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Fonds: Records of the Office of the President

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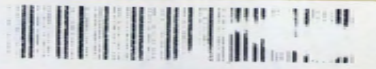
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McNamara Papers

Travel
Notes

The World Bank Group
Archives



1772736

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South America (Paraguay, Peru, Bolivia) - Travel Briefs, Peru

Folder 3 of 3

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WBG Archives

VISIT TO SOUTH AMERICA, March 2-12, 1976

<u>DATE</u>	<u>TIME</u>	<u>GMT</u>		<u>REMARKS</u>
Mar. 2	1630	2130	Depart Washington (National)	NAL01 (727) nonstop coach
Tues.	1845	2345	Arrive Miami	Airport Hotel (double room)
Mar. 3	0115	0615	Depart Miami	Aeroperu 601 (DC8) nonstop
Wed.	0650	1150	Arrive Lima	first
	0800		Rest in hotel	Sheraton Lima (small suite)
	1100		Meeting with Finance Minister, President of Central Bank, and President of COFIDE	
	1300		Lunch hosted by President Central Bank	
	1500		Meeting with COFIDE, Chief of Planning Office, and Presidents of selected public enterprises	
	1700		Meeting with Prime Minister	
	19:30	19:30	Courtesy visit to Minister Foreign Affairs	
	2000		Reception hosted by Finance Minister (with wives)	
Mar. 4				7:15 Departure to La Molina - Fubertus Inusual Potato Center
Thurs.	0900		Meeting with Minister of Housing and field visit to site of proposed "Sites and Services project" in Lima area (Villa El Salvador)	
	1330		Private meeting with President of Republic	
	1400		Working lunch with President, Ministers of Agriculture, Food, Industry, Energy & Mines, Transport, and Planning	
<u>Following meetings will take place at the hotel</u>				
	1630		UNDP ResRep	
	1700		Mr. Keller, President of ADELA until recent retirement	
	1730		Mr. L. Paredes, President of Peruvian Institute for Business Administration (IPAE); Mr. P. Reyser, Industrialist and President of ENTURPERU; Mr. G. Lanatta, Industrialist; and Mr. A. Villalobos, President of Chamber of Commerce	
	1800		Mr. C. Mariotti, Industrialist and former President of Empresas Electrical (Lima Power Company)	
	1830		Mr. E. Jaworski, Director of "El Comercio" (daily newspaper); Mr. L. Chiappo, Editor of "El Expreso" (weekly magazine); and Mr. J. Matos Mar, Director of Institute for Political Studies	Torreguier
	1900		Mr. N. Asheshov, Editor of "The Andean Report"	Michelle Prond.
	2000		Informal dinner by COFIDE (with wives)	
Mar. 5				by special plane
Fri.	0790		Depart to Trujillo	
	0820		Arrival in Trujillo and visit to Sugar Cooperative "Casagrande"	
	1100		Depart for Tarapoto	
	1300		Arrive in Tarapoto	
	1315		Lunch at Hotel De Turistas with explanation on development program of Huallaga Region	
	1430		Visit Huallaga and Alto Mayo areas, where new developments in agriculture have taken place and more are being planned	
	1600		Depart for Lima	
	1730		Arrival in Lima	

<u>DATE</u>	<u>TIME</u>	<u>GMT</u>		<u>REMARKS</u>
Mar. 6	⁰⁶¹⁵ 0730	1230	Depart for Cuzco	Aeroperu arranged by COFIDE
Sat.	0830	1330	Arrive Cuzco	
	1000		Depart for Machu Picchu	Special autowagon
	1230		Visit to Machu Picchu and lunch	
	1700		Return to Cuzco	Autowagon
Mar. 7	0900		Visit Cuzco and its surroundings	
Sun.	1200	1700	Depart for La Paz	Special plane
	1415	1815	Arrive La Paz	Hotel La Paz (small suite)
	1500--1800		Tour of city	
	2000		Small informal "get acquainted" dinner by Finance Minister, Carlos Calvo, at his home. About nine couples will be present plus six Bank participants	
Mar. 8				
Mon.	0800--1000		Meeting with Economic Group at Presidential Palace to be attended by: Minister of Finance, Carlos Calvo Minister Planning & Coordination, Lechin Presidential Advisor, Violand Undersecretary of Planning, Valdes Executive Director of External Financing Institute, Ormachea	
	1010--1030		Meeting with President Banzer	at Presidential Palace
	1035--1310		Visit by car to Ingavi Rural Development project (at Jalsuri)	
	1315--1340		Signing (in Jalsuri) of Loan Agreement for Ingavi Rural Development Project by Mr. McNamara and President Banzer and Minister of Finance Carlos Calvo on behalf of Government	
	1345--1540		Lunch at Jalsuri with President Banzer	
	1755		Arrive at Hotel Evening free	
Mar. 9				
Tues.	0800--0930		Meeting with top representatives from private sector (banking, mining and industry)	
	0935--1000		Briefing about urban development of La Paz	
	1005--1200		Tour of urban development sites in La Paz	by car
	1250 1650		Depart for Santa Cruz with President Banzer	Govt. plane (lunch served)
	1425 1825		Arrive Santa Cruz	Holiday Inn or Govt. accommodation
	1425--1445		Introduction to welcoming party of local leaders	
	1455--1800		Tour to see agricultural areas in Santa Cruz, with briefing by President Banzer Evening free	by helicopter
Mar. 10				
Wed.	0540	0940	Depart for Asuncion	Govt. plane
	0800	1100	Arrive President Stroessner Airport	Hotel Ita Enramada
	0900		Meeting with President Stroessner	
	1000		Visit rural and eastern areas of Paraguay (area of Small Farmer Credit and Rural Development Project)	by plane to Coronel Oviedo by car to Caaguazu
	1400		Trip to Itapua Department (southeastern Paraguay). Flyover Parana River and sites of future hydroelectric schemes. Lunch during flight. Visit cooperatives at Hohenau, Obligado, Capitan Meza, etc.	

1536
begin
arrives

<u>DATE</u>	<u>TIME</u>	<u>GMT</u>		<u>REMARKS</u>
	1800		Return to Asuncion	by plane
	2000		Cocktail party hosted by Finance Minister, General Cesar Barrientos--guests will include other Ministers and some prominent members of private sector	Club Centenario
Mar. 11				
Thurs.	0700		Meeting with economic team	
	1000		Field trip to El Chaco, Western Paraguay visit to Mennonite colonies and cooperatives of Loma Plata and Filadelfia	Presidential plane
	1500		Depart for Asuncion	Presidential plane
	1630		Arrive Asuncion	
	1700--1800		Open (after visitors have had chance to see the country, President Stroessner usually likes to have wrap-up meeting to exchange ideas on policies and programs that will improve their development efforts)	
	2115	0015	Depart Asuncion	Braniff 974 (D8S) one stop
	2345	0445	Arrive Lima	(La Paz) coach
Mar. 12				
Fri.	0110	0610	Depart Lima	Braniff 978 (DC8) nonstop
	0830	1330	Arrive Washington (Dulles)	(coach)

SB
March 1, 1976

11/11/1961
HIRATA BINGHAM

1 "The last of city of the
Fishes"

2 "The Wondeland of Kulu" ✓
National Geographic Society

B. Print out whom Kulu
has already met, by at
AM

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Kelley
Rudolf

Data Book

1. Macro-economic relationships
2. Fiscal - data
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DATE	TIME	LOCATION	DESCRIPTION
11/11/61	0830	1330	VALTAS DEPARTMENT (DOTTEN)
11/11/61	0710	0810	DEBELL TIME
11/11/61	0842	0942	VALTAS TIME
11/11/61	0912	1012	DEBELL VALMOTON
11/11/61	1100-1200		DEBELL VALMOTON
11/11/61	1200		DEBELL VALMOTON
11/11/61	1400		DEBELL VALMOTON
11/11/61	1500		DEBELL VALMOTON
11/11/61	1600		DEBELL VALMOTON
11/11/61	1800		DEBELL VALMOTON

PERU



COUNTRY BRIEFING

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A

SP

PROGRAMA DE ATENCIONES A LA SEÑORA MCNAMARA

Acompañantes: Sra. Hortensia de Barúa, esposa del Ministro de Economía y Finanzas
Sra. María Cecilia Barúa, hija del Ministro de Economía y Finanzas
Sra. Leonor de Santistevan, esposa del Presidente del Bco. Central Reserva
Sra. Eloísa de Espinosa, esposa del Presidente de COFIDE
Sra. Elsa de Salaverry, esposa del Director General Asuntos Financieros
Sra. Amalia de Keil, esposa del Director Superior del MEF
Sra. Cecilia de van Oordt, esposa del Gerente General de COFIDE
Sra. Lupe Valdivieso, secretaria del Presidente de COFIDE

Miércoles 3 de marzo

15.30 horas Visita al Museo Nacional de Antropología y Arqueología
20.00 horas Recepción que ofrece el señor Ministro de Economía y Finanzas y señora de Barúa Castañeda en la Casa de Goyeneche

Jueves 4 de marzo

09.00 horas Visita a los alrededores de Lima
11.00 horas Visita al Museo de Amano
Visita a las Ruinas de Puruchuco
13.00 horas Almuerzo en la Granja Azul Inn ("El Pueblo")
16.00 horas Visita al Museo de Oro
20.00 horas Comida ofrecida por el Presidente de COFIDE y señora de Espinosa

Viernes 5 de marzo

En la mañana-Día para compras
11.00 horas Visita a las Ruinas de Pachacamac
13.30 horas Almuerzo en el Santa María Beach Club

Sábado 6 de marzo

07.30 horas Viaje a la ciudad de Cuzco
Visita a las Ruinas de Machu Picchu

Domingo 7 de marzo

09.00 horas Visita turística a la ciudad del Cuzco
12.00 horas Salida en avión especial a la ciudad de La Paz, Bolivia

B

MR. McNAMARA'S VISIT TO PERU:

STATEMENT AT THE AIRPORT

	(US\$ million)	IDB
	IBRD/IDA	
64-68	109.1	123.7
69-72	30.0	99.3
74-78	459.5	286.1
74	7.5	46.3
75	-	31.5
76	192.5	122.3
77	90.0	80.0

I am very glad that this, my seventh visit to Latin America, should begin in Peru. I have long wished to visit your exciting country with which the Bank has a long record of cooperation and understanding. The most recent expression of this relationship has been the approval two months ago of a \$76.5 million loan to help finance the Lima-Pucallpa road, and the construction and expansion of river ports in the jungle; and the approval yesterday of a new \$36 million loan to help finance a fifth power project, which includes the expansion of transmission and distribution systems of the Lima Metropolitan Area.

During my stay in Peru, I will be able to gain first-hand knowledge of the profound and impressive structural changes to the economy initiated by the Revolutionary Government of the Armed Forces. I will also be able to learn more of the problems facing Peru in its progress toward economic development. I am particularly interested to learn about the Peruvian approach to reducing urban poverty, as well as your efforts to promote an active participation of the rural population in development. In these areas I believe that the exchange of ideas and experiences will be fruitful for both of us.

The Peruvian Government and the staff of the World Bank have always worked together constructively. I am sure that this will continue. But the Bank can only assist. The burden of achieving a balanced development of the country rests with the Peruvian Government and people. We are proud to play a part in your efforts to exploit Peru's abundant natural resources and to expand the participation of all Peruvians in the fruits of development.

