0	2.0	1.9	1.9
Other expenses 3/	1.1	0.8	1.6	1.2	1.0	0.9	0.8	0.7	0.7	0.8	0.9
Net acquisition of nonfinancial assets	**5.8**	**6.3**	**6.0**	**5.4**	**4.7**	**5.0**	**5.6**	**5.6**	**5.3**	**5.0**	**4.9**
Acquistions of nonfinancial assets	5.8	6.3	6.0	5.4	4.7	5.0	5.6	5.6	5.3	5.0	4.9
Gross Operating Balance	7.9	7.0	5.7	3.2	2.3	2.2	2.2	2.8	3.5	3.9	3.9
Net lending (+) borrowing (-) 4/	**2.1**	**0.7**	**-0.3**	**-2.2**	**-2.3**	**-2.8**	**-3.4**	**-2.8**	**-1.8**	**-1.0**	**-1.0**
Net acquistion of financial assets 5/	**2.1**	**0.0**	**0.0**	**0.0**	**0.0**	**-0.7**	**-0.9**	**-0.6**	**-1.2**	**-0.6**	**-0.7**
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/	2.1	0.0	0.0	0.0	0.0	-0.7	-0.9	-0.6	-1.2	-0.6	-0.7
By residency											
Domestic	2.1	0.0	0.0	0.0	0.0	-0.7	-0.9	-0.6	-1.2	-0.6	-0.7
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/	**0.0**	**-0.7**	**0.3**	**2.2**	**2.3**	**2.1**	**2.5**	**2.1**	**0.6**	**0.4**	**0.3**
By instrument											
Debt securities	0.1	0.1	0.4	2.3	2.2	2.0	1.1	2.2	0.0	0.0	0.0
Loans	-0.1	-0.8	-0.1	-0.1	0.2	0.1	1.3	-0.1	0.6	0.4	0.3
By residency											
Domestic	0.1	0.1	0.4	2.3	2.2	2.0	1.1	2.2	0.0	0.0	0.0
External	-0.1	-0.8	-0.1	-0.1	0.2	0.1	1.3	-0.1	0.6	0.4	0.3
Memorandum items											
Central Government Net lending (+) borrowing (-)	0.8	-0.1	-1.1	-2.8	-2.7	-3.4	-4.1	-3.7	-2.9	-2.2	-2.0
Regional Governments Net lending (+) borrowing (-)	0.6	0.4	0.6	0.7	0.1	0.1	0.2	0.3	0.4	0.5	0.5
Local Governments Net lending (+) borrowing (-)	-0.2	-0.2	0.2	0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.1
General Government Primary Balance	3.2	1.9	0.8	-1.2	-1.3	-1.6	-2.1	-1.5	-0.6	0.2	0.3
General Government Overall Balance	2.1	0.7	-0.3	-2.2	-2.3	-2.8	-3.4	-2.8	-1.8	-1.0	-1.0
Gen. Gov. primary spending (real percentage change)	7.6	11.1	7.3	1.5	-2.5	4.9	6.6	1.8	0.0	0.9	2.9
Of which: Current spending	4.8	10.5	10.6	4.6	0.3	2.8	4.1	0.7	0.9	2.1	3.2
Capital spending	14.8	12.4	-0.4	-6.6	-10.6	11.6	14.2	4.7	-2.5	-2.3	1.9
General Government non-financial expenditures	19.6	20.9	21.5	21.2	20.0	20.2	20.8	20.4	19.6	19.1	18.9

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)

					Prel.	Projections 1/					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Stock positions:											
Net worth	....	....	....	....	....	....	....	....	....	....	....
Nonfinancial assets	....	....	....	....	....	....	....	....	....	....	....
Net financial worth	**-4.6**	**-3.6**	**-3.6**	**-5.6**	**-7.5**	**-9.9**	**-12.6**	**-14.6**	**-15.6**	**-15.7**	**-15.8**
Financial assets	**13.1**	**12.2**	**11.3**	**10.6**	**9.9**	**8.6**	**7.2**	**6.1**	**4.6**	**3.7**	**2.8**
By instrument											
Currency and deposits 2/	12.8	11.9	11.0	10.4	9.7	8.4	7.0	5.9	4.4	3.5	2.6
Debt securities	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2
By residency											
Domestic	12.8	11.9	11.0	10.4	9.7	8.4	7.0	5.9	4.4	3.5	2.6
External	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2
By currency 3/											
Domestic	13.0	11.4	10.4	9.6	9.7	8.3	7.0	5.9	4.4	3.6	2.7
Foreign	0.4	0.4	0.3	0.3	0.3	0.3	0.2	0.2	0.1	0.1	0.1
Liabilities 4/	**17.7**	**15.8**	**14.9**	**16.2**	**17.4**	**18.5**	**19.8**	**20.8**	**20.1**	**19.4**	**18.6**
By instrument											
Debt securities	12.1	11.4	11.0	12.6	13.9	15.0	15.2	16.6	15.6	14.7	13.8
Loans	5.6	4.4	3.9	3.6	3.5	3.5	4.6	4.2	4.6	4.7	4.7
By residency											
Domestic	6.8	6.4	6.4	8.2	9.8	11.2	11.7	13.2	12.4	11.7	11.0
External	11.0	9.4	8.6	8.0	7.6	7.2	8.2	7.6	7.7	7.7	7.5
By currency 3/											
Domestic	10.6	10.2	10.3	-1.1	13.1	14.4	14.9	16.4	16.1	15.8	15.7
Foreign	7.1	5.6	4.6	17.3	4.3	4.1	5.0	4.4	4.1	3.6	2.9
Memorandum items											
Fiscal Stabilization Fund and other public savings	3.8	4.3	4.5	4.1	4.0	3.1	2.0	1.3	0.6	0.6	0.5
Debt of SOEs guaranteed by government 5/	0.7	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.5	0.5	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)

	2012	2013	2014	2015	Prel. 2016	Projections 2017	2018	2019	2020	2021	2022
Current account	**-5.2**	**-8.8**	**-8.9**	**-9.2**	**-5.3**	**-4.4**	**-4.6**	**-5.7**	**-6.8**	**-7.5**	**-7.8**
Merchandise trade	6.4	0.5	-1.5	-2.9	1.9	4.5	4.5	3.1	1.8	0.5	-0.1
Exports	47.4	42.9	39.5	34.4	37.0	41.8	43.7	44.9	46.3	47.8	49.3
Traditional	35.9	31.6	27.7	23.4	26.1	30.6	31.7	32.0	32.7	33.4	34.0
Mining	27.5	23.8	20.5	19.0	21.8	25.7	26.7	26.9	27.5	28.1	28.6
Nontraditional and others	11.5	11.3	11.8	11.0	10.9	11.2	12.0	12.9	13.6	14.4	15.2
Imports	-41.0	-42.4	-41.0	-37.3	-35.1	-37.4	-39.2	-41.8	-44.5	-47.3	-49.3
Services, income, and current transfers (net)	-11.6	-9.3	-7.4	-6.3	-7.2	-8.8	-9.1	-8.9	-8.6	-8.0	-7.7
Services	-2.5	-2.0	-1.9	-2.0	-2.0	-1.9	-2.0	-2.1	-2.1	-2.0	-2.0
Investment income	-12.4	-10.6	-9.9	-7.5	-9.2	-10.4	-10.7	-10.6	-10.6	-10.5	-10.6
Current transfers	3.3	3.3	4.4	3.3	4.0	3.4	3.6	3.8	4.1	4.5	4.9
Capital and financial account balance	**19.3**	**10.4**	**6.6**	**9.5**	**6.3**	**4.4**	**5.8**	**5.7**	**7.3**	**7.7**	**8.0**
Public sector	1.5	-1.8	-0.1	3.1	2.7	0.2	2.6	-0.2	1.5	1.1	0.8
Medium-term loans 1/	0.2	-1.3	1.3	4.0	0.2	0.3	2.9	-0.2	1.5	1.1	0.8
Other public sector flows 2/	1.7	-0.1	-0.7	-0.4	2.7	0.2	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	17.8	12.2	6.7	6.3	3.6	4.1	3.2	6.0	5.8	6.6	7.2
Foreign direct investment (net) 3/	11.7	9.7	3.6	8.1	6.6	5.4	5.6	5.8	5.8	5.8	5.8
Medium- and long-term loans	4.1	0.9	5.7	1.4	-1.7	-1.5	-0.8	-0.5	-0.2	0.1	0.3
Portfolio investment	-0.1	4.7	-1.8	-0.7	-1.2	-0.9	-0.8	-0.6	-0.6	-0.6	-0.6
Short-term flows 4/	2.1	-3.1	-0.9	-2.4	-0.1	1.1	-0.7	1.2	0.8	1.3	1.7
Errors and omissions	**0.7**	**1.3**	**0.1**	**-0.2**	**-0.8**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**14.8**	**2.9**	**-2.2**	**0.1**	**0.2**	**0.0**	**1.2**	**0.0**	**0.5**	**0.2**	**0.2**
Financing	**-14.8**	**-2.9**	**2.2**	**-0.1**	**-0.2**	**0.0**	**-1.2**	**0.0**	**-0.5**	**-0.2**	**-0.2**
NIR flow (increase -)	-14.8	-2.9	2.2	-0.1	-0.2	0.0	-1.2	0.0	-0.5	-0.2	-0.2
Change in NIR (increase -)	-15.2	-1.7	3.4	0.8	-0.2	0.0	-1.2	0.0	-0.5	-0.2	-0.2
Valuation change	0.4	-1.2	-1.2	-0.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
					(In percent of GDP)						
Current account balance	**-2.7**	**-4.4**	**-4.4**	**-4.8**	**-2.7**	**-2.1**	**-2.1**	**-2.4**	**-2.7**	**-2.8**	**-2.8**
Trade balance	3.4	0.3	-0.7	-1.5	1.0	2.1	2.0	1.3	0.7	0.2	0.0
Exports	25.1	21.7	19.5	17.9	19.0	20.0	19.8	19.1	18.6	18.2	17.7
Traditional	19.0	15.9	13.6	12.2	13.4	14.7	14.3	13.6	13.2	12.7	12.2
Mining	14.5	12.0	10.1	9.8	11.2	12.3	12.1	11.5	11.1	10.7	10.3
Nontraditional and others	6.1	5.7	5.8	5.7	5.6	5.3	5.4	5.5	5.5	5.5	5.5
Imports	-21.7	-21.4	-20.2	-19.4	-18.0	-17.9	-17.7	-17.8	-17.9	-18.0	-17.7
Services, income, and current transfers (net)	-6.1	-4.7	-3.7	-3.2	-3.7	-4.2	-4.1	-3.8	-3.5	-3.0	-2.8
Investment income	-6.6	-5.4	-4.9	-3.9	-4.7	-5.0	-4.8	-4.5	-4.3	-4.0	-3.8
Capital and financial account balance	**10.2**	**5.3**	**3.3**	**4.9**	**3.2**	**2.1**	**2.6**	**2.4**	**2.9**	**2.9**	**2.9**
Foreign direct investment (net)	6.2	4.9	1.8	4.2	3.4	2.6	2.5	2.5	2.3	2.2	2.1
Overall balance	**7.8**	**1.5**	**-1.1**	**0.0**	**0.1**	**0.0**	**0.5**	**0.0**	**0.2**	**0.1**	**0.1**
Memorandum items					(Annual percentage change)						
Export value	2.2	-9.6	-7.8	-12.9	7.6	12.9	4.5	2.7	3.2	3.2	3.1
Volume growth	4.6	-4.2	-1.0	2.4	11.6	1.8	3.8	2.6	3.0	2.7	2.4
Price growth	-2.2	-5.7	-6.9	-15.0	-3.6	10.9	0.7	0.1	0.2	0.4	0.7
Import value	10.4	3.3	-3.1	-9.0	-5.9	6.3	5.0	6.5	6.6	6.2	4.4
Volume growth	10.4	3.8	-1.6	0.2	-3.0	0.6	3.5	5.2	5.3	4.5	3.0
Price growth	0.0	-0.5	-1.5	-9.2	-3.0	5.6	1.4	1.3	1.2	1.7	1.4
Terms of trade	-2.3	-5.2	-5.4	-6.4	-0.7	5.0	-0.8	-1.1	-1.0	-1.2	0.7
Gross international reserves (in billions of US$)	64.0	65.7	62.4	61.5	61.7	61.7	62.9	62.9	63.4	63.6	63.8