IDB loans approved during last 6 months:
Banco Industrial (DFC) \$15 million
Olmos-Corral Quemado (Road) \$37.6 million

DISCURSO EN EL AEROPUERTO

Me complace mucho comenzar en el Perú esta mi séptima visita a América Latina. Desde hace mucho tiempo tenía deseos de visitar vuestro interesante país, con el cual el Banco Mundial tiene una larga trayectoria de cooperación y común entendimiento que ha resultado en beneficios mutuos y de la que el Banco está muy satisfecho. Las manifestaciones más recientes de esa estrecha relación han sido la aprobación hace dos meses de un préstamo de 76.5 millones de dólares para ayudar al financiamiento de la carretera de Lima a Pucallpa y la construcción y ampliación de puertos fluviales en la Selva, y la aprobación ayer mismo de un nuevo préstamo de 36 millones de dólares para cooperar en el financiamiento de un quinto proyecto de energía eléctrica predominantemente para la expansión del sistema de distribución y transmisión eléctrica del area metropolitana de Lima.

Durante mi estancia en el país tendré la oportunidad de conocer directamente los profundos e impresionantes cambios estructurales que ha iniciado el Gobierno Revolucionario de la Fuerza Armada, así como los problemas que se presentan en el camino del desarrollo económico del Perú y el progreso que se está logrando en la solución de tales problemas. Estoy particularmente interesado en conocer el enfoque peruano para atacar el problema de la pobreza urbana, así como el problema de la participación activa del elemento rural en el proceso de desarrollo. En ambos campos creo que el

intercambiar ideas y experiencias será fructífero para ambas partes y facilitará la cooperación del Banco en nuestro objetivo común que es el del desarrollo económico y social del país.

Las autoridades peruanas y el personal del Banco han cooperado siempre en un clima de armonía y buena disposición y tengo la seguridad de que seguirá sucediendo así en el futuro. Sin embargo el peso del esfuerzo para lograr un desarrollo equilibrado y la esperanza de su logro están enteramente sobre los hombros del pueblo y el el Gobierno peruano. Estamos orgullosos de poder prestar nuestro estusiasta apoyo a tales esfuerzos encaminados a una explotación racional de los abundantes recursos naturales del país y a una mayor participación de todos los peruanos en los frutos del desarrollo.

C

background NOTES

DEC 18 TH 2:50

Peru¹⁰⁰

department of state * february 1975

1/78



OFFICIAL NAME: Republic of Peru

GEOGRAPHY AND PEOPLE

Peru is the third largest country in South America (after Brazil and Argentina) and is bordered on the north by Ecuador and Colombia, on the south by Chile, on the east by Brazil and Bolivia, and on the west by a 1,400-mile Pacific Ocean coastline.

The country is vertically divided into three well-defined topographic and climatic regions:

(1) The coastal area, from 10 to 100 miles wide, is arid or semiarid with mild and equable temperatures throughout the year. Despite the scarcity of rain, much of the industrial,

commercial, and agricultural activity is centered in this region. Forty percent of the population lives here and produces more than 50 percent of the gross national product (GNP).

(2) The Andes Mountains, about 200 miles wide, occupy about 27 percent of Peru's land area. These mountains are the principal barrier to transportation and communication links between the coast and the interior. The rugged eastern slopes culminate in snow-clad Mt. Huascarán—22,200 feet above sea level. The climate ranges from temperate to frigid, depending on elevation. Rainfall exceeds 100 inches annually on the eastern slopes but diminishes southward causing changes in vegetation. The Andes Mountain area is the most populous region (about 50 percent, mostly Indian) and contains the major deposits of mineral wealth.

(3) The isolated eastern lowlands, or *Montaña*, occupy more than half of Peru's total land area. They consist of vast, uncharted hills, forests, and tropical jungle through which numerous rivers, the only transportation routes in the area, wind to the Amazon River. The climate is humid and warm with abundant rainfall throughout the year. This area is very sparsely populated and largely undeveloped, although mahogany and cedar are grown commercially. There is evidence of petroleum deposits in this area and oil exploration is increasing.

Lima's climate is often compared with that of San Francisco. There are

PROFILE

Geography

AREA: 496,222 sq. mi. (3 times larger than Calif.). CAPITAL: Lima (pop. ca. 4 million). OTHER CITIES: Arequipa, Chiclayo, Cuzco, Puno, Trujillo, Tumbes.

People

POPULATION: 14.9 million (1975 est.). ANNUAL GROWTH RATE: 3.1% (1975 est.). DENSITY: 30 per sq. mi. ETHNIC GROUPS: Indian (46%), Mestizo (43%), Caucasian (11%). RELIGION: Roman Catholic (over 90%). LANGUAGES: Spanish (official), Quechua, Aymara. LITERACY: 61%. LIFE EXPECTANCY: 58 yrs.

Government

TYPE: Military. INDEPENDENCE: 1821. DATE OF CONSTITUTION: April 10, 1933 (some provisions no longer operative).

BRANCHES: Executive—Military President, all-military Council and Cabinet. Legislative—None. Judicial—Supreme Court and lower courts.

POLITICAL PARTIES: Parties exist but have no role in governing process. SUFFRAGE: Elections suspended. POLITICAL SUBDIVISIONS: 24 Departments, Provinces, Districts.

FLAG: Three vertical stripes—red, white, red—with coat of arms on center stripe.

Economy

GROSS NATIONAL PRODUCT (GNP): \$8.4 billion (1973). ANNUAL GROWTH RATE: 6% (1970-74 avg.). PER CAPITA INCOME: \$560 (1973). PER CAPITA GROWTH RATE: 3%.

AGRICULTURE: Land 23%. Labor 42.7%. Products—sugar, fishmeal, cotton-wool.

INDUSTRY: Labor 15.1%. Products—copper, zinc, iron ore, other metals.

NATURAL RESOURCES: Minerals and metals, petroleum, fish, forests.

TRADE: Exports—\$1,049.5 million (1973): copper, fish products, cotton, sugar, zinc, coffee, petroleum, iron ore, wool. Imports—\$1,025.6 million (1973): machinery, cereals, chemicals, pharmaceuticals. Partners—U.S., Europe, Western Hemisphere, Japan.

OFFICIAL EXCHANGE RATE: 43.88 soles=US\$1.

ECONOMIC AID RECEIVED: Total—NA. U.S. only—\$1.4 billion (1945-74, loans, grants, P.L. 480).

MEMBERSHIP IN INTERNATIONAL ORGANIZATIONS: U.N., Organization of American States (OAS), Andean Common Market, Latin American Free Trade Association (LAFTA).

no extreme temperatures and little daily variation. During winter (May-November) Lima is covered by low-hanging fog; the atmosphere is usually cold, damp, and humid, with very little sunshine. In contrast, Chosica, a 45-minute drive inland from Lima, is at an altitude of 3,000 feet and winter days are sunny and dry. Lima's summers are warm and sunny almost every day and pleasantly cool at night.

The official language of Peru is Spanish, although many Indians speak only their native Quechua and Aymara. The forest Indians of the eastern region speak a wide variety of unrelated dialects and languages. Their number is small—about 100,000—and diminishing rapidly. These people are considered among the most primitive in the world, still maintaining a stone-age existence.

HISTORY

When the Spanish arrived in 1531 the territory now included in Peru formed the nucleus of the highly developed Inca civilization, which emerged in the 11th or early 12th century. Centered at Cuzco, Peru, the Inca Empire extended over a vast region from northern Ecuador to central Chile. The Spanish explorer Francisco Pizarro, in search of Inca wealth, arrived in the territory following a debilitating civil war and found conditions favorable for conquest. By 1533 the capital at Cuzco had fallen. During the next 10 years the Spanish engaged in civil wars, but by 1542 new Spanish arrivals had consolidated the control of Peru. Gold and silver from the Andes enriched the conquerors, and Peru became the principal source of Spanish wealth and power in South America.

Pizarro founded Lima in 1535. The viceroyalty established at Lima in 1542 had jurisdiction over Panama and all Spanish territory in South America, except Venezuela. By the time of the wars of independence (1820-24), Lima had become the most distinguished and aristocratic colonial capital, as well as the chief Spanish stronghold in America.

Peru's independence movement was led by José de San Martín (of Argen-

READING LIST

These titles are provided as a general indication of the material currently available on this country. The Department of State does not endorse the specific views in unofficial publications as representing the position of the U.S. Government.

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tina) and Simón Bolívar (of Venezuela). San Martín proclaimed Peruvian independence from Spain on July 28, 1821, and its emancipation was completed in December 1824 when Bolívar defeated the last Spanish troops, thus marking the end of Spanish rule in South America. Spain made several futile attempts to regain its former colonies, but in 1879 it finally recognized Peru's independence.

During its postindependence history, Peru has been dominated by strong-man rule—military and civilian. It is presently ruled by a military government which seized power from constitutionally elected President Fernando Belaúnde Terry on October 3, 1968, in a bloodless coup d'état. The military government is headed by Gen. Juan Velasco Alvarado.

GOVERNMENT

Although Peru is now ruled by the military, which has assumed all governing authority and rules by national decree, its constitution of April 10, 1933, established a republic with legislative, executive, and judicial branches. These constitutional provisions were last operative under the Belaúnde administration (1963-68).

Now, a revolutionary junta, composed of the three armed forces ministers, selects the President, who governs with an all-military Cabinet. President Juan Velasco has emerged as the strong, central figure of the military government, although the revolutionary junta continues to participate in major decisionmaking. The bicameral Congress was disbanded in 1968. The Supreme Court, with 16 justices, is the highest court in Peru.

TRAVEL NOTES

Climate and Clothing—During the damp winter season (May-Nov.) medium to heavyweight clothing is suitable; in summer, lightweight clothing. Local tastes are similar to those in the U.S.

Health—Community sanitation conditions are not a serious problem. Lima has several good restaurants; however, outside Lima it is best to dine at a Tourist Hotel and take reasonable precautions. Though the water in Lima is treated, outside the area you should boil it. Gamma globulin is recommended against hepatitis. At high altitudes in the Andes lack of oxygen may cause headaches.

Telecommunications—National and international telephone and telegraph service is available in Lima and major cities, although there are often delays in placing calls.

Transportation—Lima is served by several international airlines and economic air travel within the country is possible. The scenic Central Railway connecting Lima with the central highlands of the Peruvian Andes is the world's highest standard-gauge railway, crossing the main range of the Andes at over 15,000 feet. The more extensive Southern Railway links Mollendo on the coast with Arequipa, Cuzco, and Puno.

Taxis are available in Lima and principal cities; rental cars are available in Lima.

For administrative purposes Peru is divided into 24 Departments. Departmental Prefects and Mayors are appointed by the central government.

Principal Government Officials *

President—Div. Gen. (Ret.) Juan Velasco Alvarado
 Prime Minister and Minister of War—Div. Gen. Francisco Morales Bermudez Cerruti
 Minister of Navy—Vice Adm. Guillermo Faura Gaig
 Minister of Air—Lt. Gen. Rolando Gilardi Rodriguez

Other Ministers

Interior—Div. Gen. Pedro Richter Prada
 Foreign Relations—Div. Gen. Miguel Angel de la Flor Valle

(*)NOTE: The list of principal Government officials is out of date with the coup d'etat in July 1975 when Gen. Velasco was removed from office and Gen. Morales Bermudez became President (see Tab F-2).

Economy and Finance—Brig. Gen. Amilcar Vargas Gavilano
 Education—Brig. Gen. Ramon Miranda Ampuero

Health—Maj. Gen. Fernando Miro Quesada Bahamonde

Labor—Maj. Gen. Dante Poggi Moran
 Agrarian Reform and Natural Resources—Div. Gen. Enrique Gallegos Venero

Food—Div. Gen. Rafael Hoyos Rubio
 Industry and Tourism—Rear Adm. Alberto Jimenez de Lucio

Commerce—Maj. Gen. Luis Arias Graziani

Transport and Communications—Brig. Gen. Raul Meneses Arata

Mines and Energy—Div. Gen. Jorge Fernandez Maldonado Solari

Housing—Vice Adm. Augusto Valdez Velarde

Fisheries—Div. Gen. Javier Tantalean Vanini

Chief, Advisory Committee to the President (COAP)—Div. Gen. Jose Graham Hurtado

President, National Commission for Rehabilitation and Reconstruction—Brig. Gen. Luis La Vera Velarde

Chief, National System Support for Social Mobilization (SINAMOS)—Lt. Gen. Pedro Sala Orosco

Comptroller General of the Republic—Brig. Gen. Leoncio Perez Tenaud

Ambassador to the U.S.—Vice Adm. Jose Arce Larco

Ambassador to the U.N.—Javier Perez de Cuellar

Ambassador to the OAS—Luis Alvarado

Peru maintains an Embassy in the United States at 1700 Massachusetts Ave., NW., Washington, D.C. 20036.

POLITICAL CONDITIONS

In this century Peruvian governments have alternated between constitutional civilian and extraconstitutional military regimes. Political conditions since the 1930's have been influenced by the relationship between the Popular American Revolutionary Alliance (APRA), Peru's oldest mass-based political party, and the military. Experiencing alternate periods of legal

and illegal status as a party, APRA has so far been unable to assume the presidency. A mutual hostility between APRA and the military has in the past caused occasional bloodshed.

Free elections were last held in 1963 and were won by Fernando Belaúnde Terry of the Popular Action Party (AP) in coalition with the Christian Democratic Party. Control of the Congress, however, fell to a coalition of the opposition parties, which frustrated and diluted Belaúnde's reform program. Belaúnde's 6-year term was cut short by the October 1968 coup.

Latin America as a whole is concerned with national development, redistribution of income, and control of national resources. The Peruvian military has made clear that it, too, is preoccupied with these issues. The military announced at the time of the coup that it intended to transform Peru socially, economically, and culturally, emphasizing morality, law and order, and nationalism.

In December 1968 a 5-year plan was announced, stressing reorientation of capital from agriculture to industry, expropriation of large estates, and land distribution to peasants in the sierra. Based on estimates that by 1990 Peru's population will have doubled and become predominantly urban, a 20-year plan proposed integration of the Indian population; doubling per capita income; redistribution of urban population away from the coast and Lima, along with the encouragement of alternate foci of development inland; encouragement of internal investment in infrastructure; subordination of foreign investment to development goals; and reduction of dependence on external forces, political and economic.

The military government also made clear in 1968 that it would not relinquish power until its reforms were irreversible. It promised that it would transfer power to civilians through free elections and announced it would draft a new constitution which would, among other things, greatly enlarge the electorate.

Beginning in early 1969 the military government announced a series of reforms of a redistributive, Social-

ist, and statist nature. The first and most dramatic of these was an agrarian and water reform which includes the preservation of the principle of private ownership by having beneficiaries pay for the land.

Tax and credit incentives were created for the formation of cooperatives and a consolidation of smaller holdings. The cooperatives are intended to help absorb the steady increases in agrarian population and discourage rural-urban migration. Compensation is principally in long-term bonds which can be partially reinvested at face value in new industry. One of the more controversial aspects of the agrarian reform has been its application to the highly efficient and modern coastal sugar estates which have been turned over to cooperatives.

Today the government is studying further land reform measures, including whether to redistribute smaller private land holdings and whether to reorganize control of the larger cooperatives.

The Law of Industries of July 1970 established the blueprint of the military government's nationalist, Socialist, and statist approach to industrialization. The law sets priorities which identify industries reserved for the state, industries in which foreign investment is permitted and the amount of that participation, the state's priorities for industrialization, and tax and credit incentives applicable to each priority. This law also provides private capital with incentives for reinvestment and decentralization, as well as special incentives for small and medium producers. The redistributive aspects of the law are contained in the provision for "industrial communities." Twenty-five percent of annual pretax profits are to be set aside for the workers. Part of this amount is distributed as direct remuneration; the remainder buys shares for the "community" in the enterprise. Worker communities may eventually acquire up to 50 percent ownership of enterprises and a proportionate voice in management.

The industrial law's divestment provisions for foreign firms have been softened to harmonize with the

Andean Group regulations. (Present members of the Andean Group are Bolivia, Chile, Colombia, Ecuador, and Peru.) The subsequent mining, fishing, and telecommunications laws, although also providing for worker communities, emphasize profit-sharing among the workers within the entire sector.

On July 28, 1974, President Velasco announced the "Inca Plan," which he described as the blueprint which the military government has followed since 1968 to affect its social and economic revolution in Peru. The plan envisages a society in which nearly all industrial, commercial, and agricultural enterprises are state-owned, collectively worker-owned (termed "social property"), or co-managed by workers and owners. Peruvians will have a voice in their society by belonging to vocationally structured "organized sectors" (e.g. peasant, industrial labor, professional, etc., organizations). Control at the top is to remain in the hands of the military.

Political parties continue to exist but they have no formal role in the governing process. The military government has restructured the educational system, nationalized the media, and expropriated the free national press in order to make the education and information systems "more relevant" to the country's needs. In June 1971, the military government created an agency to mobilize popular support for its programs, the National System of Support for Social Mobilization (SINAMOS). Since mid-1974 this organization has been concentrating on creating the "organized sectors" of the population envisaged by the Inca Plan.

ECONOMY

Since the Spanish conquest, Peru has been world famous for its rich and varied mineral resources. Lead, copper, zinc, and iron ore constitute the principal metals of commercial importance and are frequently mined in lodes also containing silver, bismuth, cadmium, tin, and gold. Other minerals of significance are antimony, tungsten, man-

ganese, selenium, tellurium, and mercury. Among the numerous non-metallic minerals produced, petroleum is the most valuable. Others include coal, salt, limestone, marble, and gypsum. The mining sector accounts for about 40 percent of Peru's total exports.

The agricultural sector is sharply divided between two productive systems—commercial agriculture, largely export-oriented, and consumption agriculture, oriented to local markets and subsistence production. Nearly half the population works in agriculture.

From insignificance in 1950 the fish, fishmeal, and marine products industries have moved to the forefront of the national economy. The principal component of the fishing industries is fishmeal production. The fishmeal industry is recovering slowly after a sharp drop in production in 1972, which resulted from a decline in catches of anchovies because of a shift in ocean currents in spawning grounds. Fishmeal exports in 1974 were still well below 1970 and 1971 levels.

Peru faces serious economic problems, possibly the most serious of which is a growing deficit balance of payments resulting from sharp increases in imports and the purchase of services abroad. Increasing requirements for imports of food, fuel, raw materials, and capital goods at consistently higher prices are pushing the import bill up while export income is increasing less rapidly. Peru's mineral production, its major export, is not expected to increase significantly until 1976 when new mines are brought into production. Peru hopes to be self-sufficient in petroleum products by 1978 when oil from the eastern jungles reaches the coast. Whether these hopes will materialize will be better known by late 1975 when the level of Peru's jungle oil reserves should be more clearly established.

The military government's reform program and restrictions on foreign capital have created uncertainty for new investment in Peru. Apart from growing exploration expenditures by oil companies and investment in mining, there is little new foreign private investment. Some reinvestment

is occurring in manufacturing to replace obsolete or wornout equipment and to stay abreast of rising demand. Japan and European countries as well as the United States have been involved in financing the development of Peru's rich mineral deposits and petroleum resources.

Trade

Foreign trade is of fundamental importance to the country, and the diversity of Peru's exports makes the national economy less susceptible than that of many other Latin American countries to price fluctuations for individual commodities. A sharp drop in 1974 in world copper prices—Peru's leading foreign exchange earner—however, had an immediate adverse effect on Peru's trade balance and financial position. Future growth in exports is likely to be concentrated in mining and petroleum if a sufficient amount is discovered.

The total value of Peru's foreign trade is over \$2 billion annually. From 1966 through 1973, Peru maintained a favorable balance of trade, but a deficit balance of trade was forecast for 1974 and 1975. Peru has had to borrow extensively abroad to finance its record imports. The foreign exchange position of the Central Reserve Bank of Peru was \$438.8 million on December 31, 1973.

U.S. Investment in Peru

In the early 1970's following the military government's expropriation of several major U.S.-owned enterprises and its declaration of intent to nationalize basic industry, the nature of U.S. and other foreign investment in Peru underwent fundamental changes. In February 1974, an agreement was reached between Peru and the United States by which the military government agreed to compensate owners of properties which it had confiscated from U.S. firms in the 1968-73 period. This settlement cleared the way for more normal economic relations between the two countries.

New U.S. investment is concentrated in the fields of mining and petroleum, but new "Peruvian-model"

management and development contracts (with the government retaining title and a larger share of the product) have replaced the former system of mineral concessions. Nevertheless, a few of the old-style mining concessions remain, most notable of which are the new Cuajone copper mines in southern Peru (\$550 million financing was completed in December 1974) and the iron mines operated by the Marcona Corporation.

U.S. Economic Assistance

The Agency for International Development (A.I.D.) has focused most of its resources on projects in agriculture and education. In agriculture, A.I.D. grant assistance, which in prior years helped establish research and extension capabilities, is now concentrated on developing a more systematic approach to problem solving and decisionmaking to help the Government of Peru deal with the rapidly increasing demands on agriculture. A \$10 million loan authorized in FY 1974 for rural enterprise development is directed at increasing employment and income opportunities by assisting rural enterprises with an integrated program of credit and technical assistance.

In education, A.I.D. is supporting Peru's education reform which emphasizes providing education opportunities for all Peruvians to permit their greater participation in society as well as providing useful training for the economic needs of the nation. Assistance is directed at education planning and research with emphasis on determining manpower needs, training of administrators, development and testing of nonformal education programs and development and testing of alternative methods of bilingual education for non-Spanish (i.e. Indian) speaking Peruvians.

U.S.-supported school lunch programs currently reach some 600,000 students. Three U.S. voluntary agencies provide lunches for about 100,000 of these children. Support is also provided for certain government sponsored maternal-child health programs.

	Cumulative Total (in millions-US \$) 7/1/45 - 6/30/74
TOTAL	1,442.0
Agency for International Development (A.I.D.)	226.1
Loans	(136.6)
Technical Assistance Grants	(89.5)
International Bank for Reconstruction and Development (World Bank)	318.3
Inter-American Development Bank (IDB) Loans (Ordinary Capital and Fund for Special Operations)	303.6
Export-Import Bank Loans	331.1
Food for Peace	132.3
Peace Corps	24.6
Other (Including Commodity Credit Corporation)	106.0

FOREIGN RELATIONS

Peru's foreign policy emphasizes independence, nationalism, universality, and the defense of sovereignty, natural resources, and frontiers.

Peru is a leading proponent of the interests of the Third World and raw material-producing countries. The military government maintains diplomatic relations with most Communist governments as well as trade relations with North Korea and periodic liaison with the People's Revolutionary Government of Viet-Nam (Viet Cong). Peru has had diplomatic relations with Cuba since 1972 and has advocated readmission of Cuba to the OAS.

The Andean Common Market is headquartered at Lima.

U.S.-PERU RELATIONS

Relations between the United States and Peru markedly improved after the investment expropriation settlement in February 1974 and today, despite occasional differences of views on matters of economics, relations are cordial. Peru is an important element in the "new dialogue" which the United States seeks with Latin American governments.

An important unresolved U.S.-Peruvian problem is Peru's claim, along with Ecuador and Chile, to sovereignty over a 200-miles extent of contiguous

waters, a claim affecting U.S. tuna fishermen, among others.

U.S. policy objectives are to: (1) maintain friendly relations with Peru and resolve outstanding bilateral issues, (2) support Peru's efforts to raise living standards and develop a sound economy, (3) insure Peru's continued support of the basic non-Communist international policies, and (4) assure Peru's continued cooperation in the defense of the Western Hemisphere from external threat and internal subversion.