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)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
						Projections					
						I. Central Reserve Bank					
Net foreign assets	**138**	**144**	**140**	**133**	**142**	**140**	**142**	**141**	**142**	**142**	**142**
(In billions of U.S. dollars)	74	80	78	84	81	82	84	84	85	86	86
Net international reserves 2/	163	184	186	210	207	208	213	214	216	217	218
(In billions of U.S. dollars)	64	66	62	61	62	62	63	63	63	64	64
Long-term net external assets	0	0	0	0	0	0	0	0	0	0	0
Foreign currency liabilities	-25	-40	-46	-77	-66	-69	-71	-73	-74	-75	-76
Net domestic assets	**-85**	**-92**	**-86**	**-82**	**-88**	**-80**	**-76**	**-68**	**-60**	**-51**	**-41**
Net credit to nonfinancial public sector	-55	-61	-67	-71	-76	-72	-65	-59	-54	-49	-44
Credit to the financial sector 3/	-9	-8	2	23	22	22	22	22	22	22	22
Securities issued	-27	-22	-14	-20	-21	-23	-26	-28	-31	-34	-38
Other assets (net)	6	-2	-6	-13	-13	-7	-8	-3	3	10	18
Monetary base	**53**	**52**	**54**	**51**	**53**	**59**	**66**	**73**	**82**	**91**	**101**
Currency	32	35	39	41	43	46	51	56	61	67	73
Reserve	20	17	15	11	10	13	15	18	20	24	28
						II. Depository Corporations 4/					
Net foreign assets	**132**	**152**	**152**	**171**	**176**	**176**	**181**	**181**	**184**	**185**	**185**
Net domestic assets	**45**	**52**	**72**	**78**	**85**	**98**	**114**	**137**	**159**	**184**	**212**
Net credit to the public sector	-69	-73	-73	-78	-78	-59	-42	-18	-8	-2	5
Credit to the private sector	168	198	224	256	269	283	301	321	342	364	389
Other assets (net)	-53	-74	-79	-100	-106	-127	-144	-166	-175	-178	-182
Broad money	**177**	**204**	**224**	**250**	**260**	**274**	**295**	**318**	**343**	**369**	**397**
Domestic currency	123	137	152	156	170	185	205	227	251	278	307
Foreign currency	54	67	72	94	90	89	90	91	91	91	90
						III. Financial System 5/					
Net foreign assets	**178**	**203**	**211**	**237**	**246**	**241**	**246**	**247**	**249**	**250**	**251**
Net domestic assets	**115**	**119**	**143**	**157**	**178**	**204**	**235**	**271**	**308**	**350**	**395**
Net credit to the public sector	-51	-58	-50	-52	-45	-33	-24	-10	-4	-1	3
Credit to the private sector	213	240	271	303	323	341	373	409	447	486	527
Other assets (net)	-48	-63	-77	-94	-100	-103	-115	-128	-134	-135	-134
Liabilities to the private sector	**293**	**322**	**355**	**394**	**424**	**446**	**481**	**518**	**558**	**600**	**646**
Domestic currency	229	246	273	288	317	340	373	410	450	493	541
Foreign currency	64	76	82	106	107	106	107	108	108	107	105
						(12-month percentage change)					
Monetary base	31.9	-1.5	3.7	-4.8	4.1	10.7	11.4	11.5	11.3	11.1	11.1
Broad money	12.5	15.3	9.5	11.6	4.3	5.2	7.8	7.8	7.6	7.6	7.7
Domestic currency	23.3	11.6	10.6	3.0	9.1	8.4	11.0	10.9	10.7	10.5	10.5
Foreign currency	-6.2	23.6	7.3	29.8	-3.6	-0.9	1.2	0.8	0.1	-0.5	-1.1
Liabilities to the private sector	15.4	10.1	10.2	10.9	7.7	5.2	7.8	7.8	7.6	7.6	7.7
Domestic currency	22.4	7.6	11.1	5.5	9.9	7.3	9.9	9.9	9.7	9.6	9.6
Foreign currency	-4.3	19.0	7.4	29.2	1.6	-1.1	1.0	0.6	-0.1	-0.8	-1.4
Depository corporations credit to the private sector	13.3	18.3	13.2	14.0	5.0	5.2	6.5	6.6	6.5	6.6	6.7
Domestic currency	16.0	22.6	17.7	28.4	6.8	7.0	8.8	8.8	8.5	8.5	8.5
Foreign currency	9.8	12.6	6.5	-9.4	0.8	0.7	0.5	0.5	0.5	0.4	0.2

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)

	2012	2013	2014	2015	2016
		(as of December)			
Capital Adequacy					
Capital to risk-weighted assets 2/	14.4	13.9	14.2	14.3	15.1
Regulatory Tier I capital to risk-weighted assets 3/	10.9	10.4	10.4	10.3	11.0
Nonperforming loans net of provisions to capital 4/	-12.6	-10.8	-9.0	-9.4	-9.1
Leverage 5/	7.9	7.9	8.3	7.9	8.7
Asset Quality					
Nonperforming loans to total gross loans 4/	2.2	2.6	2.9	2.9	3.1
In domestic currency	3.0	3.3	3.4	2.9	3.2
In foreign currency	1.1	1.5	2.1	2.9	2.8
Nonperforming, refinanced and restructured loans to total gross loans 4/ 6/	3.2	3.6	4.0	4.0	4.4
In domestic currency	4.2	3.3	3.4	2.9	3.2
In foreign currency	1.8	1.5	2.1	2.9	2.8
Refinanced and restructured loans to total gross loans	1.1	1.0	1.1	1.1	1.3
Provisions to nonperforming loans 4/	202.0	175.2	157.7	161.8	157.1
Provisions to nonperforming, restructured, and refinanced loans 4/ 6/	134.9	126.3	114.4	116.5	111.1
Sectoral distribution of loans to total loans					
Consumer loans	19.1	18.4	18.1	18.3	18.9
Mortgage loans	14.7	15.3	15.5	15.2	15.1
Large corporations	15.8	17.6	17.2	21.4	22.2
Small corporations	15.3	15.5	17.0	15.8	14.8
Medium size firms	17.5	17.6	18.3	16.9	16.4
Small firms	12.5	11.4	10.1	9.0	9.1
Microenterprises	5.2	4.3	3.8	3.4	3.6
Earnings and Profitability					
Return on equity (ROE)	21.5	20.0	18.2	21.1	19.2
Return on assets (ROA)	2.2	2.0	1.9	2.1	2.0
Financial revenues to total revenues	82.7	85.6	85.0	85.2	85.3
Annualized financial revenues to revenue-generating assets	11.2	10.9	10.6	10.5	10.1
Liquidity					
Total liquid assets to total short-term liabilities (monthly average basis)	45.0	43.0	39.4	37.7	35.4
In domestic currency	44.2	31.4	25.3	26.2	26.7
In foreign currency	46.2	56.4	55.2	47.5	44.9
Deposit-to-loan	95.2	98.1	90.5	92.0	88.4
Foreign Currency Position and Dollarization					
Share of foreign currency deposits in total deposits	38.2	43.6	43.4	49.5	44.1
Share of foreign currency loans in total credit	44.4	41.1	38.4	30.1	28.8
Operational efficiency					
Financing to related parties to capital 7/	11.5	9.3	9.4	12.3	9.1
Nonfinancial expenditure to total revenues 8/	33.6	33.7	33.0	30.9	30.8
Annualized Nonfinancial expenditure to total revenue-generating assets 8/	4.6	4.3	4.1	3.8	3.7
Memorandum items					
General Stock market index, IGBVL	20,629	15,754	14,794	9,849	15,567
EMBI+ PERU spread, basis points	117	174	181	243	170

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. Figures are net of specific and general provisions.

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)

	2012	2013	2014	2015	Prel. 2016	Projections 2017	2018	2019	2020	2021	2022
Financial indicators											
Public sector debt/GDP	21.6	20.8	20.7	24.0	24.4	25.2	26.4	27.0	26.8	26.3	25.7
Of which: in domestic currency (percent of GDP)	11.0	11.8	12.0	12.9	14.1	15.3	15.7	17.1	16.8	16.4	16.2
90-day prime lending rate, domestic currency (end of period)	5.0	4.5	4.7	4.9	5.2	...	...	...	...	...	...
90-day prime lending rate, foreign currency (end of period)	4.0	1.0	0.7	1.1	1.2	...	...	...	...	...	...
Velocity of money 1/	2.8	2.6	2.6	2.5	2.5	2.6	2.5	2.5	2.5	2.4	2.4
Net credit to the private sector/GDP 2/	33.6	37.1	38.9	41.8	40.8	40.1	40.2	40.3	40.4	40.6	40.8
External indicators											
Exports, U.S. dollars (percent change)	2.2	-9.6	-7.8	-12.9	7.6	12.9	4.5	2.7	3.2	3.2	3.1
Imports, U.S. dollars (percent change)	10.4	3.3	-3.1	-9.0	-5.9	6.3	5.0	6.5	6.6	6.2	4.4
Terms of trade (percent change) (deterioration -) 3/	-2.3	-5.2	-5.4	-6.4	-0.7	5.0	-0.8	-1.1	-1.0	-1.2	0.7
Current account balance (percent of GDP)	-2.7	-4.4	-4.4	-4.8	-2.7	-2.1	-2.1	-2.4	-2.7	-2.8	-2.8
Capital and financial account balance (percent of GDP)	10.2	5.3	3.3	4.9	3.2	2.1	2.6	2.4	2.9	2.9	2.9
Total external debt (percent of GDP)	27.8	27.2	30.6	34.6	33.5	30.0	28.8	26.4	25.1	23.8	22.4
Medium- and long-term public debt (in percent of GDP) 4/	10.3	8.7	8.3	10.4	10.4	9.8	10.6	9.9	10.0	9.8	9.5
Medium- and long-term private debt (in percent of GDP)	12.7	15.3	19.2	20.7	19.4	16.9	15.3	13.9	12.9	11.9	11.2
Short-term public and private debt (in percent of GDP)	4.7	3.1	3.1	3.5	3.7	3.3	2.9	2.6	2.3	2.0	1.7
Total external debt (in percent of exports of goods and services) 4/	100.4	110.4	136.6	163.6	150.7	130.0	126.8	120.0	117.0	113.6	110.1
Total debt service (in percent of exports of goods and services) 5/	11.0	16.6	16.5	18.9	21.6	22.4	13.9	15.1	13.0	12.6	12.8
Gross official reserves											
In millions of U.S. dollars	64,049	65,710	62,353	61,530	61,731	61,731	62,931	62,931	63,431	63,631	63,831
In percent of short-term external debt 6/	495.9	536.5	534.3	523.0	449.8	410.5	603.6	586.5	667.4	701.3	712.1
In percent of short-term external debt, foreign currency deposits, and adjusted CA balance 6/ 7/	132.9	125.7	131.2	112.9	121.6	123.6	137.1	132.0	133.6	134.1	134.6
In percent of broad money 8/	93.2	90.0	83.2	84.1	79.6	76.2	72.2	67.2	63.1	58.9	54.9
In percent of foreign currency deposits at banks	300.5	273.9	257.8	224.3	230.1	233.4	235.8	234.6	237.0	239.3	242.6
In months of next year's imports of goods and services	15.3	16.1	16.4	17.0	16.2	15.5	14.9	14.1	13.5	13.0	n.a.
Net international reserves (in millions of U.S. dollars)	63,991	65,663	62,308	61,485	61,686	61,686	62,886	62,886	63,386	63,586	63,786
Central Bank's Foreign Exchange Position	46,063	41,097	35,368	25,858	27,116	27,116	28,316	28,316	28,816	29,016	29,216

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

					Prel.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	(Annual percentage change)										
Production											
GDP at constant prices	6.0	5.8	2.4	3.3	3.9	2.7	3.8	4.0	3.9	3.8	3.8
Consumer prices (end of period)	2.6	2.9	3.2	4.4	3.2	2.9	2.5	2.5	2.4	2.2	2.0
GDP deflator	1.2	1.4	5.3	2.9	3.5	4.1	2.3	2.4	2.3	2.2	2.3
Trade											
Merchandise trade											
Exports, f.o.b.	2.2	-9.6	-7.8	-12.9	7.6	12.9	4.5	2.7	3.2	3.2	3.1
Imports, f.o.b.	10.4	3.3	-3.1	-9.0	-5.9	6.3	5.0	6.5	6.6	6.2	4.4
Terms of trade (deterioration -)	-2.3	-5.2	-5.4	-6.4	-0.7	5.0	-0.8	-1.1	-1.0	-1.2	0.7
	(In percent of GDP; unless otherwise indicated)										
External current account balance	-2.7	-4.4	-4.4	-4.8	-2.7	-2.1	-2.1	-2.4	-2.7	-2.8	-2.8
Total external debt service 1/	3.0	4.1	3.7	4.0	4.8	5.2	3.2	3.3	2.8	2.6	2.6
Medium- and long-term	3.0	4.0	3.7	3.9	4.7	5.1	3.0	3.2	2.7	2.5	2.5
Nonfinancial public sector	1.2	1.9	1.3	1.3	1.6	2.4	0.8	1.1	0.8	0.8	0.9
Private sector	1.8	2.1	2.4	2.7	3.1	2.6	2.3	2.1	1.9	1.8	1.6
Short-term 2/	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
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	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Interest	0.9	1.0	1.1	1.4	1.4	1.2	1.3	1.3	1.2	1.2	1.1
Amortization (medium-and long-term)	2.1	3.1	2.6	2.6	3.3	3.9	1.8	2.0	1.6	1.5	1.5
Public sector											
NFPS primary balance 3/	3.5	2.0	0.9	-1.0	-1.5	-1.7	-2.1	-1.5	-0.5	0.3	0.4
General government revenue	22.8	22.8	22.3	20.0	18.7	18.6	18.7	18.8	19.1	19.3	19.2
General govt. non-interest expenditure 3/	24.8	26.4	27.1	26.0	24.7	24.8	25.3	24.9	24.1	23.5	23.3
NFPS interest due	1.1	1.1	1.1	1.0	1.1	1.2	1.4	1.4	1.4	1.4	1.4
NFPS overall balance 3/	2.4	0.9	-0.2	-2.0	-2.6	-3.0	-3.5	-2.9	-1.9	-1.0	-1.0
Public sector debt 3/	21.6	20.8	20.7	24.0	24.4	25.2	26.4	27.0	26.8	26.3	25.7
Savings and investment											
Gross domestic investment	24.7	26.5	24.9	24.6	22.8	22.2	22.2	23.0	23.8	24.4	24.4
Public sector 3/	5.5	5.9	5.5	5.0	4.8	5.2	5.6	5.6	5.3	5.1	5.1
Private sector	19.2	20.6	19.4	19.6	18.1	17.0	16.5	17.4	18.5	19.3	19.3
Private sector (excluding inventories)	20.7	21.2	20.1	19.3	17.7	16.7	16.5	17.3	18.4	19.3	19.4
Inventory changes	-1.5	-0.7	-0.8	0.3	0.3	0.3	0.0	0.0	0.0	0.0	-0.1
National savings	22.0	22.0	20.5	19.8	20.1	20.1	20.1	20.6	21.0	21.6	21.5
Public sector 4/	8.2	7.2	6.0	3.8	2.7	2.7	2.7	3.3	4.0	4.6	4.3
Private sector	13.7	14.8	14.4	16.1	17.4	17.3	17.4	17.2	17.1	17.0	17.2
External savings	2.7	4.4	4.4	4.8	2.7	2.1	2.1	2.4	2.7	2.8	2.8
Memorandum items											
Nominal GDP (billions of nuevos soles)	498.5	534.7	576.3	612.8	658.7	703.9	747.8	796.0	845.9	897.6	952.3
Gross international reserves (billions of U.S. dollars)	64.0	65.7	62.4	61.5	61.7	61.7	62.9	62.9	63.4	63.6	63.8
External debt service (percent of exports of GNFS)	11.0	16.6	16.5	18.9	21.6	22.4	13.9	15.1	13.0	12.6	12.8
Short-term external debt service (percent of exports of GNFS)	0.2	0.2	0.2	0.3	0.4	0.4	0.5	0.6	0.5	0.5	0.4
Public external debt service (percent of exports of GNFS)	4.4	7.6	5.8	6.0	7.2	10.5	3.5	5.1	3.6	3.7	4.3

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, 2014–22
(In percent of GDP, unless otherwise indicated)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	Debt-stabilizing non-interest current account 6/
				Projections						
Baseline: External debt	**30.6**	**34.6**	**33.5**	**30.0**	**28.8**	**26.4**	**25.1**	**23.8**	**22.4**	**-2.0**
Change in external debt	3.4	4.0	-1.1	-3.4	-1.2	-2.4	-1.3	-1.3	-1.3	
Identified external debt-creating flows (4+8+9)	2.8	-0.2	-1.4	-0.9	-1.1	-0.9	-0.3	0.0	0.1	
Current account deficit, excluding interest payments	3.3	3.3	1.3	0.9	0.7	1.1	1.5	1.7	1.7	
Deficit in balance of goods and services	1.7	2.6	0.0	-1.2	-1.1	-0.5	0.1	0.6	0.7	
Exports	22.4	21.1	22.2	23.1	22.7	22.0	21.4	20.9	20.4	
Imports	24.1	23.7	22.3	21.9	21.6	21.5	21.5	21.5	21.1	
Net non-debt creating capital inflows (negative)	-0.9	-3.9	-2.8	-2.2	-2.1	-2.2	-2.1	-2.0	-1.9	
Net foreign direct investment, equity	1.8	4.2	3.4	2.6	2.5	2.5	2.3	2.2	2.1	
Net portfolio investment,equity	-0.9	-0.4	-0.6	-0.4	-0.4	-0.3	-0.2	-0.2	-0.2	
Automatic debt dynamics 1/	0.5	0.4	0.1	0.4	0.3	0.2	0.2	0.3	0.3	
Denominator: 1+g+r+gr	1.0	0.9	1.0	1.1	1.1	1.1	1.1	1.1	1.1	
Contribution from nominal interest rate	1.1	1.4	1.4	1.2	1.3	1.3	1.2	1.2	1.1	
Contribution from real GDP growth	-0.6	-1.1	-1.3	-0.8	-1.1	-1.1	-1.0	-0.9	-0.8	
Contribution from price and exchange rate changes 2/	...	...	...	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	0.6	4.1	0.3	-2.5	-0.1	-1.5	-1.0	-1.3	-1.4	
External debt-to-exports ratio (in percent)	136.6	163.6	150.7	130.0	126.8	120.0	117.0	113.6	110.1	
Gross external financing need (in billions of U.S. dollars) 4/	20.4	20.5	18.7	19.8	15.4	16.9	16.7	16.9	17.1	
In percent of GDP	10.1	10.6	9.6	9.5	7.0	7.2	6.7	6.4	6.1	
Scenario with key variables at their historical averages 5/		**34.6**	**33.5**	**27.6**	**23.6**	**18.3**	**13.7**	**9.1**	**4.6**	**-4.3**
Key Macroeconomic Assumptions Underlying Baseline										
Real GDP growth (in percent)	2.4	3.3	3.9	2.7	3.8	4.0	3.9	3.8	3.8	
GDP deflator in U.S. dollars (change in percent)	0.2	-8.3	-2.4	4.3	1.9	2.1	2.0	2.0	2.2	
Nominal external interest rate (in percent)	4.1	4.4	4.2	3.9	4.7	4.8	4.8	4.9	5.0	
Growth of exports and services (U.S. dollar terms, in percent)	-6.6	-10.6	6.6	11.4	4.1	2.8	3.1	3.3	3.3	
Growth of imports and services (U.S. dollar terms, in percent)	-2.6	-6.7	-4.8	5.3	4.5	5.9	5.9	5.6	4.1	
Current account balance, excluding interest payments	-3.3	-3.3	-1.3	-0.9	-0.7	-1.1	-1.5	-1.7	-1.7	
Net non-debt creating capital inflows	0.9	3.9	2.8	2.2	2.1	2.2	2.1	2.0	1.9	

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 Fund Advice

1. **The authorities' policies have largely been in line with past Fund advice.** The authorities have implemented most of the 2011 FSAP recommendations—particularly in the areas of banking oversight, insurance, and pensions—and are looking forward to the planned 2018 FSAP Update. In addition, there has been a significant collaboration via technical assistance on a wide range of areas, with the current focus being on fiscal, monetary, and statistical issues.

2. **More recently, the authorities' policies have been consistent with the main recommendations of the 2016 Article IV Consultations.** More specifically,

- *Fiscal policy:* the 2016 Article IV consultation advised a gradual fiscal consolidation, along with the creation of fiscal space to accommodate higher capital spending. The government's 2017 budget and reform package went quite deeply in this direction, with the budget (and medium-term fiscal plans) envisaging a consolidation of the fiscal accounts, while boosting public investment. Regarding the latter, the government introduced reforms to improve the PPP framework and the system of public investment. Furthermore, the authorities have been receptive to staff's recommendation of being cautious with planned reductions in the VAT rate.

- *Monetary and exchange rate policy:* the BCRP has continued to implement a flexible exchange rate regime, and its wait-and-see policy rate stance during the past year and the cut in the policy rate in May 2017 have been consistent with Fund advice.

- *Structural reforms:* the government has introduced a set of structural reforms to reduce informality and cut red tape (e.g., modifications to the income tax regime to small and medium enterprises), while the Fund's advice of introducing labor market reforms aimed at lowering the costs of hiring and firing workers remains an area that the authorities are exploring carefully.

3. **The recent modification of the fiscal framework, however, runs against past Fund advice.** The 2013 fiscal framework was put together with Fund support, and was anchored on a *structural* deficit rule for the overall balance of the Nonfinancial Public Sector (NFPS). The use of the structural deficit rule injected a component of countercyclicality into the framework, which was complemented with benchmarks for the NFPS gross debt, as well as rules regarding the activities of local and regional governments. The 2016 (new) framework contains very similar numerical parameters to the previous one, but the main anchors are now ceilings on the headline deficit and gross debt stock of the NFPS (table). The new fiscal framework maintains other dispositions of its predecessor, such as the role of the independent fiscal council, and will continue to calculate and publish the structural fiscal balance.

Peru: Comparison of the Main Features of the New and Previous Fiscal Frameworks

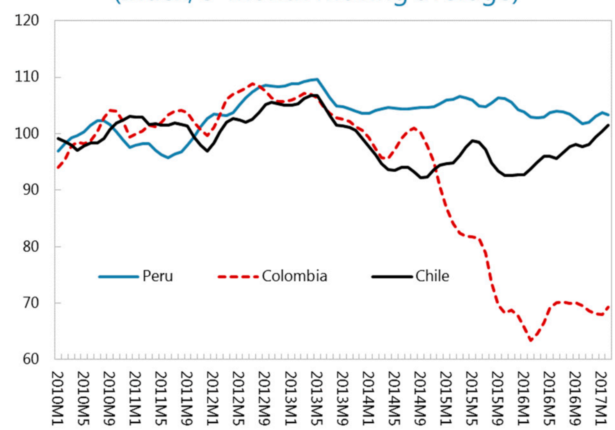
	2016 Framework	2013 Framework
Nonfinancial Public Sector		
Debt rule	Gross debt of the NFPS shall not exceed 30 percent of GDP. In cases of financial volatility, and if the other rules are met, the debt could experience temporary deviations of at most four percentage points of GDP.	The provision on debt limits was part of the corrective actions. It stated that if the debt surpassed 30 percent of GDP, or if it is expected to surpass that limit in the next three years, then corrective actions should be taken to bring debt below 30 percent of GDP in a period of at most seven years.
Fiscal deficit rule	The annual deficit of the NFPS shall not exceed 1 percent of GDP. Transitory provisions apply to transition from the current state to the new target, which is set to be achieved by 2021.	Within 90 days of taking office, the new administration shall issue a strategy of macro fiscal policy for the whole presidential term. This strategy shall provide ex ante guidance on the structural deficit of the NFPS, which shall not exceed 1 percent of GDP.
Expenditure rule	There is a dual expenditure rule, which imposes a ceiling in the growth of: (i) the real non-interest expenditure of the general government, and (ii) the real current expenditure of the general government. The ceiling is determined using as reference the average 20 year growth of real GDP (with the 20 years including, the past 15 years, the estimated growth of the year in which the Multiannual Macroeconomic Framework is elaborated, and the projected growth of the next four years).	The non interest expenditure of the national government shall not exceed the limit established under the strategy for the ex ante attainment of the structural deficit rule.
Regional and Local Governments		
Debt rule	The ratio between total debt and the average of current revenues for the past four years, or the ratio between total debt and a limit established in a complementary law (whichever is lower), cannot exceed 100 percent.	The ratio between total debt and the average of current revenues for the past four years cannot exceed 100 percent.
Expenditure rule	Expenditure needs to be consistent with savings rule.	The percent change in nonfinancial expenditures cannot exceed the four-year moving average of total revenues (counted from the second year before every fiscal year) .
Savings Rule	The difference between total current revenues and nonfinancial current expenditures shall not be negative.	N.A.
Credit rating exception	Regional or local governments with a crdit rating of BBB+ or higher, may conduct financing operations even though those may result in a breach of the previous fiscal rules or of the corrective actions to achieve them.	N.A.

Annex II. External Sector Assessment

Peru's external position is assessed to be broadly consistent with fundamentals and appropriate policy settings. The current account narrowed to 2¾ percent of GDP in 2016, which reduced the real effective exchange rate gap to be in line with fundamentals. Reserve adequacy remains satisfactory, notwithstanding the impact of volatile commodity prices from Peru's large mining exports and the presence of large domestic FX liabilities in foreign reserves. Over the medium term, the current account is expected to widen somewhat but remain financed largely by longer-term FDI flows.

1. The current account improved markedly between 2015 and 2016, from a deficit of 4.9 percent of GDP in 2015, to 2.7 percent of GDP in 2016. This improvement follows a sharp turnaround in the goods balance, which went from a 2015 deficit of -1.6 percent of GDP to a 2016 surplus of 0.9 percent of GDP—improving by some 2½ percentage points. The improvement in the merchandise balance was largely thanks to strong export growth, particularly in copper exports, as well as import compression due to lower non-oil intermediate and capital goods imports. These factors largely reflect the shift from construction to production stage of a number of mega mining projects. The coming on-stream of these projects boosted copper volume exports by over 40 percent on average, while the drag from falling prices was gradually being reversed. Non-metals exports remained broadly stable, despite impressive growth in selected sectors such as agropecuarios. The better outcome in the trade balance was partially offset by higher outflows in the income account, as profits recovered by some 25 percent. Over the medium term, the current account is expected to widen somewhat as the trade surplus falls, and would remain financed mainly by FDI flows.

Real Effective Exchange Rate
(Index, 3-month moving average)



Source: Fund staff estimates.

2. The real effective exchange rate remained broadly constant since the 2016 Article IV Consultation and external position is assessed as consistent with fundamentals and policy settings. As the real effective exchange rate remained broadly constant and the assessment of the CA norm remained broadly unchanged from the previous year, as did the estimate of the small policy gap (0.4 percent of GDP in 2016), the improvement in the current account narrowed the CA gap compared to 2015. As a result, the moderate real effective exchange rate overvaluation disappeared in 2016. The REER level regression results reported in the table above have historically shown large residuals for Peru and are therefore considered less reliable than other estimates.