Principal U.S. Officials

- Ambassador—Robert W. Dean
- Counselor of Embassy—Malcolm R. Barneby
- Public Affairs Officer (USIS)—Jack W. Gallagher
- Chief, Political Section—Jackson L. Smith
- Chief, Economic Section—Edward R. Cheyney
- Chief, Consular Section—Walter H. Hummel
- Commercial Attache—Richard Rueda, Jr.

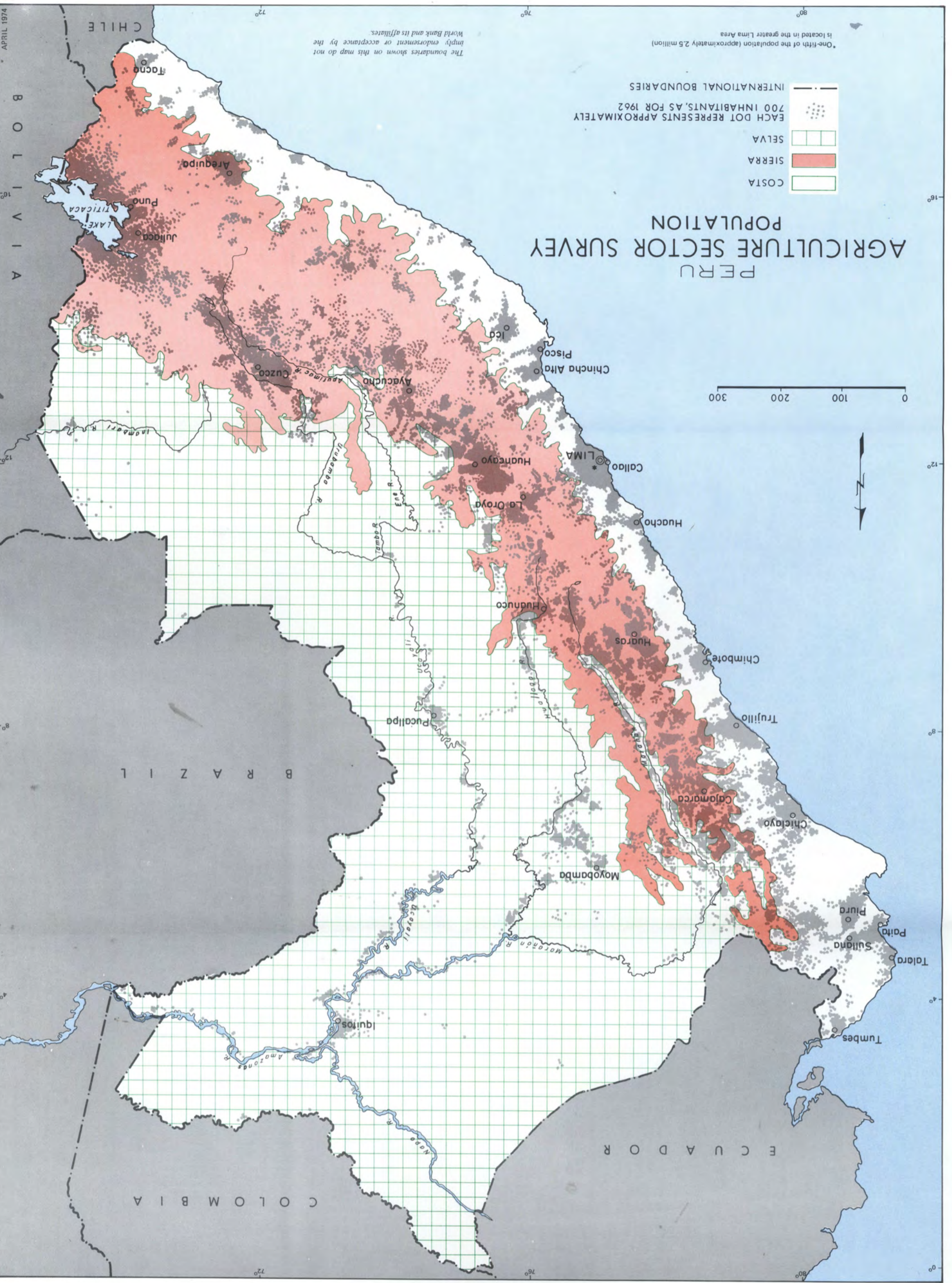
- Director, U.S. A.I.D. Mission—Donald R. Finberg
- Army Attache—Col. William E. Grugin
- Air Attache—Lt. Col. Robie Hackworth
- Naval and Defense Attache—Capt. James R. Parce
- Chief, Military Assistance Advisory Group (MAAG)—Col. Russel D. Brewington USAF

The U.S. Embassy in Peru is located at Avenidas Garcilazo de la Vega and Espana, Lima.

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The boundaries shown on this map do not imply endorsement or acceptance by the World Bank and its affiliates.

One-fifth of the population (approximately 2.5 million) is located in the greater Lima Area.

PERU AGRICULTURE SECTOR SURVEY POPULATION

INTERNATIONAL BOUNDARIES

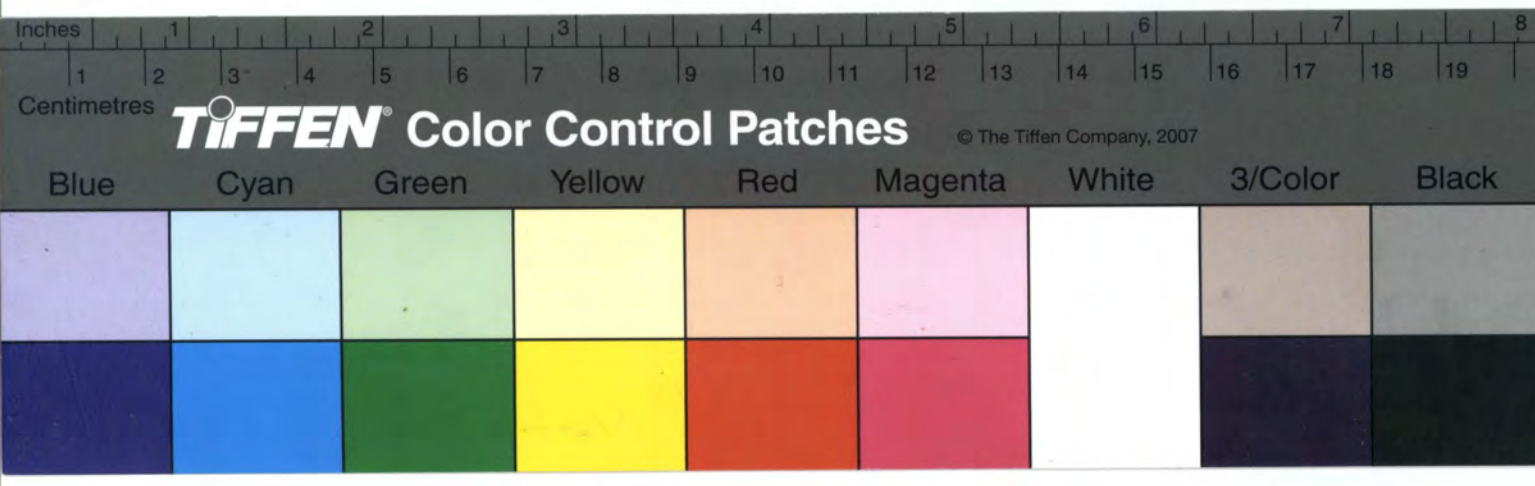
EACH DOT REPRESENTS APPROXIMATELY 700 INHABITANTS, AS FOR 1962

SELVA

SIERRA

COSTA

0 100 200 300



LIST OF MINISTERS

PRESIDENT OF THE REPUBLIC:

General Francisco Morales Bermudez

PRIME MINISTER AND MINISTER OF WAR:

General Jorge Fernandez Maldonado

MINISTER OF THE AIR FORCE:

General Dante Poggi

MINISTER OF AGRICULTURE:

General Enrique Gallegos Venero

MINISTER OF FOOD:

General Rafael Hoyos Rubio

MINISTER OF COMMERCE:

General Luis Arias Graziani

MINISTER OF ECONOMY AND FINANCE:

Dr. Luis Barua Castañeda

MINISTER OF EDUCATION:

General Ramon Miranda Ampuero

MINISTER OF ENERGY AND MINES:

General Arturo La Torre Di Talla

MINISTER OF INDUSTRY AND TOURISM:

General Gaston Ibañez O'Brien

MINISTER OF INTERIOR:

General Luis Cisneros Vizquerra

MINISTER OF THE NAVY:

Vice-Admiral Jorge Parodi Galliani

MINISTER OF FISHERIES:

Rear Admiral Francisco Mariategui Angulo

MINISTER OF FOREIGN AFFAIRS:

General Miguel A. de la Flor Valle

MINISTER OF HEALTH:

General Jorge Tamayo de la Flor

MINISTER OF LABOR:

General Luis Galindo Chapman

MINISTER OF TRANSPORT AND COMMUNICATIONS:

General Artemio Garcia Vargas

MINISTER OF HOUSING AND CONSTRUCTION:

Rear-Admiral Isaias Paredes Arana

NOTE:

The bio-sketches are not complete because we have not found data on new appointees in Washington. Fernando Mendoza will prepare additional sketches for other key officials concerned with economic matters while in Peru next week for insertion in the briefing book on Mr. McNamara's arrival in Peru.

Francisco MORALES BERMUDEZ Cerrutti

President of PERU ^{1/}

1. Until August 28, 1975 when he seized power in a bloodless coup against President Juan Velasco, Division General Morales Bermudez was Prime Minister and Minister of War, positions he had held since the preceding February.
2. For a few months in 1968 at the end of the Belaunde Government -the last elected government of Peru- and again from 1969 to 1973, he was Minister of Economy and Finance. A career military man, he acquired his expertise in financial matters in army staff positions. Generally he is regarded as a pragmatist and a realist in his financial policies.
3. Morales Bermudez was born October 4, 1921 in Lima. His grandfather, Colonel Remigio Morales Bermudez, was a hero of the War of the Pacific and was President of Peru from 1890-1894. His father, Lt. Col. Segundo Remigio Morales Bermudez was an army officer who was killed during an APRA uprising in Northern Peru in the 1930's.
4. Morales Bermudez was a brilliant student in school and in military colleges. He is an anti-communist, but he has been frequently critical of U.S. policy in Latin America. He is a nationalist who enjoys a reputation for high personal integrity and temperance. He is married to the former Rose Peraglio and the couple have five children.
5. President Morales Bermudez does not speak English.

Jorge FERNANDEZ MALDONADO Solari

Prime Minister and Minister of War

1. General Fernandez Maldonado, 53, became Prime Minister and Minister of War on February 1, 1976, succeeding General Vargas Prieto, who reached mandatory retirement age. Since the August 28, 1975 coup he had been chief of the joint military staff. From 1969 to 1975, under President Velasco, he served as Minister of Energy and Mines.
2. Fernandez Maldonado has a strong and charismatic personality and is widely regarded as a standard bearer of the radicals in the Peruvian military government. He was one of the army officers who planned the October 1968 coup. It was he who read the army's radio message announcing the success of the coup and, a few days later, the announcement of the expropriation of the U.S.-owned International Petroleum Company.

^{1/} More insights on his political thinking and activities is available under Tab F-3 on recent political developments.

3. However it was under his tenure as Minister of Energy and Mines that the contracts for the large Cuaajone mine and the petroleum explorations were signed with foreign companies. He is probably more sensitive to the nationalistic feelings of the revolution and to outside criticism than General Morales Bermudez. He is a longtime personal friend of General Morales Bermudez.
4. Fernandez Maldonado is a southerner, born on May 29, 1922 in Ilo. His higher education was in the army schools system. He is married to the former Estela Castro Faucheux. The couple have four children.
5. He speaks English but prefers not to use it.