Current Account and REER Gaps, 2016
(in percent of GDP, unless stated otherwise)

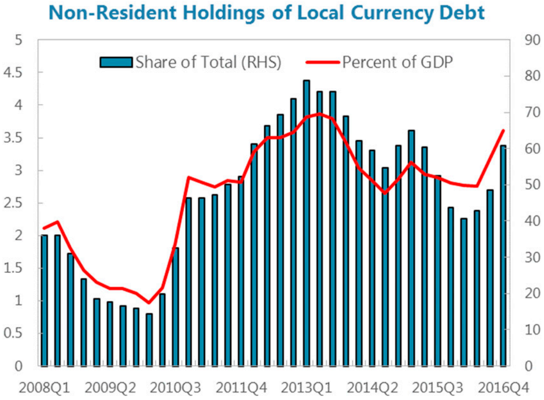
	EBA methodology			
	CA regression	RER regression (index)	RER regression (level)	External Sustainability Approach
CA headline	-2.7	..	..	-2.7
CA underlying 1/	-1.4	..	..	-1.4
CA norm	-1.5	..	..	-2.0
CA gap 2/	0.1	..	..	0.6
RER gap (in percent) 3/	***-0.5***	***2.7***	***13.5***	***-2.9***
Adjusted 4/				
CA underlying 1/	-1.0	..	..	-1.0
CA norm	-1.5	..	..	-2.0
CA gap 2/	0.5	..	..	1.0
RER gap (in percent) 3/	***-2.3***	***2.7***	***13.5***	***-4.7***

Source: Fund staff estimates.

1/ Cyclically adjusted CA for EBA results. Medium term adj. CA for ES Approach.
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.

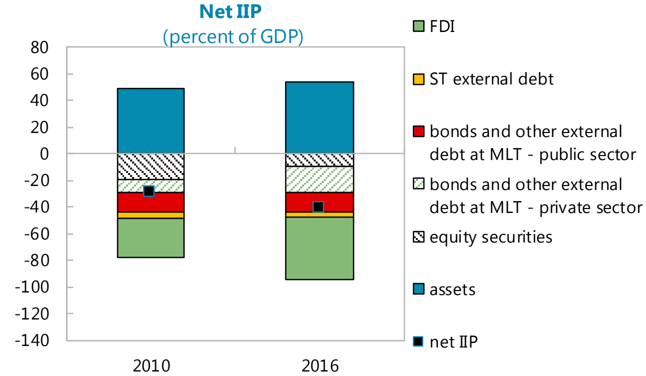
3. Capital inflows are dominated by FDI and pose limited risks. Peru's negative IIP position increased to -38.6 percent of GDP at end-2016 largely due to large FDI inflows (3.4 percent of GDP in 2016) amid broadly stable foreign reserves and other assets. External debt remained broadly unchanged, with the increase in public external debt offsetting the decline in private external debt—the latter due to a drop in disbursements of MLT loans. Non-resident holdings of domestic public debt increased in 2016, but the total size of such holdings amounts to a mere 3.6 percent of GDP. Peru's negative IPP position is the result of significant external assets (53 percent of GDP)—including sizeable holdings of foreign assets by the central bank (32 percent of GDP)—that are offset by large FDI liabilities (47 percent of GDP), moderate MLT external indebtedness (public and private external debt remains below 35 percent of GDP). Short term external debt and other liabilities remain small.

Non-Resident Holdings of Local Currency Debt



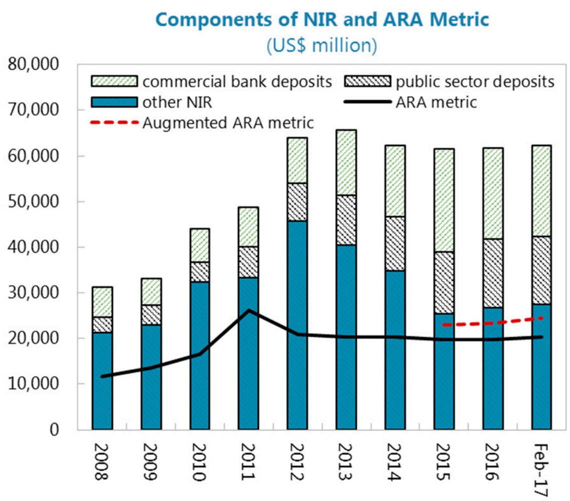
Sources: BCRP; and Fund staff estimates.

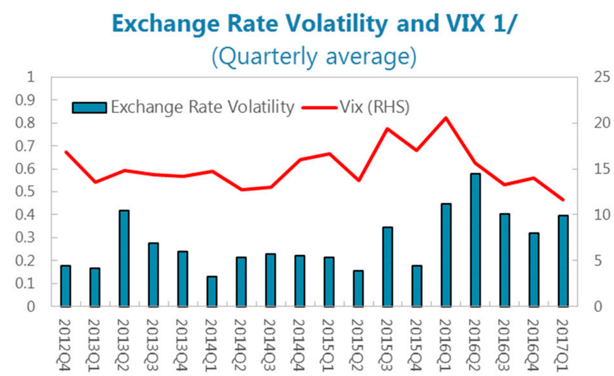
Net IIP
(percent of GDP)



Source: Fund staff estimates.

4. Peru's gross international reserve coverage exceeds adequacy metrics. Gross and net international reserves remained broadly unchanged in 2016, ending at US$61.7 billion (32 percent of GDP), or 310 percent of the ARA metric, which is well above the 100–150 percent adequacy range. However, a large share of GIR consists of domestic FX liabilities, mainly reserve requirements on FX deposits with commercial banks, FX reserves in the Fiscal Stabilization Fund, and deposits corresponding to FX repos introduced as part of the BCRP's de-dollarization program. A small amount of the FX repos is expected to come due in 2017, but the majority will come due in 2020, hence not posing a short-term risk to GIR. Other FX liabilities serve the purpose of reducing dollar liquidity risks under partial dollarization, and providing countercyclical savings that can only be used as regulated in the law. Excluding these domestic FX liabilities, reserves remain within the adequacy range. Reserves are also adequate when taking into account Peru's heavy reliance on commodity exports—at 264 percent of the augmented metric, and excluding domestic FX liabilities, 115 percent of the augmented metric.



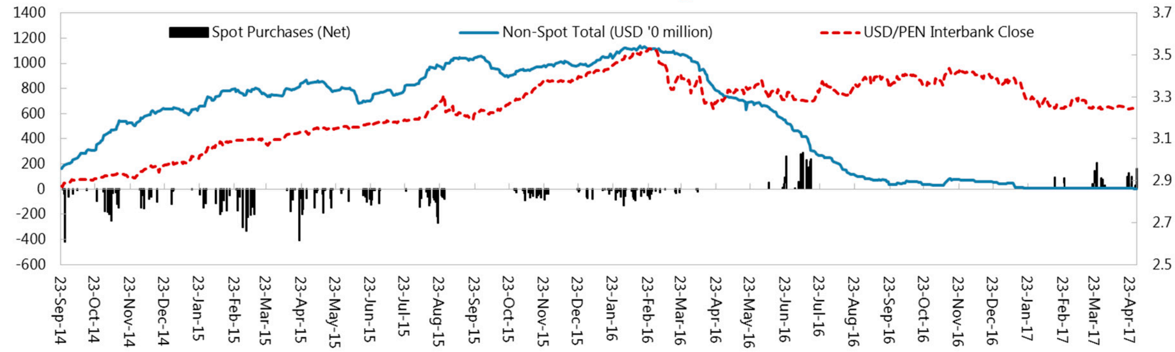


1/ Exchange rate volatility measured as standard deviation of daily exhange rate change. See IMF Country Report 16/235.

Sources: BCRP; and Fund staff estimates.

5. The BCRP unwound a large stock of non-spot intervention instruments and reduced its spot market intervention, while exchange rate volatility increased. In 2016Q1, the central bank sold some US$1.2 billion in the spot market, amid gradual depreciation of the sol. A course reverse took place in the remainder of 2016, following the elections and as copper prices rebounded: spot market sales in 2016Q2–Q4 amounted to US$2 billion and the BCRP was able to fully unwound the stock of non-spot intervention instruments—Certificates of Deposit linked to the exchange rate (CDRs) and sales of FX swaps—which in early 2016 peaked at US$11 billion (5½ percent of GDP)—amid a moderate appreciation. Net purchases continued in early 2017, amounting to US$0.8 billion in 2017Q1 and GIR increased to US$62.3 by end-February 2017.

Intervention and Exchange Rate

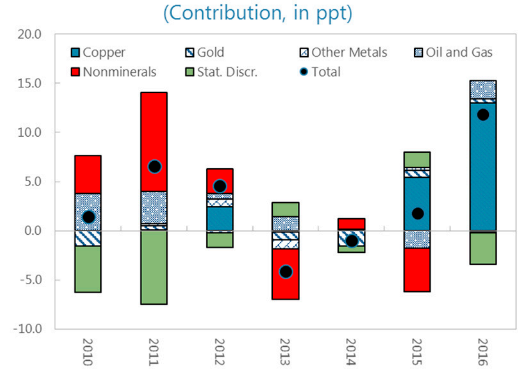


Sources: BCRP, and IMF calculations.

Special Feature. Nontraditional Exports

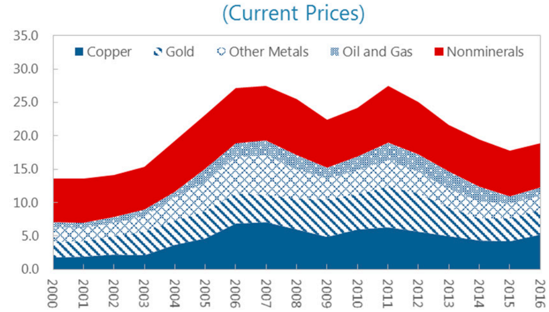
Peru's recent impressive export growth has been dominated by developments in metals, and especially copper. With new capacity in mining coming on stream, growth of copper exports has amounted to over 40 percent in 2016 in volume terms, being the main driver behind overall export volume growth. Overall, metals—largely copper, but gold, lead and zinc are important as well—along with other mineral exports (oil and gas) account for about half of total export value.

Export Volume Growth
(Contribution, in ppt)

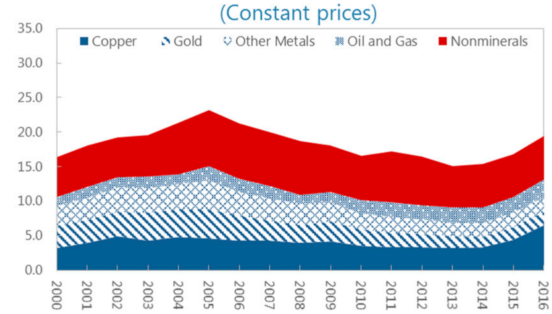


Source: Fund staff estimates.

Exports in Percent of GDP
(Current Prices)



Exports in Percent of GDP
(Constant prices)

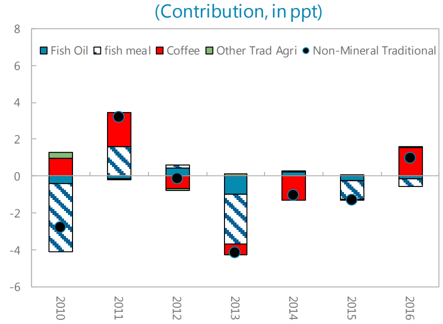


Source: Fund staff estimates.

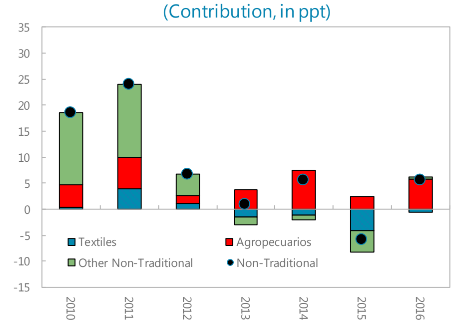
Peru's non-mineral exports, however, have shown more mixed dynamics recently. Non-mineral exports account for the other half of total export value, but their contribution to total export growth has been largely negative in the last four years. First, other 'traditional' products such as fishmeal and fish oil—Peru is the leading world exporter—and agricultural exports such as coffee and cocoa, have seen mostly negative volume growth, due to natural phenomena—El Niño—and coffee crop related diseases. Second, the 'non-traditional' products, which cover a variety of commodities including textiles, agropecuarios, and manufacturing products such as paper, wood, chemical or metallurgical products, among others—have shown particular dynamism for agropecuarios, but textiles and other non-traditional exports have been mostly in contractionary territory.

Special Feature. Nontraditional Exports (continued)

Export Volume Growth - Other Traditional
(Contribution, in ppt)



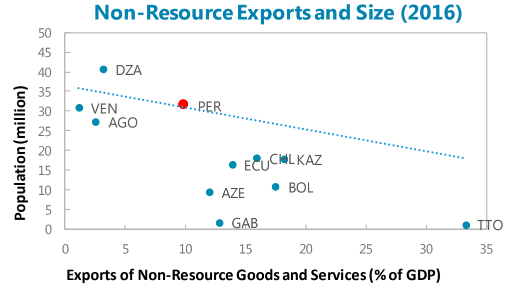
Export Volume Growth - Non Traditional
(Contribution, in ppt)



Non-Resource Exports 1/
(Percent of total goods exports, average 2010-16)

1/ Excludes HS 26, 27, 74; WEO non-oil exports for GAB, TTO.