Luis BARUA Castañeda

Minister of Economy and Finance

1. Dr. Luis Barúa Castañeda became the first civilian member of a cabinet in Peru's military government when President Morales Bermudez named him to this position a few days after taking power in August 28, 1975.
2. Highly respected economist, could be considered as a technocrat. He worked in the Ministry of Economy and Finance during the time General Morales Bermudez was Minister of Economy and Finance as Director General for Economic Affairs. From January 1971 to at least June 1973 he served as President of the Board of Directors of the state-owned Banco Popular and, from January 1973 until his appointment as Minister of Economy and Finance, as President of the Board of Directors of the Government's development finance company, COFIDE.
3. Dr. Barúa is reputed to have the President's unlimited confidence. He is well traveled and speaks some (rather limited) English.
4. As President of COFIDE he has served as Alternate Governor of the Bank beginning in 1973 and is currently the Governor for Peru.

Miguel Angel DE LA FLOR Valle

Minister of Foreign Affairs

1. Army Brigadier General de la Flor, 52, has been Minister of Foreign Affairs since January 1972. A member of former President Juan Velasco's inner circle of supporters since the 1968 coup, after the military takeover he served first as president of the Peruvian Telephone Company. In 1971 he became commandant of the Military Instruction Center.

2. He is a strong nationalist and self-styled "Catholic socialist". He is a leading exponent of Peru's militant position in various Third World fora and in hemispheric councils.

3. De la Flor speaks fluent French, but knows no English. He is married and the father of four children.

Oscar ESPINOZA

President of COFIDE

1. Born in Arequipa in 1938. Obtained the degree of Civil Engineer in 1961 in Lima and attended several courses abroad (North Carolina University in 1961-62 and Italy in 1963-64). Since 1965 through 1970 held executive positions in regional organizations in the southern part of the country and taught at the Universities of the Altiplano and Santa Maria de Arequipa. In 1970-71 studied at Harvard where he obtained a Master's Degree. Subsequently held high positions in the National Planning Institute until 1973 when Dr. Barua appointed him as General Manager of COFIDE. Upon the appointment of Dr. Barua as Minister of Economy and Finance last August, Mr. Espinoza was appointed as President of COFIDE; as such he is Alternate Governor of the Bank for Peru.

2. Mr. Espinoza is the prototype of the young, aggressive and well educated manager. He has an exuberant personality always full of enthusiasm and of willingness to express articulately his views. He combines a good technical background with a sense of political constraints. He became well known to Bank staff during the preparation of the Bank loan to COFIDE now being appraised. As Alternate Governor of the Bank he is likely to accompany you to a number of meetings and trips.

3. He is married and speaks English fluently.

Carlos SANTISTEVAN de Noriega

President of the Central Reserve Bank

1. Born in Arequipa in 1937. Studied Law and Economics at San Agustin University (Arequipa) and Catholic University (Lima). Since 1963 through 1968 Mr. Santistevan was involved in private banking in various capacities including Assistant Manager of First National City Bank in Lima. In 1968 through 1971 he was Assistant Manager of the Central Reserve Bank and advisor to the Office of the President; during this time he had an opportunity to work closely with the then Minister of Economy and Finance, General Morales Bermudez. In August 1971, he was appointed Alternate Executive Director of the Bank where he served until October 1976 when he was appointed President of the Central Reserve Bank.

2. Mr. Santistevan is part of a new generation of bright young technicians that rose to positions of power with General Morales Bermudez. He is a man of stature that combines an unusual capacity for diplomacy and negotiation with an aggressive personality willing to get involved deeply in development issues. Although he is a hard bargainer he has a keen sense of realism of what is politically and economically feasible. During his term as Alternate Executive Director of the Bank he acquired a solid understanding of macroeconomic issues that complemented his commercial banking background. Here he also strived incessantly to maintain good relations between the Bank and the Peruvian Government and to build up an image of solidity of the Government in the international banking community. He was also an active mediator in the negotiations with the U.S. Government on the settling of investment disputes that culminated in the "Green Agreement". He also won the confidence and respect of Bank staff (and never abused it) as an intermediary helping solve economic and project related issues.

3. Mr. Santistevan is married; speaks fluent English and has an acute sense of humor.

Guillermo VAN OORDT

General Manager of COFIDE

1. Born in Lima in 1939, where he attended primary and secondary schools. He then studied at MIT (Boston) where he obtained a degree of Bachelor of Science in Engineering Management in 1962 and in Harvard University where he obtained a Masters Degree in Public Administration in 1973. Since 1962 Mr. van Oordt has held a number of executive jobs in Peru with foreign companies in the country, regional institutions and in the Central Government. In 1969, he joined the Ministry of Industry and Commerce as Director for Planning and in 1973 he became Undersecretary of the Ministry. In August 1975, he was appointed as Director General of COFIDE.

2. Mr. van Oordt combines a solid academic background in engineering, management and economics with a deep conviction of the overall objectives of the Government. He is however constructively critical of some of the specific policies pursued in the past, particularly in the industrial sector. He is very articulate in presenting his views and in analyzing issues in a "no nonsense" practical way with little use of political rhetoric although he has a rather quiet and reserved personality. He has impressed Bank staff for his solid grasp and understanding of the problems in the industrial sector. Now, as General Manager of COFIDE he is bound to be more closely involved in Bank lending activity.

3. He is married and speaks fluent English.

CORPORACION FINANCIERA DE DESARROLLO - COFIDE
GERENCIA GENERAL

RELACION DE PERSONAS QUE VIAJAN EN EL VUELO

LIMA - TRUJILLO - TARAPOTO - LIMA

1. ✓ Sr. Robert McNamara Presidente
2. ✓ Sr. Adalbert Krieger Vice Presidente Regional para América Latina y el Caribe
3. ✓ Sr. William Clark Vice Presidente de Relaciones Exteriores
4. ✓ Sr. Enrique Lerdau Director de Programas para América Latina y el Caribe
5. ✓ Sr. Elkyn Chaparro Economista Encargado del Perú
6. ✓ Sr. Fernando Mendoza Oficial de Préstamos para el Perú
7. ✓ Ing. Oscar Espinosa Presidente de COFIDE
8. ✓ Ing. Guillermo van Oordt Gerente General de COFIDE
9. ✓ Ing. Alejandro Vera Director Técnico del Instituto Nacional de Planificación
10. ✓ Dr. Otoniel Velasco Presidente de ELECTROPERU
11. ✓ Dr. Gil Indacochea Presidente de INDUPERU
12. ✓ Ing. Alejandro Seminario Coordinador del Area de Proyectos de Inversión del Instituto Nacional de Planificación
13. ✓ Ing. John Hartley Gerente de Operaciones de COFIDE
14. C.P.C. Pedro MacKee Gerente Financiero de COFIDE
15. Sr. Sven Burmeester Asistente del Presidente
16. PIP Alfredo Valdivia Comisario Superior PIP ✓

CABRERA

ERIK

KOLIN-HANSEN

Thuylls
Caragane - 30 kaur
Paprydant - Chagari Thuyal
Thuylls 1038
Faldyrotte } 1140
 } overflugt alle papyrer

luch Faldyrotte
leant 438
alder 631

RELACION DE ASISTENTES

BANCO MUNDIAL

Sr. Robert Mc Namara	Presidente
Sr. Adalbert Krieger	Vice Presidente Regional para América Latina y el Caribe
Sr. William Clark	Vice Presidente de Relaciones Exteriores
Sr. Enrique Lerdau	Director de Programas para América Latina y el Caribe
Sr. Sven Burmeester	Asistente del Presidente
Sr. Elkyn Chaparro	Economista Encargado del Perú
Sr. Fernando Mendoza	Oficial de Préstamos para el Perú

SECTOR ECONOMIA Y FINANZAS

Ing. Oscar Espinosa	Presidente del Directorio de COFIDE
Ing. Guillermo van Oordt	Gerente General de COFIDE
Dr. Ulises Montoya	Director Técnico de la Dirección de Crédito Público - MEF
Dr. Marco Antonio Pajuelo	Director Ejecutivo de la Dirección General de Asuntos Financieros

INSTITUTO NACIONAL DE PLANIFICACION

Ing. Alejandro Vera	Director Técnico
Ing. Alejandro Seminario ✓	Coordinador del Area de Proyectos de Inversión

EMPRESAS PUBLICAS

General de Brigada EP	Presidente de PETROPERU
Máximo León Velarde	Gerente General de PETROPERU
Crnel. EP Jorge Luna Salinas	Sub-Gerente Técnico
Ing. Alberto Bruce	Presidente de MINERO PERU
✓ Ing. Antonio Tord	Gerente General de MINERO PERU
✓ Ing. Luis Briceño	Presidente de CENTROMIN = <i>Cerro de Pasco</i>
✓ Ing. Guillermo Flores	Gerente General Ejecutivo de CENTROMIN
✓ Ing. Behram Wadia	Presidente de ELECTROPERU
Dr. Otoniel Velasco	Gerente General de ELECTROPERU
Ing. Jorge Ratto	Presidente de INDUPERU
Dr. Gil Indacochea	Gerente General de INDUPERU
Dr. Adrián Fajardo	Asesor del Presidente de INDUPERU
Ing. Jorge Cárcamo	Presidente de SIDERPERU
Cmdte. AP Eduardo Barragán	

MR. JEAN LABBENS

UNDP Resident Representative

French nationality, 55 years old. He studied sociology in France. Active member of the "Resistence Francaise" during the war. Has worked for over twenty years in UNESCO, mostly in Latin America (Brazil, Costa Rica, Chile, etc.) For the last three years and a half has been UNDP Representative in Peru.

Mr. Labbens is a talkative man, well informed about Peruvian politics, and knowledgeable about the Bank in general and the Bank's activities in Peru, in particular. He has been helpful to Bank staff during field trips and keeps in touch with the Bank as necessary.

Married; speaks fluently many languages including english.

ERNST KELLER

Ex-President of ADELA

Mr. Keller is a Swiss national who has lived in Peru since 1953. He studied Industrial Engineering ~~in~~ and Business Administration in Switzerland (Ecole Politechnique). Up to 1957 was General Manager of Grace Co. in Peru and from 1957 through 1964 Senior Partner of Keller Engineering, a consulting firm. He was also the founder and President of PERUINVEST, a development finance company. Since 1964 through 1975 has served as President and Chief Executive of ADELA. Recently he has retired.

Mr. Keller is well known to Mr. Krieger. Speaks fluent english

ALVARO VILLALOBOS

An economist in his early forties. Has been professor for seven years at the Catholic University in Lima and General Manager of "Sociedad de Industrias" for 14 years. Dean of the Peruvian Association of Economists and Director of the Peruvian Institute of Business Administration.

Vice-President of the Advisory Council of the Minister of Economy and Finance, a consultative organ composed of private sector individuals appointed by the Minister. He is particularly interested in the field of economic integration. Does not speak english.

PEDRO REISER

A prominent industrialist in Peru, 40 years old, member of the Board of Directors of several banks, including the Central Reserve Bank, and many private companies in the Industrial, Commerce and Tourism Sectors. Ex-member of the Advisory Council of the Minister of Economy and Finance. Mr. Reiser is Doctor in Political Science and speaks english.

GABRIEL LANATA

Industrial Engineer in his mid-fifties. General Manager of Compañía Nacional de Cerveza (Brewery), Director of PERUINVEST. He is a member of the Advisory Council of the Minister of Economy and Finance. Strong private entrepreneur; speaks english.

LUIS PAREDES

President of the Peruvian Institute of Business Administration and member of the Advisory Council of the Minister of Finance. He is member of the board of several companies and banks, and General Manager of a fertilizer company. Does not speak english.