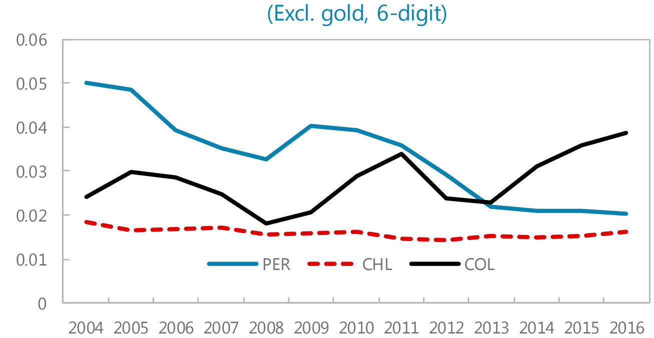
Non-Resource Exports and Size (2016)



Source: Fund staff estimates.

Non-mineral exports are relatively diversified. Compared to other emerging or frontier market commodity exporters, Peru's non-commodity exports—on average at 55 percent of total exports since 2010—are relatively sizeable and higher than those of neighboring commodity exporters such as Chile, Ecuador, or Bolivia. This points to a higher degree of diversification of Peru's export base. The magnitude of Peru's non-commodity exports, measured as a percent of GDP, also compares well with what would be expected, that is, after controlling for size (measured by population)—given Peru's larger domestic market, export shares in percent of GDP are expected to be smaller than those of other countries, but this bias disappears after controlling for size.

Concentration Index, Exports of Non-Minerals
(Excl. gold, 6-digit)

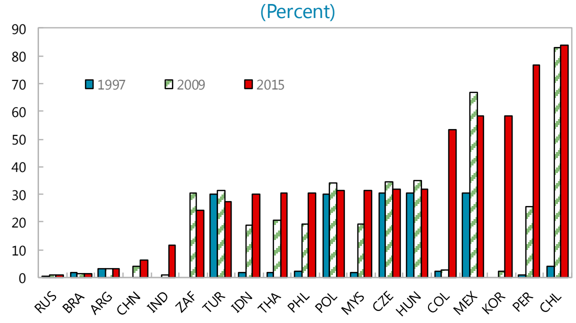


Source: Fund staff estimates.

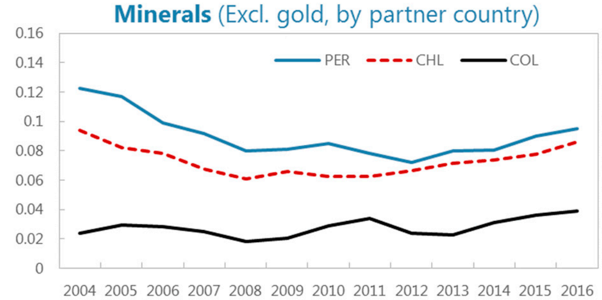
Starting from its non-mineral export base, Peru still holds enormous potential for diversification, and is well on the way to exploiting it. For instance, product diversification in the non-mineral export sector has increased significantly over time and is now similar to countries such as Chile, as measured by the Herfindahl-Hirschman concentration index. In terms of export destinations, Peru has preferential access through Regional Trade Agreements to countries representing close to 80 percent of world GDP, and has used such access to increase the average number of countries a given product reaches from 6.2 to 8 over the period 2004-2016. That said, Peru's exports remain geographically more concentrated than those of neighbors Chile and Colombia. Peru has significantly increased market share in U.S. and EU markets in fruits and vegetables, reflecting the success of the agricultural sector. This has helped to offset losses in market share in other sectors such as textiles. While growth in the agropecuarios sector bodes well for further diversifying Peru's non-mineral exports, such exports retain a significant 'resource' component.

Special Feature. Nontraditional Exports (concluded)

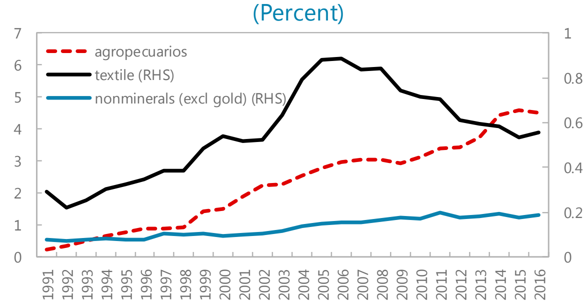
RTA partner countries share in global GDP
(Percent)



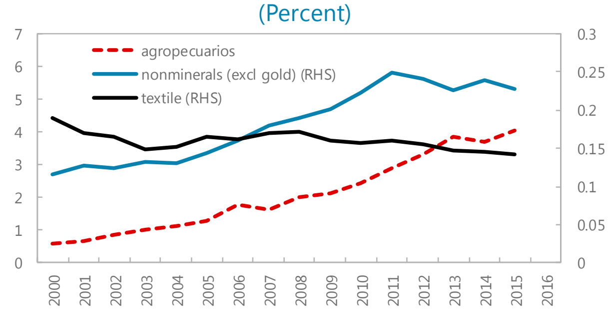
Concentration Index, Exports of Non-Minerals (Excl. gold, by partner country)



Market Share of Peruvian Exports in USA
(Percent)



Market Share of Peruvian Exports in EU28
(Percent)



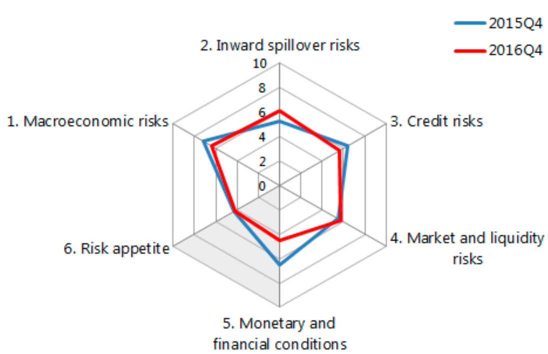
Sources: WTO, and Fund staff estimates.

Annex III. Macro-Financial Stability Update

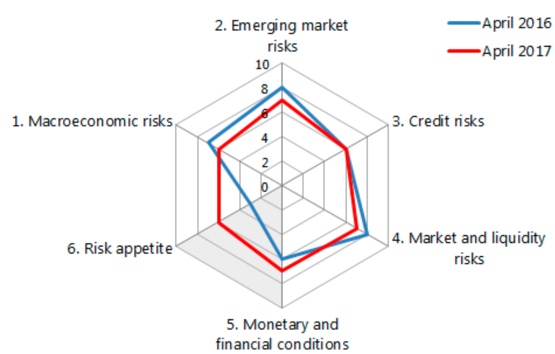
A. Overall Macro-Financial Stability

1. Macrofinancial stability risks in Peru are broadly stable. The main change from 2015 is that monetary and financial conditions have tightened, reflecting slower domestic credit growth. In contrast, global monetary and financial conditions remain accommodative, and risk appetite is buoyed by the stronger global economic backdrop.

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. Vulnerability risks appear to be contained. The financial system in Peru on the whole remains sound. Banks are well-capitalized (15 percent at end-2016), profitable (ROA: 2 percent) and with stable liquidity (total liquid assets to short-term liabilities: 35.4 percent). Non-performing loans have continued to rise slowly (3.1 percent at end-2016), and are expected to increase further following the floods, but are well-provisioned for (158 percent of total loans). The loan-to-deposit ratio is above one, mainly due to BCRP funding in the form of credit expansion repos (used in the dedollarization program to avoid a credit crunch). Some of the smaller non-banks are fragile due to scale problems and delinquencies. This reflects their portfolio composition, which mainly comprises of the SME and household sectors that are more sensitive to the economic cycle. Nevertheless, these do not constitute systemic risks.

Financial Soundness Indicator Map 1/

Peru	2014Q2	2014Q3	2014Q4	2015Q1	2015Q2	2015Q3	2015Q4	2016Q1	2016Q2	2016Q3	2016Q4	Latest
Overall Financial Sector Rating	M	M	M	M	M	M	M	M	M	M	M	M
Credit cycle	L	L	L	L	L	M	M	L	L	L	n.a.	L
Change in credit / GDP ratio (pp, annual)	2.0	1.4	1.6	2.7	2.9	3.6	3.0	1.3	0.4	-0.5	n.a.	-0.5
Growth of credit / GDP (%, annual)	6.4	4.4	4.9	8.3	8.8	10.9	8.9	3.7	1.0	-1.3	n.a.	-1.3
Credit-to-GDP gap (st. dev)	0.6	0.2	0.4	0.5	0.4	0.3	-0.6	-2.7	-2.7	-2.4	n.a.	-2.4
Balance Sheet Soundness	M	M	M	M	M	M	M	M	M	M	M	M
Balance Sheet Structural Risk	M	M	M	M	M	M	M	M	M	M	M	M
Deposit-to-loan ratio	94.9	91.6	89.6	89.4	88.3	89.4	91.6	90.9	88.2	88.8	88.1	88.1
FX liabilities % (of total liabilities)	49.4	49.6	48.4	48.8	48.5	49.5	49.2	48.2	46.9	45.5	44.7	44.7
FX loans % (of total loans)	39.9	39.7	38.2	36.4	33.7	31.2	30.1	28.6	28.5	29.4	28.7	28.7
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 (%)	10.3	10.4	10.7	9.9	10.1	9.9	10.1	9.9	10.6	10.9	11.4	11.4
Profitability	L	L	L	L	L	L	L	L	L	L	L	L
ROA	1.9	1.9	1.9	2.0	2.1	2.1	2.1	2.0	2.0	2.0	2.0	2.0
ROE	18.5	18.5	18.2	19.4	20.5	20.7	21.1	20.3	19.6	19.1	19.2	19.2
Asset quality	M	M	M	M	M	L	L	L	M	M	M	M
NPL ratio	3.8	3.9	4.0	4.0	4.1	4.0	3.9	4.1	4.3	4.4	4.3	4.3
NPL ratio change (%, annual)	8.0	10.6	12.9	8.9	7.9	1.9	-0.7	1.8	6.1	10.2	9.3	9.3

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

3. **Dollarization levels remain asymmetric between deposits (43 percent) and loans (28 percent), at end-February 2017.** Deposit dollarization has fallen to 43.3 percent at end-February 2017 (50.4 percent a year ago), while credit dollarization fell slightly to 28.3 percent (from 30.1 percent) in the same period.[1] The decline in deposit dollarization likely reflects lower expectations of depreciation and the change in composition of AFP deposits towards local currency deposits. The latter was probably in anticipation of the withdrawals related to the change in the pension law in 2016.[2] FX credit to corporates has started growing again (mainly trade credit), though the dedollarization targets in place have kept the credit dollarization ratio stable. Meanwhile, some of the repos used by the authorities in the credit dedollarization program in 2015 will mature in 2017 and 2018. The repos that have matured in early 2017 have not been rolled over, but the authorities are prepared to do so if there is demand.

4. **The financial cooperatives sector is rapidly growing and needs more effective supervision.** The rapid expansion of this sector needs to be carefully monitored, as several cooperatives have grown to be as big as the small banks in the system. Currently, supervision is under the National Federation of Savings and Credit Cooperatives in Peru (FENACREP), an umbrella body that is supervised by the SBS. The SBS is seeking to bring the larger cooperatives under its direct purview, which will help improve supervision and systemic risk identification.

[1] In general, the SBS estimates that the true FX exposure of the system is smaller (11.4 percent at end-2016), considering collateral and hedging.

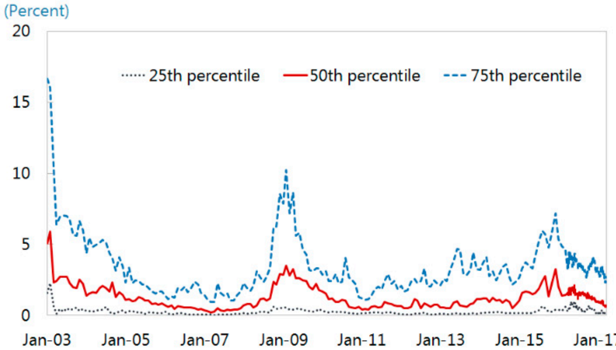
[2] The new laws allow pensioners over 65 years old to withdraw up to 95.5 percent from their accounts, and all affiliates to withdraw up to 25 percent for a down-payment or to amortize their mortgages for their first home purchase.

5. The change in the pensions law did not generate a large market disruption in the near-term, but could have longer-term implications. Private pension funds had shifted their portfolios towards more liquid assets in anticipation of withdrawals, but flow patterns have stabilized and inflows seem to sufficiently compensate for outflows. Nevertheless, the sustainability of the public system could be affected, as more people opt into the more flexible private system. The underdeveloped insurance sector is also impacted—insurance companies have received less premiums, affecting the annuity market.