MICHELLE PROUD

Co-Editor of Andean Times

Nationality British; age 35; educated in England (M.A. Cambridge University); lived for five years in Peru.

Co-editor, with Nicholas Asheshow, of Andean Report; contributor to Financial Times, London, and Latin America Economic Report, to technical journals (mining, oil, chemicals, engineering, etc.) in the U.S. and U.K., and locally to Lima Times, Ingeniero Andino, Adela Bulletin, and others.

Besides writing on general economic themes (finance, industry, etc.) in Perú and the five other Andean countries, has specialized in coverage of the Andean Group and its programs.

Previously associate editor of Peruvian Times, and editor of Latin America Economic Report, until end 1974 when Peruvian Times closed down by Government and editorship of Economic Report transferred to London.

Before coming to Peru worked in book publishing (Penguin Books, London) and free-lance journalism, and has travelled extensively in Europe, Asia (India, Nepal, Ceylon) and Africa (Ethiopia).

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CARLOS MARIOTTI

Swiss national, born in 1912. Doctor in Economics by Berne University (Switzerland). Until 1953 he worked for Swiss Federal Government, Red Cross International in Berlin and the Swiss Organization for Assistance to Refugees in Brazil. In 1953 he moved to Peru to work for ELECTROLIMA where he became General Manager and Chief Executive until 1973. During that time, the Bank made four loans to ELECTROLIMA which is one of the best run utility companies in Latin America. In 1973 the Government took over control of the company and Mr. Mariotti left. On March 2nd, the Bank made a fifth loan for ELECTROLIMA.

He is Director of several companies, co-founder and ex-president of the Peruvian Institute of Business Administration, ex-president of the Stock Exchange of Lima, ex-president of the Rotary Club of Lima and ex-member and ex-president of the Advisory Council of the Minister of Economy and Finance.

He is a very capable man, fully integrated in the Peruvian life, personal friend of President Morales Bermudez and well known to Bank staff.

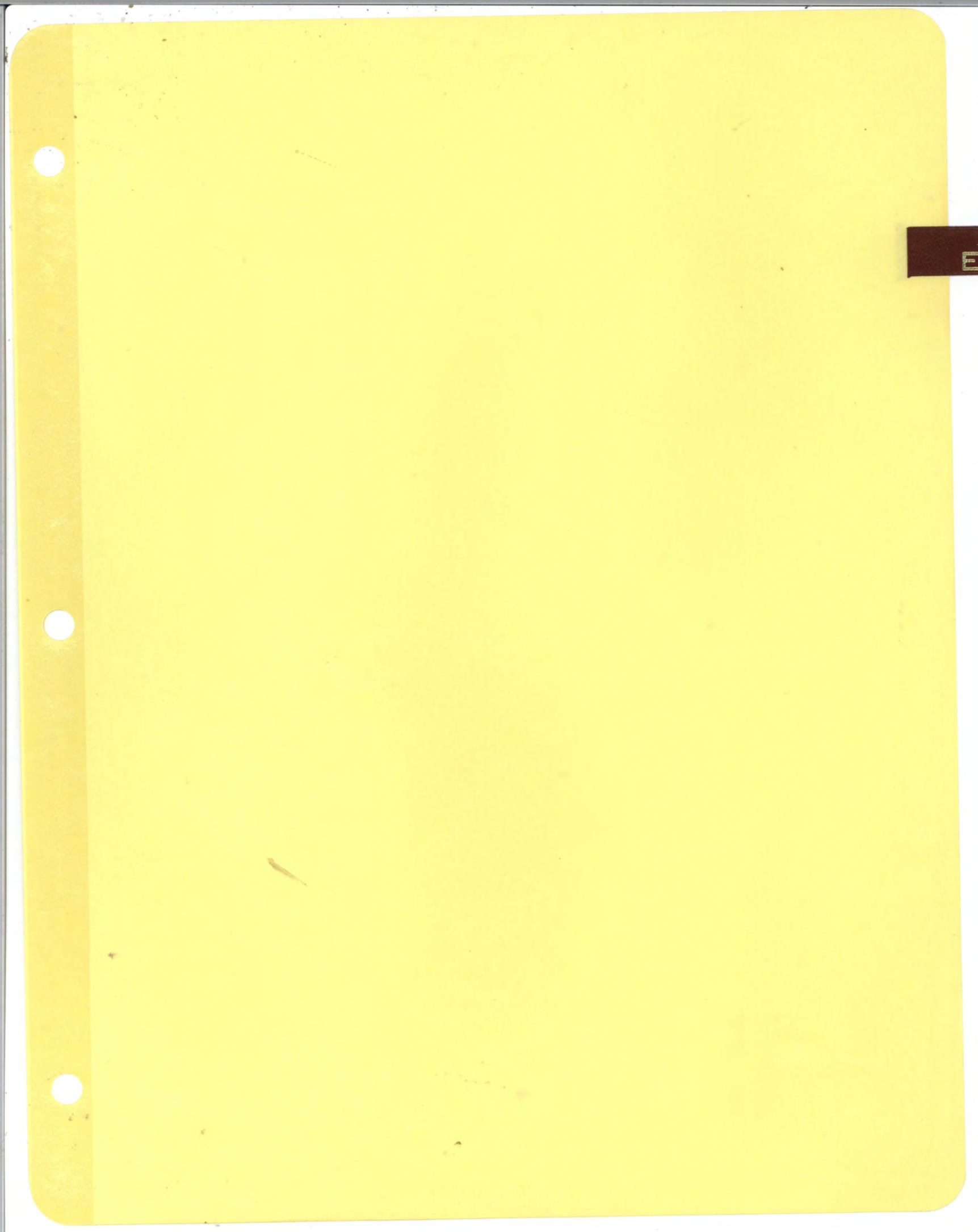
He is married, has three children and speaks fluent english.

Labbers 3/4 4:30 pm (RDR, urban, WDC)

distribution income has not improved -
middle urban - need at intermediate
export - crops of food? Better food - gives
more employment - (have 55% of urban double
of rural from RDR). Middle-class worried -
the evolution is for left of middle-class - not
for everybody (includes for peasant - urban, downward)
- 1976 will see serious political difficulties
Velloso Calvador is an interesting sign (RDR in bed)
Will get \$10 million WFP. Have ideas on plan
for mining, solar energy, companies Nacional - want
benefit for majority (plenty of overbudget) - de
Advantages peasant slogans

Keller 3/4 6 pm - Adels. Revolution was necessary -
democratic Govt didn't work out. But neither does
state planned economy. They all pretty
planned and poorly managed. Rev. tried to solve
some problems with political solutions. Velloso
became elaborate - one can argue with holes - one
can show with him - (has it well at both ends). Models
didn't finish housecleaning - what he says today
is entirely diff from what he said as Minister. Plan
is in great form and econ diff - this is blamed on
external forces - industrial all much more important
yesterday only possible with 1 good and productivist
the latter has dropped 20-25% - due to union problems.
New unions were created to oppose APPRA - unions
and they all leftist. Com. Industrial was then
related to dominate unions - it went the other
way. Can't free, transfer people - labor demands
all unreasonable - 5-10 times profit (negative growth)

Paredes, Lavalle, Lopez 5:40 (Lopez left) Govt has
good intentions - have managed agricultural changes
without conflict. But we are all suffering from U. agri
productivity (he is afraid) - over time industrial det
Lamma on Keller. Need the largest possible support -
holders of low material way of and then bubble off
- roller for RDR. Reply: Nature of foreign I (detour 2nd)
+ would be practice has had bad psychological influence
Paredes. owners lost sense of ownership



E.

TOPICS FOR DISCUSSION

Background

1. While President Morales Bermudez was Minister of Economy and Finance (April 1969 through December 1974) he worked closely with the Bank, including meetings with you during the Bank-Fund Annual Meetings in 1969, 1970 and 1971. He also followed with a great deal of interest your statements at the Annual Meetings and was particularly impressed with your Nairobi speech. (Resumes of your meetings and correspondence with the Minister are in Tab G-4).

2. In his period as Finance Minister, General Morales Bermudez demonstrated a steadily growing understanding of Peru's economic problems and leadership in overcoming them. In an extremely difficult political situation in Peru, he had a leading part in resolving compensation problems resulting from expropriations of properties which enabled the Bank to resume lending after an extended period (see Tab G-3). He also had a key role in the revival of the Consultative Group for Peru and was the head of the Peruvian Delegation at the 1973 meeting.

3. After becoming Army Chief of Staff at the beginning of 1974 General Morales Bermudez continued to follow economic matters closely. Shortly after becoming Prime Minister in February 1975 he organized an Economic Council consisting of ministers concerned with economic affairs in an effort to strengthen Peruvian economic policies in the face of a difficult situation vis-a-vis the then President Juan Velasco.

Meeting with the President (Thursday, March 4, 12:00 noon)

4. After expressing your pleasure at being in Peru and referring to the useful meetings you had earlier when the President was Finance Minister, you might point out that you are particularly happy to have an opportunity to visit Peru and to observe at first hand the progress which Peru has made in recent years in attacking major social problems. In this connection you might refer to Peru's having rapidly carried out one of the most comprehensive land reform efforts in Latin America and to its effective program for attacking problems of urban slums, particularly in the Lima area. You might then point out the Bank's readiness to assist the Government in its program for reducing urban problems, citing as an example the sites and services project now under appraisal and indicating our expectation that it is likely to be a model for application in other countries since it builds upon the valuable experience Peru has already gained

in this field. You might also refer to the readiness of the Bank and other members of the Consultative Group to provide financing on rural development, particularly in the poorer zones of Peru, and to our hope that project preparation efforts can be accelerated in this field.

5. Turning to broader economic problems, reference might be made to the serious problems which have resulted for Peru and other developing countries because of the combination of the steeply increasing prices of petroleum and other imports and the weakening of markets for exports with the world recession. After referring to the major actions which have been taken under General Morales Bermudez leadership first as Prime Minister and recently as President to stem the reduction in savings and restrain imports, you might invite his views regarding Peru's economic outlook and the further actions the Government is planning to take to reduce Peru's present fiscal and balance of payments problem. (A summary of economic actions taken by the Government in 1975 and the initial months of 1976 to reduce Peru's current large fiscal and balance of payments gap, as well as additional actions still needed, is presented under Tab F-3).

6. In connection with the discussion of the overall economic situation and the Peruvian efforts both to curb imports and expand exports, mention might be made to the Bank's readiness to lend for projects designed to help in improving Peru's balance of payments and to assist Peru in organizing financing from other sources. An example which might be cited is the \$40 million IBRD loan (being negotiated during the week of February 17) for CENTROMIN with cofinancing from the IDB and with this operation with the company also serving as a catalyst for obtaining financing from other sources.

7. In the course of the discussion regarding plans for future Bank lending the caution would, of course, need to be expressed that the volume of our future lending will necessarily depend on the extent of Peru's creditworthiness. In the event that, prior to your visit, reasonable progress has not been made by the Peruvian and U.S. Governments toward reaching a final settlement of the outstanding Marcona compensation dispute, you also might indicate that our lending will also be dependent on such progress. (A brief summary of the status of the dispute is presented in Tab G-3. The subject of compensation may be raised by the Peruvian Government during the visit of Sec. Kissinger in the week of February 17 and/or be discussed between officials of the two countries during the following week. A supplementary briefing will be given you on this matter, before your meeting with the President).

8. Finally, reference might be made to the Basic economic mission which is scheduled to begin its work in Peru in the week of March 15 and to our expectation that its report will help to assure a greater understanding of Peru's medium- and long-term plans and prospects by the Bank and, as well as other external lenders. (We expect that the report will provide a framework for the Consultative Group Meeting planned for late this year or early in 1977, and help in obtaining an increasing flow of external finance on longer terms to meet the priority needs of Peru's rapid economic and social development without over-burdening her debt servicing capacity).