C. Non-Financial Sector Risk Assessment

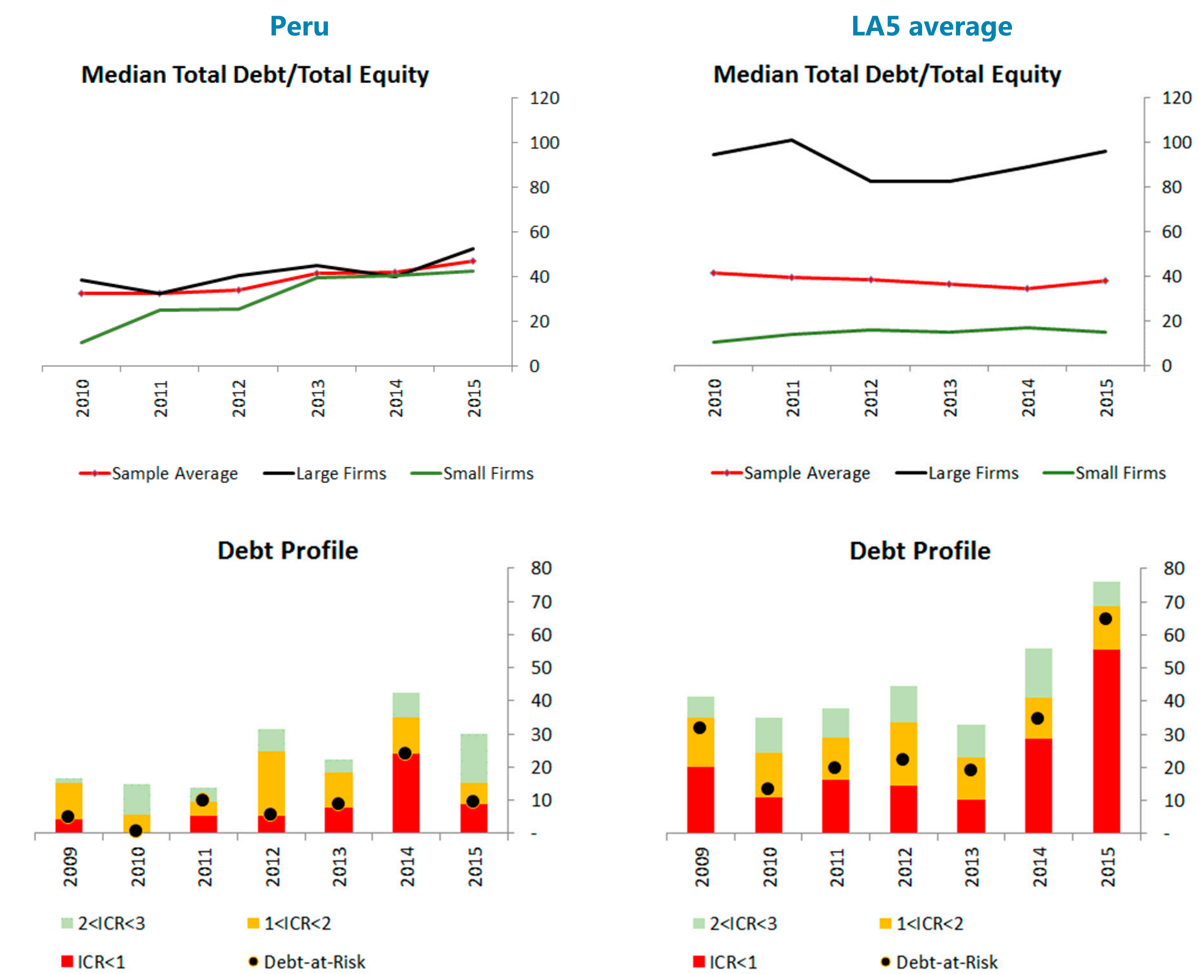
6. Corporate leverage has increased but debt riskiness has moderated. Based on a limited sample of 54 firms in Peru, corporate leverage increased in 2015, particularly for large firms. Despite the slight fall in median interest coverage ratio, debt-at-risk (defined as having interest coverage ratio below 1.5) and the percentage of firms-at-risk declined compared to 2014. The rise in leverage is consistent with the LA5 regional average, although the debt-at-risk in the region is much higher. A study done by the BCRP on a different sample of non-financial enterprises[3] showed that leverage ratios were stable in the first half of 2016 and below 1.5, with improved profitability indicators due to cost reductions. Furthermore, estimates of the one-year ahead probability of default for firms have trended downward in the past year.

Peruvian publicly listed firms, 1 year probability of default
(Percent)



Source: Moody's CreditEdge
Note: Sample of 58 publicly listed firms

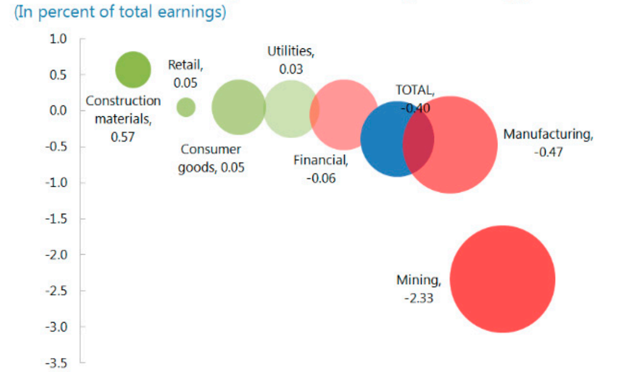
[3] A total of 99 enterprises were analyzed in this study—70 industrial, 16 mining and 13 utilities companies.



Source: Orbis, Staff calculations
Note: Firm sample based on data availability up to 2015. Size of firms determined by quartile of sample.

7. Exchange rate movements in 2016 resulted in slight FX losses (0.4 percent of total earnings). Overall, the ratio of FX assets to FX liabilities was 1.15. This masked a variation between sectors—those with larger FX assets relative to FX liabilities (mining and manufacturing) made FX losses, and vice versa for the other non-financial sectors. This reflects balance sheet effects only (rather than cash flow losses).

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



Source: Apoyo Consultoria, Staff calculations.
Note: Sample consists of firms publicly traded on the BVL. The size of the bubbles indicate the relative size of FX assets/FX liabilities for each sector. The financial sector has a ratio of 1.
[1/] The exchange rate appreciated by 1.5 percent in 2016 (year-on-year). Negative earnings indicate losses.

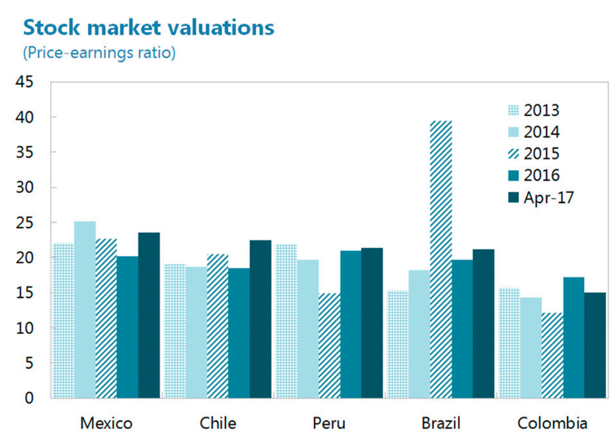
8. While dollarization of overall household credit has fallen, certain subcategories are still significantly dollarized and vulnerable to FX depreciation. Dollarization of household credit portfolios fell to 12.7 percent by end-February 2017 (December 2015:15.9 percent). While mortgages represent only 15 percent of total financial system credit, mortgage loans still reflect significant dollarization, at 21.4 in February 2017. This loan segment also has a higher NPL ratio in FX (3.8 percent in February 2017, compared to 2.0 percent in local currency). The estimated debt-to-income ratio is below 30 percent, though the range of uncertainty around household indebtedness statistics are large, as high informality affects the proper quantification of income sources.

D. Capital Markets

9. Companies have increasingly issued bonds in local currency and in the domestic market. In 2016 and the first few months of 2017, firms continued to show a preference for local currency bond issuance. Financial sector firms issued much more (with a growth of 217 percent over 2015) relative to non-financial firms (12 percent), and over 70 percent of total issuance was in soles. Issuance was relatively muted in the international market in 2016 compared to 2015 and 2014, with only three issuances for a total of USD$797 million.

10. The stock exchange, the Bolsa de Valores de Lima (BVL), kept its Emerging Market status in MSCI and recorded gains to become one of the highest-performing bourses in 2016. The general index rose by 58 percent compared to 2015, underpinned by higher commodity prices. The price-earnings ratio shows an increase from 2015, comparable to regional peers. In June 2016, the BVL successfully retained its status in the MSCI Emerging Market Index. The possibility of a downgrade to frontier status had accelerated several reforms on the stock market, including introducing algorithmic trading and incentives for market makers. While the size of the market remains small, liquidity indicators are showing an improvement. The Alternative Securities Market, targeted at SMEs, has seen limited issuance due to competition from banks in providing funding.

Stock Market Indicators



Source: Bloomberg

11. More can be done on financial integration to fully tap its benefits. Peru is part of the Latin American Integrated market, or *Mercado Integrado Latinoamericano* (MILA), together with the other Pacific Alliance (PA) countries of Chile, Colombia, and Mexico. However, activity has been minimal as intraregional trades are hampered by restrictions in individual countries, for example, pension funds investing in cross-border MILA securities are not treated as domestic investments. Removing these restrictions and harmonizing tax and operational procedures across the PA countries would help the market to tap the benefits from financial integration.

12. Capital market reforms are ongoing. The BVL is in the process of clarifying tax rules related to FIBRA (*Fideicomiso de Titulización en Renta de Bienes Inmuebles*), which are modelled after the Mexican Real Estate Investment Trusts (REITs). They are also considering secondary trading for the growing factor receivables market. The development of these new products will increase the diversity of investment vehicles in Peru, which will be helpful to the growth of the domestic capital market.

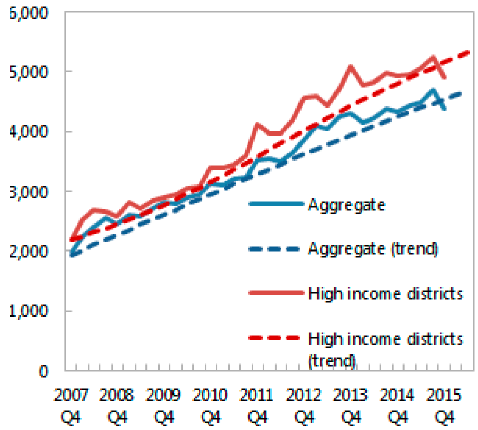
E. Housing Market

13. The property sector has grown rapidly, though there has been some price moderation recently and indicators do not suggest overheating. Prices have risen over the decade, in tandem with Peru's economic expansion. In Q2 2016, the growth in median apartment prices in Lima softened compared to Q2 2015, but remained well above the 5-year average. Valuation indicators show that Peru's property market is on an average footing compared to regional peers (figure). The country also faces a housing deficit, particularly in the lower-income segments, and buying patterns do not appear speculative. Furthermore, property price indices in Peru only reflect the capital, Lima, which has a higher population growth and urbanization level than the rest of the country.[4]

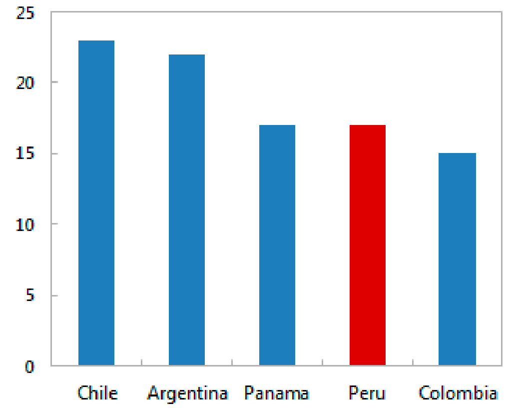
[4] The authorities collect information on property prices for other major cities in Peru, but these are not publicly available. IMF technical assistance is helping to expand this coverage nation-wide.

Housing Indicators

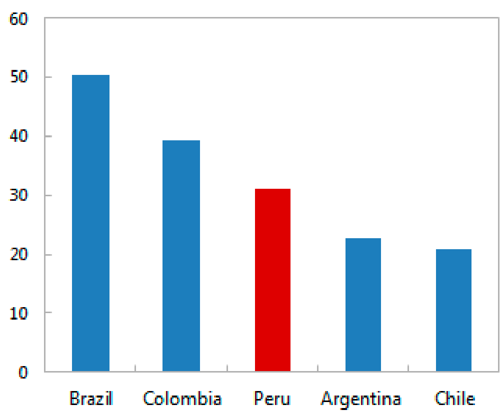
Median apartment prices in Lima
(2009 constant prices, in soles, per square meter)



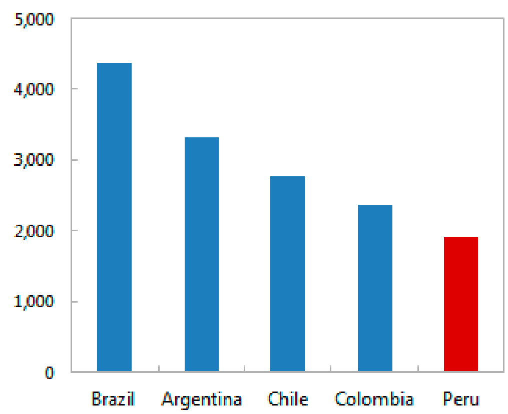
Price-to-rent ratio
(Years)



Price-to-GDP per capita
(Multiple)



Square meter prices, premier city center
(USD)



Source: Authorities, Global Property Guide, Fund staff calculations

Annex IV. Risk Assessment Matrix

Risk Assessment Matrix[1]

	Likelihood	*Impact*	*Policy Advice*[2]
		Country-specific risks	
Protracted period of weak domestic investment	M	M (↓) Investment could be affected by uncertainties stemming from external conditions, spillovers from the ongoing Odebrecht corruption investigation, and legacy of El Niño shock.	Persevere with structural reforms, especially those aimed at increasing investment potential and improving framework for PPPs. Strengthen anticorruption institutions and seek synergies between anticorruption and AML tools.
Slow implementation of reconstruction efforts	M	M (↓) Economic activity would be affected as key infrastructure has been damaged.	Improve coordination across line ministries (including through the new medium term budget framework) and provide support to local and regional governments to expedite the implementation of the capital expenditure budget.
		External risks	
Policy uncertainty and divergence. Two-sided risks to U.S. growth with difficult-to-predict policies and global spillovers. In Europe, uncertainty associated with negotiating post-Brexit arangements and with upcoming major elections.	H	M (↓) Peru's exports could be adversely affected and financial conditions would become tighter. This could occur also in an environment of higher public sector financing needs.	Exchange rate flexibility and use of fiscal buffers. Countercyclical monetary policy instruments could be used.
Significant further strengthening of the US dollar and/or higher interest rates	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. Countercyclical macroprudential instruments could be used.
Structurally weak growth in key advanced and emerging economies/Significant China slowdown and its spillovers	H/L	M/M (↓) Weaker global demand would lead to a worsening of 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. Use policy space (e.g., fiscal and/or monetary if inflation remains anchored) as a countercyclical measure if necessary). Accelerate structural reforms.