Meeting with Prime Minister, General Fernandez Maldonado, and Cabinet Members Concerned with Economic Matters (Wednesday, March 3, 5:00 p.m.)

9. Your introductory statement might, as in the meeting with the President, include an expression of pleasure at the opportunity of viewing at first hand Peru's progress in recent years in attacking major social problems. You might then briefly summarize the Bank's current emphasis on aiding the developing countries in overcoming problems of urban and rural poverty.

10. With this introduction, you might indicate to the Prime Minister your interest in hearing from him and his colleagues about the Government's policies and programs for accelerating social and economic development while assuring financial stability.

11. During the course of the meeting you might cite the \$78.5 million Transandean Corridor loan approved last December and the \$36 million electricity loan scheduled for the Board March 2, as examples of the readiness of the Bank to help Peru and indicate that other projects are now at an advanced stage of consideration, e.g., for the sites and services project designed to assist Peru's outstanding program for aiding slum areas in Lima and Arequipa and for mining, agriculture and industry.

12. One or more of the ministers may make a request for the Bank to provide financing for large projects such as the Chimbote steel expansion scheme. Your response might be that we are planning to send a programming mission to Peru in late March and would be happy during the course of the work of this mission to consider with the Government the inclusion of these projects in our future lending program.

Meeting with Minister of Finance, Dr. L. Barua; President of Central Bank, Dr. C. Santistevan; and President of COFIDE, Mr. O. Espinosa (Wednesday, March 3, 11:00 a.m.)

13. This meeting could most usefully focus on outstanding fiscal and balance of payments problems as summarized in Tab F-3 and the further steps planned by the Government to overcome them. The status of plans to increase the general level of interest rates could also advantageously be covered (continuation of the relatively low real interest rates levels now in effect would make it difficult to proceed with the COFIDE and irrigation rehabilitation loans now under appraisal, as well as another agricultural credit loan in a year or two).

NOTE. A special agenda for this meeting will be proposed on the basis of discussions of Messrs. Lerdaun and Chaparro with Peruvian officials on March 1 and 2.

Meeting with COFIDE (Wednesday, March 3, 3:00 p.m.)

14. COFIDE is both a holding company for the principal government enterprises and the country's main project financing institution. You could mention that we are impressed with COFIDE's fast growth and with its dynamic and highly qualified staff. We thus are interested in working through COFIDE to support the development of the manufacturing sector. We could also work jointly with COFIDE in arranging financing for projects in the rest of the public sector.

15. Concerning the loan to COFIDE which we are now considering, you could mention to Mr. Espinosa that we are looking forward to supporting COFIDE'S efforts to improve the efficiency of the manufacturing sector, support the expansion of social property enterprises and promote export production. In this connection you might express hope that the Bank can be of assistance in developing techniques for selection of projects which utilize the country's resources more efficiently.

16. Although Mr. Espinosa will be present at the meeting with the Prime Minister, you may raise again the issue of interest rates. The issue does not affect our operation directly since subborrowers will pay an interest rate of 11-12% and also bear the foreign exchange risk, but we do consider it most important to reduce the negative spread of interest rates on local currency loans, both because they tend to distort investment decisions and because they discourage the mobilization of savings by financial intermediaries. You might mention that the Bank will find it increasingly difficult to justify lending to Peru if interest rates remain at levels which seriously jeopardize the mobilization of savings.

17. COFIDE is the Government's agent for raising financing abroad. Therefore, you might be asked whether the Bank would be willing to assist in large investment projects such as the Chimbote steel expansion scheme. In response you might indicate that the Bank would be glad to consider loans for such projects. However, we could only consider coverage of part of the external financing needed for a large project because of the substantial volume of lending already under consideration for Peru. It might be worth calling to Mr. Espinosa's attention that the Bank could work with COFIDE in mobilizing other sources of long-term finance for such projects. If COFIDE wishes to do so, this form of cooperation could be explored further during the visit of the programming mission planned for late March.

11

March 2, 1976

TO : Mr. Robert S. McNamara
From : E. Lerdau
Subj. Peruvian Economic Situation, Supplementary Briefing

The economic situation has deteriorated since our November mission, in spite of the fiscal and financial measures of September and January, related in the briefing paper.

The deterioration is primarily the result of the continuing lack of definition of the Government's priorities and objectives; this lack of definition in turn reflects the fact that the Government continues to be a coalition of centrist and radical leftist elements and that each of these have their own power base among the military. The President seems to feel compelled to satisfy both wings and, in pursuit of this goal has recently made a public attack on his "financial and economic advisors who are more reactionary than the reactionaries." Presumably the Minister of Finance and the President of the Central Bank were not excluded from this classification. Nevertheless, they seem to continue to have access to the President and, to a degree expect to be listened to.

The short term situation appears to be quite serious. Net foreign reserves are down to under \$50 million (8 days' imports at 1975 rates) and the foreign commercial banks appear to be increasingly concerned. The President appears to be influenced by the experience of the past two years when, because of the U.S. recession commercial banks were glad to find borrowers. He does not seem to be fully aware of the turnaround and of its impact. Indeed, he appears to have lost direct contact with short term economic management issues to a greater extent than was to be expected from a former Minister of Finance.

The conflicts within the Government also interfere with a solution of the fiscal problem. The financial authorities (Ministry of Finance, Central Bank, COFIDE) themselves seem fully convinced that public expenditures must be curtailed, but they do not have the last word on this. The Planning Institute seems more remote from these matters. The Ministry of Finance appears to be considering a new set of financial measures, but has no firm timetable for them. Moreover, these measures seem to be all revenue oriented, and the real problem now is on the expenditure side. Military expenditures in 1975, for instance, rose by over 70 per cent (42 per cent in real terms) and are now about 25 per cent of Central Government expenditures.

In general, the briefing paper numbers only understate the deterioration in 1975 slightly, but one has less of a conviction now that the excessively large external and fiscal gaps will be dealt with promptly. (Net capital inflows in 1975 were 11% of GDP, the consolidated public sector deficit on current account was 3.6% of GDP and the overall deficit of the public sector was 11.8% of GDP). The 1976 outlook is further worsened because the Cuacone copper project has slipped and will not come on stream

until some time in 1977.

Interest rates continue to be fixed at levels yielding strongly negative rates at Peruvian rates of inflation. Savers get from 7 to 10 % depending on the instrument, and industrial borrowers pay 10-14 %. Inflation last year was 22% and is not likely to be less in 1976. Already at the time of the Consultative Group meeting in April 1975, the Government declared its intention to review and raise these rates drastically in the near future; it has not yet acted.

Regarding the exchange rate there is some real doubt about the adequacy of the present rate (in force since last September) already, although the IMF takes the view that with the preponderance of state enterprises in the export sectors, a change in the rate would not affect exports much. I am inclined to disagree because loss-making public enterprises have to be financed from the budget or the Central Bank. Moreover, the socialized sector will ruin the economy unless it becomes profit conscious. Finally, even now there is scope for new private ventures going into profitable export lines, and an adequate incentive through the exchange rate is vital for this.

Of equal or greater concern than the above are the medium term implications of recent legislation affecting the operating capabilities of the public sector. In January, salary ceilings of 70 000 soles per month (U.S. \$ 1 800) were imposed for all public sector employees -for reasons of equalitarian ideology- and it is clear that the major state enterprises (petroleum, steel, mining) will not be able to retain their higher level technical personnel, let alone expand it, unless they are exempted from these rules. (We have already communicated informally to the Government that we do not expect to bring the Centromin loan to the Board, until we are informed how the enterprise will be protected. We became aware of the scope of the legislation during the recent negotiations of this loan, which were otherwise completed successfully). This legislation has to be seen in the context of a complex and volatile general labor situation; especially in the public enterprises are strikes and featherbedding a serious problem, which is connected in turn with the political affiliations and objectives of some of the unions.

All the above leads me to the conclusion that in your discussions with the Minister of Finance and the President you should voice concerns rather less muted than suggested in the Briefing Paper. The Minister has conveyed to us that he would welcome this and that he hopes that you will be equally candid with the President. I suggest that the following point be stressed, in addition to the more positive ones mentioned in the Briefing Paper :

- (1) The external constraints; the difficulties Peru will have to persuade creditors to maintain and expand their involvement in Peru given :
 - (a) the changing external environment;
 - (b) lack of evidence of financial control;
 - (c) lack of evidence of production and export orientation.
- (2) On the last point above : stress the need for efficiency of the public enterprises (present large loss makers are the petroleum, steel and fishing enterprises and the food trading firm)

and cite the salary legislation as a major example of the need for an orientation towards efficiency which it would be fatal to sacrifice for some symbolic equalitarian measures. (The cost and fiscal impact of the higher salaries is totally negligible).

(3) Interest rate issue.

(4) Exchange rate issue in terms of development of new exports and of tourism. Peru has become extraordinarily expensive for tourists, ~~and~~

October 21, 1974

PERU - COUNTRY PROGRAM PAPER

		IBRD/IDA Lending Program (Current US\$ millions)		
		<u>FY69-73</u>	<u>FY74-78</u>	<u>FY76-80</u>
1973 Population: 14.5 million	IBRD	30	535	600
1972 GNP per capita: \$520 ^{1/}	IDA	-	-	-
Current Population Growth Rate: 2.9 percent per annum				
Current Exchange Rate: US\$1 = S/.38.70				
	Total	<u>30</u>	<u>535</u> ^{2/}	<u>600</u>
	Operations Program			<u>780</u>
		<u>Ann. Avg. Per Cap., cur \$ (const. \$)</u>		
	IBRD/IDA	0.44 (0.61)	6.70 (5.60)	<u>7.14</u> (5.31)
	IDA	- (-)	- (-)	- (-)

A. INTRODUCTION

1. The last CPP was reviewed by Mr. McNamara on June 8, 1973. The last economic report (136-PE) was distributed to the Board on May 10, 1973. A new updating economic report is now being finalized and should be distributed to the Board before the end of CY74.

Recent Political Developments

2. No significant change has taken place in the general political situation in Peru since the last CPP. While apparently the Government continues to have broad national acceptance, it has not yet succeeded in building up active popular support in spite of the various economic and social reforms implemented. Strikes in the mining and industrial sectors continued in 1974, in part due to the tense relations between the Government and the labor unions. Last July, the Government took over the daily newspapers and distributed their management among important social groups of the country. Although the Government justified this move as a means of democratizing the press, it did cause strong negative reactions and did not help to improve the prevailing uncertainty within the private sector. The settlement of the investment disputes with the U.S. has been well received and

^{1/} World Bank Atlas, 1974.

^{2/} The proposed FY75-79 lending program compares with the program for the same period agreed upon during the revision of the Bank-wide lending program -- and shown in P&B Standard Table IV -- as follows:

	<u>FY75-79 Lending Program</u>		<u>Percentage Change</u>
	<u>Std. Table IV.</u>	<u>Prpsd.</u>	<u>(Prpsd. & Apprvd.)</u>
Current \$ millions	705	600	-15
Constant \$ millions	540	468	-13
Per Capita p.a. (Constant \$)	6.63	5.74	-13

increased Peruvian expectations of more long-term external financial assistance. It has also improved the atmosphere regarding private foreign investment.

Recent Economic Developments

3. GDP grew by an estimated 5.8 percent in 1973. Agricultural output growth of 2.4 percent, though higher than in the last three years, was still below the rate of population growth. The 7 percent increase in industrial output was lower than in previous years. Mineral production expanded only by 2 percent, a drop in iron ore offsetting a somewhat larger output increase of non-ferrous metals.