[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.

Annex V. Public Sector Debt Sustainability Analysis

Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators 1/

	Actual	Prel.		Projections					
	2011-2014 2/	2015	2016	2017	2018	2019	2020	2021	2022
Nominal gross public debt	21.6	24.0	24.4	25.2	26.4	27.0	26.8	26.3	25.7
Public gross financing needs	-0.1	3.1	3.8	5.6	4.5	3.9	3.1	1.9	1.6
Real GDP growth (in percent)	5.2	3.3	3.9	2.7	3.8	4.0	3.9	3.8	3.8
Inflation (GDP deflator, in percent)	3.3	3.5	3.6	3.1	2.6	2.5	2.4	2.3	2.3
Nominal GDP growth (in percent)	8.4	6.3	7.5	6.9	6.2	6.5	6.3	6.1	6.1
Effective interest rate (in percent) 4/	5.4	5.3	4.8	5.5	6.2	6.1	6.0	6.1	6.2

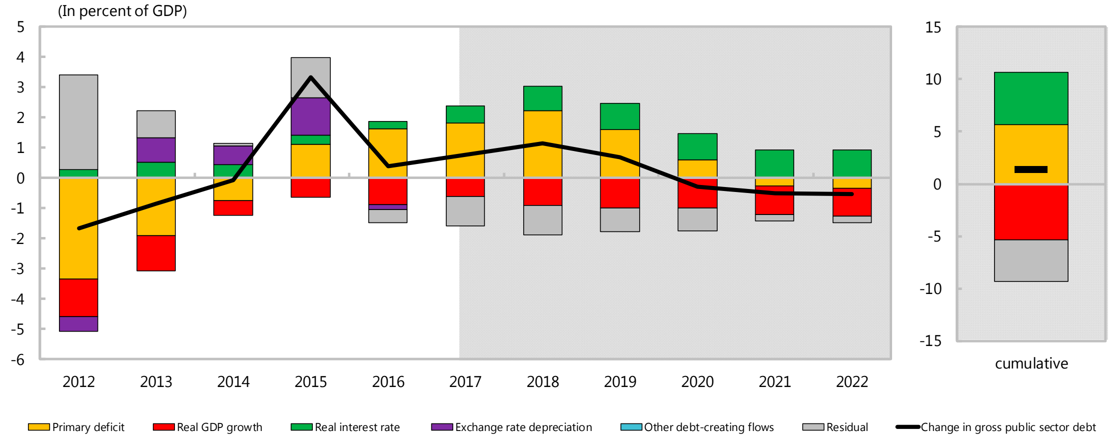
As of December 30, 2016		
Sovereign Spreads		
Spread (bp) 3/		175
CDS (bp)		108
Ratings	Foreign	Local
Moody's	A3 positive	A3 positive
S&Ps	BBB+ stable	A stable
Fitch	BBB+ Stable	A Stable

Contribution to Changes in Public Debt

	Actual	Prel.		Projections							
	2011-2014	2015	2016	2017	2018	2019	2020	2021	2022	cumulative	debt-stabilizing primary balance 9/
Change in gross public sector debt	-1.2	3.3	0.4	0.8	1.2	0.7	-0.3	-0.5	-0.5	1.3	
Identified debt-creating flows	-2.9	2.0	0.8	1.8	2.2	1.5	0.5	-0.3	-0.3	5.4	
Primary deficit	-2.3	1.1	1.6	1.8	2.2	1.6	0.6	-0.3	-0.3	5.7	0.0
Primary (noninterest) revenue and grants	27.9	24.9	23.1	23.0	23.1	23.3	23.5	23.8	23.7	140.3	
Primary (noninterest) expenditure	25.6	26.0	24.7	24.8	25.3	24.9	24.1	23.5	23.3	145.9	
Automatic debt dynamics 5/	-0.6	0.9	-0.8	0.0	0.0	-0.1	-0.1	0.0	0.0	-0.2	
Interest rate/growth differential 6/	-0.7	-0.4	-0.6	-0.1	-0.1	-0.1	-0.1	0.0	0.0	-0.4	
Of which: real interest rate	0.4	0.3	0.2	0.5	0.8	0.9	0.9	0.9	0.9	5.0	
Of which: real GDP growth	-1.1	-0.6	-0.9	-0.6	-0.9	-1.0	-1.0	-1.0	-0.9	-5.4	
Exchange rate depreciation 7/	0.1	1.3	-0.2	...	...	...	...	...	...	...	
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/	1.7	1.3	-0.4	-1.0	-1.0	-0.8	-0.8	-0.2	-0.2	-4.0	

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).

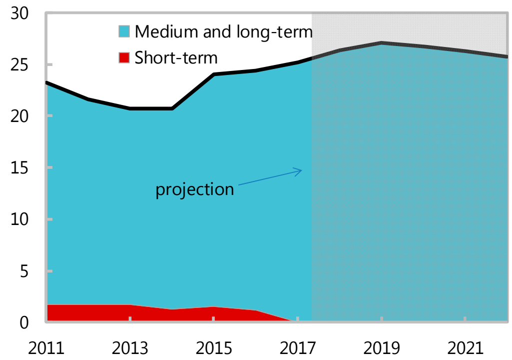
8/ For projections, this line includes exchange rate changes during the projection period.

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.

Public DSA—Composition of Public Debt and Alternative Scenarios

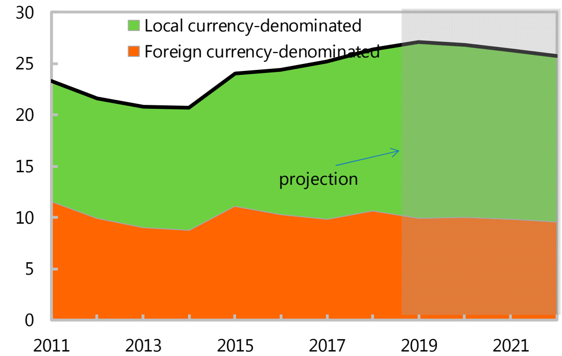
By Maturity

(In percent of GDP)



By Currency

(In percent of GDP)

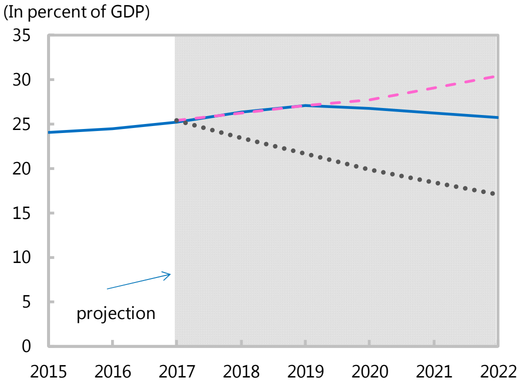


Alternative Scenarios

Baseline   Historical   Constant Primary Balance

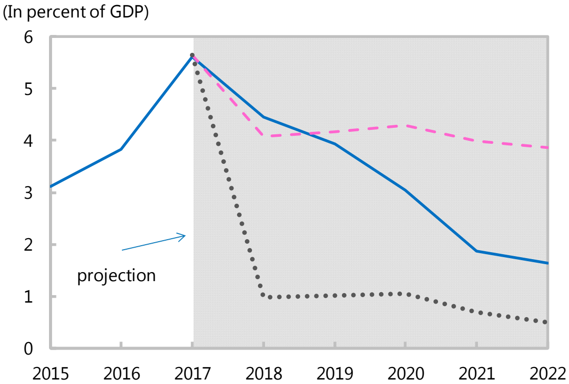
Gross Nominal Public Debt

(In percent of GDP)



Public Gross Financing Needs

(In percent of GDP)



Underlying Assumptions

(In percent)

Baseline Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	2.7	3.8	4.0	3.9	3.8	3.8
Inflation	3.1	2.6	2.5	2.4	2.3	2.3
Primary Balance 1/	-1.8	-2.2	-1.6	-0.6	0.3	0.3
Effective interest rate	5.5	6.2	6.1	6.0	6.1	6.2
Constant Primary Balance Scenario						
Real GDP growth	2.7	3.8	4.0	3.9	3.8	3.8
Inflation	3.1	2.6	2.5	2.4	2.3	2.3
Primary Balance	-1.8	-1.8	-1.8	-1.8	-1.8	-1.8
Effective interest rate	5.5	6.2	6.1	6.0	6.0	5.8

Historical Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	2.7	5.5	5.5	5.5	5.5	5.5
Inflation	3.1	2.6	2.5	2.4	2.3	2.3
Primary Balance	-1.8	1.2	1.2	1.2	1.2	1.2
Effective interest rate	5.5	6.2	6.6	6.9	7.4	7.8

Source: Fund staff estimates.

1/ Excludes interest income.

Annex VI. Road Ahead for PPPs

1. **Peru's PPP framework stacks up relatively well compared to peer group countries, although there is room for improvement.** The World Bank report on *Benchmarking Public-Private Partnerships Procurement, 2017*—which evaluated the framework in place at March 2016—assigns high marks to Peru's framework, particularly regarding PPP preparation, processes for unsolicited proposals, and contract management. The largest room for improvement relates to the procurement/tendering process itself, notably in terms of: strengthening the evaluation committee, expanding the scope for dialogue with bidders, dealing with sole proposals, and use of exceptions or fast-track regimes. Similarly, the 2017 Infrascope—*Evaluating the environment for public-private partnerships in Latin America and the Caribbean*—prepared by the Economist Intelligence Unit and the Inter-American Development Bank assesses Peru's environment as developed (the highest category), and ranks it fifth among 19 countries. The main areas for improvement highlighted in the report include: coordination and clarity of jurisdictions and competencies among relevant agencies, renegotiation processes and bureaucratic delays, standardization of contracts, prioritization, industry concentration, and support to regional and local governments.

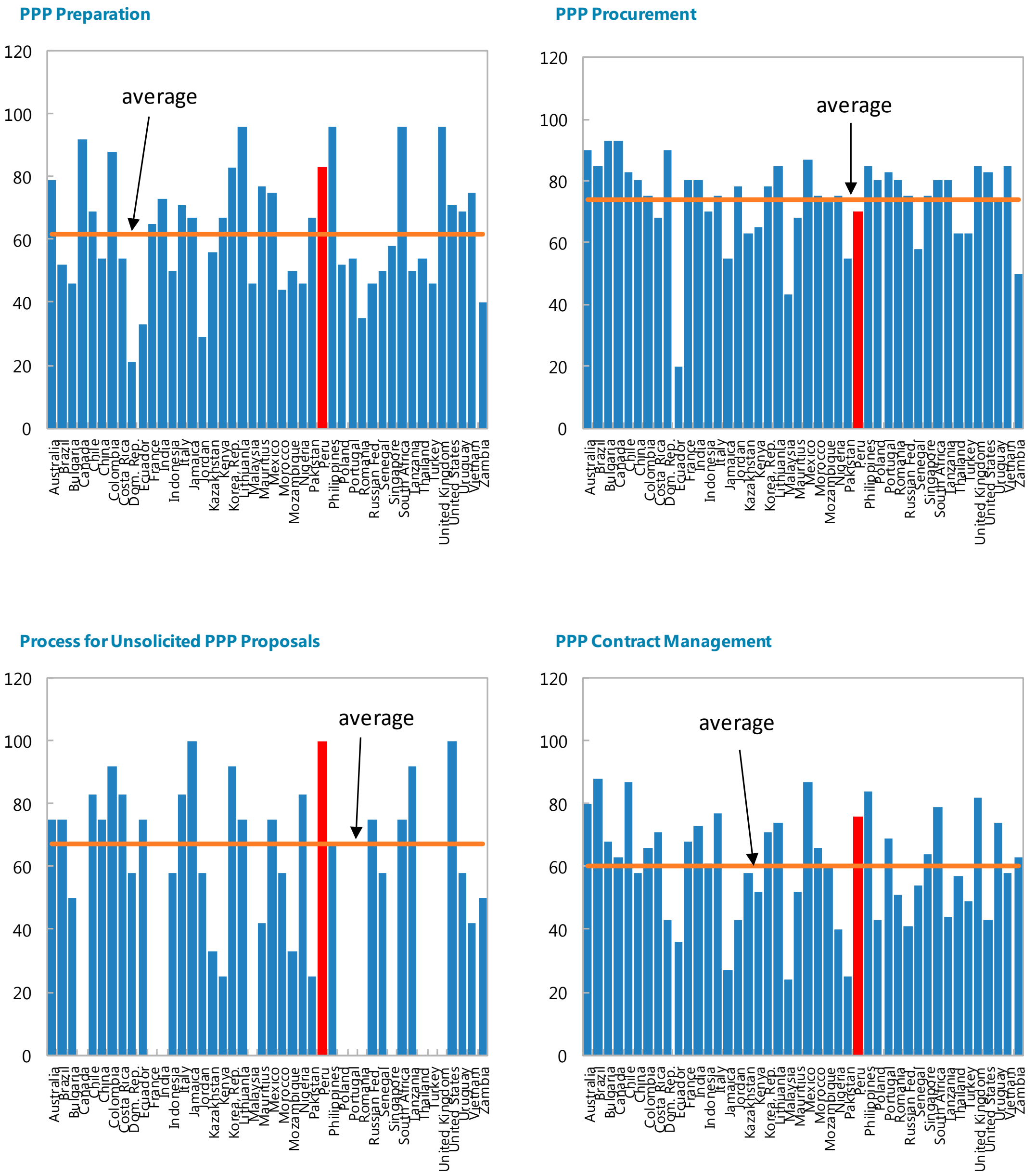
2. **The new government has issued a set of reforms to try to make the PPP framework more agile, transparent, and efficient.** The strategy is based on two main pillars:

- *The optimization of the role of the investment promotion agency, Proinversion*, aimed at increasing its autonomy, strengthening transparency and accountability, and expanding its supporting role to regional and local governments.

- *Making investment promotion more efficient and agile*, with emphasis on simplifying bureaucratic procedures, and improving project and contract designand proposal assessments. The new government expects to achieve meaningful efficiency gains in this area, since it perceives that the previous framework/practice resulted in numerous renegotiations. For instance, out of 30 PPP projects awarded by Proinversion during 2012–15, there was a total of 157 contract versions, or an average of 5.2 version per project contract. Further improvement should focus on risk reporting, mitigation, and management.

3. **Given the expansion of investment that is envisaged for the coming years, it will be important for the government to maintain a clear assessment of risks related to PPPs.** Furthermore, it would be important to strengthen the gateway role of the Ministry of Economy and Finance (through the General Directorate for Promotion of Public Investment, DGPIP) during all the stages of the PPP process. In this context, it will be crucial that the new separation of functions between Proinversion and the Ministry of Economy and Finance does not result in a weakening of the capacity of the latter to monitor and control risks.

Benchmarking PPPs
(ranking 0-100)



Source:World Bank (Benchmarking Public-Private Partnerships Procurement, 2017)

INTERNATIONAL MONETARY FUND

PERU

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

June 1, 2017

Prepared By

The Western Hemisphere Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of April 30, 2017)

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	531.15	87.09

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				
	2017	2018	2019	2020	2021
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.26	0.39	0.39	0.39	0.39
Total	0.26	0.39	0.39	0.39	0.39

[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 29, 2016, the average of interbank buying and selling rates was 3.35 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 2016 Article IV consultation was concluded on June 20, 2016 (IMF Country Report No. 16/234).

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

Department	**Purpose**
FAD	Medium Term Budgeting
	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
STA	Housing Price Indexes
	Monetary and Financial Sector Statistics

WORLD BANK RELATIONS

(As of May 2, 2017)

A. Bank Group Strategy

The World Bank Group support to Peru is defined in the FY17–FY21 Country Partnership Framework (CPF) discussed by the Board on May 2, 2017. The Peru CPF is fully aligned with the goals of Government of Peru National Plan for 2016–2021. It was developed in consultation with the Peruvian authorities and a wide range of key stakeholders at the national and local levels and builds on the lessons-learned from the previous CPS and its evaluation. The CPF is structured across three pillars: (i) Productivity for growth; (ii) Services for citizens across the territory; and (iii) Natural resource and climate risk management. Since the common challenge in these three pillars is implementation, effectiveness of public action and spending will be a crosscutting issue. Gender and indigenous disparities will be streamlined into all interventions to the extent possible.

The CPF's five-year implementation period (FY17–FY21) is fully aligned with Peru's political cycle. The WBG will work in close coordination to deliver an integrated package of financial products, guarantees and knowledge services based on relative comparative advantages and the strengths of the WBG's programs in Peru. The CPF builds on this engagement and focuses increasingly on the institutional challenges Peru faces, while highlighting the opportunity to crowd-in private sector investment and sharing Peru's globally recognized successes.

The WB portfolio includes 15 investment projects and a GEF grant totaling US$960 million. In addition, Peru has access to four contingent lines of credit for US$3 billion, including two DPF–DDOs and two Catastrophe Deferred Drawdown Option (CAT–DDO). The indicative WB financing for FY17–FY18 is around US$500 million (which will be focused exclusively towards IPF projects). WB lending volumes over the FY19–FY21 period are tentative at this stage and will depend on country demand and overall progress in the course of the CPF period.

B. Bank-Fund Collaboration in Specific Areas

OECD. Peru has formally declared its intention to join the OECD by 2021. The WBG has provided advisory support to the OECD engagement. Accompanying the OECD Country Program, the WB delivered a strategy on OECD engagement and provided support in the adoption of OECD instruments, standards or action plans for reform. In particular, technical input to improve statistics, environmental standards, integrity in the public sector, international taxation and innovation.

Public Private Partnerships to infrastructure. The WB will continue working in a closely coordinated manner in two areas to: (i) help strengthen the institutional framework to distribute risks and returns so that new investment does not impose excessive fiscal pressures (while strongly safeguarding environmental and social standards); and (ii) support the development of the domestic capital markets to lengthen maturities and reduce costs by expanding the number of domestic and international capital market and commercial financing available for the country. Public Expenditure DPF-DDO and technical assistance will be used to continue providing support, which might be aided with guarantee instruments to help private players manage risks that are devolved to them.

Development of the capital markets in Peru. The WB ongoing program will continue supporting the development of capital markets and infrastructure finance through the National Development Bank (Corporación Financiera de Desarrollo, COFIDE).

Peru: World Bank Portfolio Status

As of April 30, 2017

(In millions of U.S. dollars)

Active Projects

			Original Amount in US$ Millions					Difference Expected and Actual Disbursements a/	
Project ID	Project Name	Fiscal Year	IBRD	IDA	Grants	Cancel.	Undisb.	Orig.	Frm Rev'd
P156250	Peru Innovation	2017	45	-	0.0	0.0	45.0	0.3	0.0
P147342	PE Enhancement of Env. Quality Services	2017	40	-	0.0	0.0	40.0	0.0	0.0
P155902	PE Fisheries and Aquaculture Innovation	2017	40	-	0.0	0.0	40.0	0.1	0.0
P156858	PE Boost. Hum. Cap. and Productivity DPL	2016	1,250	-	0.0	0.0	1,250.0	0.0	0.0
P154981	Pub. Exp. and Fiscal Risk Mgmt DPL-DDO	2016	1,250	-	0.0	0.0	1,250.0	0.0	0.0
P145610	PE Lima Metro Line 2 Project	2016	300	-	0.0	0.0	260.0	97.5	0.0
P132515	PE Support to the Subnational Transport	2016	50	-	0.0	0.0	50.0	8.8	0.0
P149831	PE CAT DDO II	2015	400	-	0.0	0.0	400.0	0.0	0.0
P132505	PE Cuzco Transport Improvement	2014	120	-	0.0	0.0	118.6	28.6	12.7
P131013	PE National Ag. Innovation Program	2014	40	-	0.0	0.0	34.2	12.2	0.0
P117318	PE Cuzco Regional Development	2014	35	-	0.0	0.0	34.0	29.0	20.6
P123151	PE Basic Education *	2013	25	-	0.0	0.0	8.3	0.7	1.5
P122194	PE HIGHER EDUCATION QUALITY IMPROVEMENT *	2013	25	-	0.0	0.0	12.1	7.3	5.6
P131029	PE Social Inclusion TAL *	2013	10	-	0.0	0.0	1.3	1.3	0.0
P117293	PE Optimization of Lima Wat & Sewerage	2011	109.5	-	0.0	0.0	56.3	-53.2	33.3
P120860	PERU CAT DDO	2011	100	-	0.0	0.0	100.0	0.0	0.0
P117864	PE Second Rural Electrification *	2011	50	-	0.0	0.0	5.7	0.0	1.1
P117310	PE Results Nutrition for Juntos SWAp *	2011	25	-	0.0	0.0	1.7	1.7	0.0
P079165	PE Sierra Rural Development Project *	2007	40	-	0.0	0.2	0.0	-19.8	0.0
P129647	PE (GEF) Strengthening Sust Mgmt Guano Islands	2014	0	-	8.9	0.0	4.9	1.3	0.0
Overall Result			**3,954.5**	**0.0**	**8.9**	**0.2**	**3,712.1**	**115.7**	**75.0**

International Financial Corporation Portfolio

As of April 30, 2017

(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

(As of April 30, 2017)

A. Country Strategy

The new Country Strategy with Peru covers the period 2017–2021. The strategy intends to work on three main areas: (i) productivity, with an emphasis on the labor market, business climate, business development, and infrastructure; (ii) institutional strengthening and basic service delivery, with an emphasis on public management, health, and citizen security; and (ii) environmental sustainability and climate change, with an emphasis on water resources, environmental management, and agribusiness. The proposed actions are aligned with the Peruvian government plan, which prioritizes (i) boosting and formalizing the economy; (ii) strengthening public management; (iii) improving the delivery of services to the population; and (iv) reinforcing environmental management.

The Country Strategy was approved by the Board of Directors on May 2017. 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. An approval scenario of US$1,500 million is estimated. Disbursements with sovereign guarantee are estimated at US$1,250 million.

B. Lending

As of April 2017, the Bank's portfolio of active, public sector operations consisted of 22 loans for a total amount of US$1,266 million, including one policy-based loans with a deferred disbursement modality for a total amount of US$300 million. The rest of the active portfolio consists of 21 loans for an amount of US$966 million, of which US$347.6 million (27 percent) have been disbursed. The public sector lending program for 2016 comprised two operations for a total of US$120 million. The public sector lending program for 2017 comprises seven investment loans for a total amount of US$400 million.

Regarding private sector lending, as of March 2017 the Inter-American Investment Corporation (IIC), member of the IDB Group, has an active portfolio of 23 operations for a total approved amount of US$904.9 million and a total net exposure of US$621.18 million. The IIC's active portfolio exposure is distributed in the following sectors: Oil and Gas, 44 percent; Energy, 25 percent; Financial Intermediaries, 19 percent; Agribusiness, 6 percent; Education, 5 percent; and others, 1 percent.

Peru: IDB Sovereign Guaranteed Loan Portfolio by Sector
As of April, 2017
(In millions of U.S. dollars)

Sector	Commitments	Disbursements	% Disbursed
Agriculture	95.0	4.2	4
Science, Technology and Competitiveness	75	26.4	35
Social Investment	355.0	22.0	6
Modernization of the State	102.5	75.2	73
Integration and Trade	20	0	0
Water and Sanitation	115.0	55.2	48
Transportation	503.9	164.5	33
Total	1,266.6	347.5	27

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 and the base year for the calculation of the weights is 2013.

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, and INEI is now publishing a broader regional coverage of the labor market statistics based on the Encuesta Nacional de Hogares (ENAHO). It would be useful to 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 for revenues and on accrual basis for expenditures, 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 published in the International Financial Statistics (IFS), but is available from the weekly report of the BCRP.

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. After the completion of the two technical assistant missions the BCRP sent a first version of the SRFs in October 2016. The IMF is reviewing them prior to publication and a follow up technical assistance mission is scheduled in 2017.

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 April 30, 2017)

	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	04/27/17	04/28/17	D	M	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	02/28/17	03/31/17	D	M	W		
Reserve/Base Money	02/28/17	03/31/17	W	M	W		
Broad Money	02/28/17	03/31/17	W	M	W		
Central Bank Balance Sheet	02/28/17	03/31/17	W	M	W		
Consolidated Balance Sheet of the Banking System	02/28/17	03/31/17	W	M	W	O, LO, LO, LO	O, O, O, O, O
Interest Rates[2]	02/28/17	03/31/17	D	M	D		
Consumer Price Index	02/28/17	03/31/17	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 2016	03/17/17	Q	Q	Q	O, LO, O, O	O, O, O, LO, O
Stocks of CG Debt[5]	Q4 2016	03/17/17	Q	Q	Q		
International Investment Position[6]	Q4 2016	03/17/17	Q	Q	Q		
External Current Account Balance	Q4 2016	03/17/17	Q	Q	Q	O, LO, LO, LO	LO, LO, O, O, O
Exports and Imports of Goods and Services	M2 2017	04/30/17	M	M	M		
GDP/GNP	Q4 2016	03/17/17	Q	Q	Q	LO, LO, LO, LO	LNO, LNO, LNO, LO, LO
Gross External Debt	Q4 2016	03/17/17	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.