4. The process of structural and institutional reforms analyzed in last year's CPP has continued. The land reform in the coastal areas is much advanced and although little has yet been achieved in improving the lot of the highland peasants, efforts to organize production cooperatives are being accelerated. At the same time, the project generation capacity of the public sector has improved and PETROPERU has successfully accelerated the rate of petroleum exploration. The largest mining complex and the fishmeal industry were nationalized during the last year and are now run by new autonomous public sector institutions. The excess capacity of the fishmeal industry is being drastically reduced and efficiency increased. Also in the field of industry most enterprises have complied with the Industrial Community legislation--which provides for a gradual participation in the ownership of the enterprise. By the beginning of this year the average participation of workers in equity reached 8 percent, although there were wide variations among firms.^{1/} More recently a new Social Property Law was approved aimed at promoting new industrial and entrepreneurial capacity within a system of self-management by the employees.

5. The large changes during the last year of international prices of commodities and capital have seriously complicated the management of Peru's economy. To a large extent as a result of increased import prices, inflation has accelerated markedly. The Consumer Price Index for Lima which rose an average of 6.3 percent during 1969-72 increased 17 percent in the July 1973-July 1974 period. To minimize the impact of inflation on the consumption patterns of urban families, the Government has been subsidizing heavily the prices of petroleum, foodstuffs and public services.^{2/} This in turn has put a heavy burden on the Central Government finances and reduced the savings of some large public enterprises such as PETROPERU.

6. During 1973 and probably 1974, however, Peru has sharply increased the level of net external borrowing and has achieved gains from terms of trade. The drastic increase in prices of petroleum and other basic commodity imports has been more than offset by the rising world prices of Peruvian exports (especially minerals). However, a large import volume expansion resulted in 1973 in the first trade deficit in many years; this will probably be repeated in this year.

^{1/} It is worthwhile noting that although the scheme to increase workers participation was a positive step in redistributing wealth, it is having a negative effect on jobs creation, because of the reluctance of workers to dilute ownership through increased employment.

^{2/} The commodities whose prices are controlled have a large weight in the price index, thus the recorded rate of inflation would have been much higher without the Government's subsidy.

Following the 1972 and 1973 Consultative Group meetings around \$400 million of long-term development loans from governments and international agencies have been contracted during the last two years. In addition, the Government has continued contracting non-project loans from commercial banks (mostly in the Eurodollar market). These loans were used to finance almost half of the foreign amortizations payments due and helped finance the fiscal deficits. Although the maturity structure of the debt has somewhat improved, interest payments are increasing sharply in 1973-74 with rising Eurodollar rates. This non-project borrowing appears justified as a means for bridging Peru's resource gap until mineral and possibly petroleum exports expand substantially starting in 1977-78. However, external borrowing is being increasingly used as a substitute for a greater effort at domestic resource mobilization to finance the fiscal deficit.

7. The poor performance of public finances has become in the last two years a matter of serious concern. Central Government revenues continued to grow less rapidly in 1973 than GDP and at about half the growth of current expenditures, resulting in a small current account deficit in contrast with the substantial current surplus registered in 1970-72. Though capital expenditures increased moderately --11 percent-- the 1973 Central Government's overall deficit almost doubled to 4 percent of GDP. The estimates for 1974 show a similar picture. In spite of considerable restraint in salary increases and purchases of goods and services, Central Government current account savings are expected to remain negligible, mainly because of the fast rise in interest payments and current transfers (mostly subsidies on petroleum and foodstuffs). Assuming around a 5.5 percent increase in capital expenditures (at 1973 prices), the overall fiscal deficit this year may remain at around 4 percent of GDP.

B. COUNTRY OBJECTIVES AND PROSPECTS

Development Strategy

8. The military government that took power in Peru in October 1968 has adopted an approach to development in which economic growth is directly linked to a transformation of the society to achieve broader popular participation in the country's economic, social and political life. Among other things, this should imply drawing the "forgotten" rural poor into the modern development process, improving the distribution of income and wealth, and increasing the participation of Peruvians in the ownership and management of the economy. Since the Government attributes much of the limitations of the past development to the dominance of unregulated private enterprise in general and to the excessive weight of foreign interests in particular, its strategy assigns to the State an active and much increased role in the economy. The key elements of the development strategy adopted could be summarized as consisting of (a) expanding the economic role of the State by increasing its direct participation in developing and exploiting the country's basic productive resources and marketing its main export products; (b) carrying out structural reforms in agriculture and industry aimed at achieving a broader distribution of wealth and incomes; and (c) decentralizing economic activity away from the Lima Metropolitan area. The

expansion of the direct role of the State in the control and management of the country's basic productive resources has been sought through the creation of public enterprises in all major productive and service sectors, on the one hand, and the control of foreign and domestic investment in industry and public utilities on the other. Redistributive policies have found expression in the deepening and acceleration of the agrarian reform and in reforms in the structure of enterprises providing for the participation of employees in their profits and management and the gradual acquisition of part of their capital. Much progress has been made in the course of the last four years in implementing many of the components of the Government's strategy.

Major Constraints and Prospects

9. In general, Peru's ability to continue achieving the ambitious goals of maintaining satisfactory average per capita income growth while further implementing the deep socio-economic structural reforms within a stable financial environment, will mainly depend on the solution of three interrelated issues:

- (a) rapidly increasing the level of investment and savings;
- (b) raising the rate of growth of agricultural output, especially food; and
- (c) expanding exports (especially minerals and manufacturing) necessary to finance the large import requirements.

10. The most urgent issue that confronts Peru is raising the level of investment and savings. In part because of low investment, export volume has stagnated, agricultural output has failed to keep pace with population growth and at least in some manufacturing branches demand may be outstripping possible supply with the present installed capacity. The 1974-76 period will place particular strain on the country's internal and external finances. Because of the long gestation and construction period required to expand mining and petroleum, even if the major investment projects now in the pipeline are swiftly implemented, a substantial expansion of output and export volume will not be achieved before 1977. Furthermore, requirements for better physical infrastructure are acute. Therefore, the investment-output ratio is expected to rise rapidly in the next few years. Thus, to finance the very high levels of capital import requirements expected, reduce the presently growing internal inflationary pressures and not mortgage excessively future incomes with present consumption through heavy external borrowing, a major increase in the national savings rate will have to be achieved.

ECONOMIC AND SOCIAL OBJECTIVES (1978)^{1/}

	Unit	Current Level		Bank Projection	
		Actual	Estimated	Absolute	Growth Rate
		1970	1973	1978	1973-78
GNP (constant 1970 prices)	US\$ million	6010	7139	9612	6.1
Population	millions	13.6	14.9	17.2	2.9
GNP per capita	US\$	441	479	559	3.2
Employment percent of labor force	percent				
Investment (constant 1970 prices)	US\$ million	744	1016	1805	12.2
National savings (constant 1970 prices) ^{2/}	" "	1000	1024	1640	9.7
Exports of goods and NFS (current prices)	" "	1224	1342	3860	23.5
Imports of goods and NFS (current prices)	" "	972	1381	3717	22.0
Net capital inflow	" "	55	194	477	19.7
Debt service ratio ^{3/}	percent	17.3	23.6	15.5	
p.c. calorie supply as percentage of requirements	"	88	n.a.	n.a.	n.a.
Adult literacy rate	"	72	n.a.	n.a.	n.a.

- 1/ No country projections available.
 2/ Takes into account income effect from terms of trade change.
 3/ Debt service on public external debt repayable in foreign currency.

11. The recent and expected behavior of the main economic aggregates is summarized in the above table and presented in greater detail in Attachments S1 and S2. Our projections suggest that an annual rate of real GDP growth of 6-7 percent can be attained only if investment grows at least at twice that rate. The rapid growth of investment required reflects the low rates of the past several years (when investment averaged 13 percent of GDP), the very high level of investment required by the petroleum exploration and the oil pipeline, and the bulkiness of large mining projects such as the Cuacone copper mine and the refineries of lead, copper and zinc (see para 18). To finance the large increment of investment targeted will require a marginal rate of national savings in excess of 25 percent in the 1974-78 period. The savings target implies reducing the annual rate of growth of consumption from 7.5 percent in 1970-73 to around 5 percent in 1974-78; this would still allow a yearly 2 percent per capita increase in real terms.

12. Restricting the growth of consumption demand to achieve the savings target is also consistent with the objective of maintaining internal and external financial stability. Import capacity growth in 1974-76 will be constrained by the low increase expected in export volume, while the high level of investment targeted will sharply raise capital import requirements. Thus, to minimize the loss in reserves in the next three years (without incurring excessive foreign borrowing) the growth of other imports will have to be

compressed. At the same time, to minimize the compounding effect of domestic demand pull on imported cost push inflation, a strict control of growth of domestic consumption is also required. In more general terms, to ensure that the distributive policies of the Government are implemented in an environment of expanding aggregate output, greater priority will have to be given to savings mobilizing policies that allow a higher investment rate.

13. During the last few years direct participation of the State in the ownership and operation of the economy has become pervasive, and therefore the ability of the public sector to generate enough savings to finance the investment required for satisfactory growth has become a decisive factor for assessing the economy's overall prospects. The Government's basic strategy of expanding the direct role of the State in the economy has made substantial progress in the last few years and, consequently, both current and capital expenditures have risen sharply, reflecting the expansion of the public sector machinery and the need to provide for the initial and continuing capitalization of most of the newly created public enterprises. The investment capability of both the Central Government and of the public enterprises has also improved in the last two years and thus the need to generate additional public savings has become even more acute. The need for larger savings in the public sector is so much the greater because the importance of the private sector in the economy has diminished in relative terms and private sector investment has expanded slowly reflecting a feeling of uncertainty concerning government policies.

14. The poor performance of Peru's public finances, which had become increasingly apparent since 1972, largely reflects the structural deficiencies of the tax system. Moreover, in spite of the expansion of Government activities the tax burden remains low, at less than 14 percent of GDP. The problem has been aggravated by the sharp rise in commodity prices, which has greatly increased the volume of subsidies, and by the steep increase in debt service payments, particularly interest payments, resulting from the Government's heavy external borrowing; debt service accounted for about 30 percent of Central Government revenues in 1973. The public sector projections (Table below and Attachment S1) indicate that public sector fixed investment in 1974-76 would on the average triple the 1970-73 level. At the same time the share of public fixed investment financed by public savings would fall from almost 65 percent in 1970-73 to less than 40 percent during 1974-76. Clearly raising public savings substantially is a most urgent need if the public investment program is to be carried out without strong inflationary effects and a deteriorating debt picture.

PUBLIC SECTOR FINANCES, 1973-76
(billions of current soles)

	<u>Est.</u> <u>1973</u>	<u>Projected</u>	
		<u>1974</u>	<u>1975-76</u>
<u>Central Government</u>			
Savings	1	5	7
Capital expenditures (fixed capital formation)	16 (9)	19 (11)	60 (33)
Overall balance	-15	-14	-53
<u>Public Enterprises and Social Security</u>			
Own savings generated	2	1	6
Central Government transfers (net)	3	5	19
Capital expenditures (fixed capital formation)	10 (9)	20 (20)	43 (42)
Overall balance	-5	-14	-18
<u>Consolidated Public Sector</u>			
Overall balance	-20	-28	-71
Foreign financing, net ^{1/}	13	17	23
Domestic financing, net	7	11	22
Unfinanced gap	-	-	-25

1/ For 1975-76 includes only project related borrowing.

Source: IBRD estimates.

15. The Peruvian Government shares our concern on the seriousness of the low public sector savings issue. The Ministry of Finance last August presented to the Council of Ministers estimates for the 1975-76 biannual budget which indicated that an unfinanced gap of almost S/.20 billion for the two-year period (or nearly 10 percent of total expenditures) would remain after taking into account expected levels of foreign project borrowing, \$150 million of non-project foreign borrowing (around S/.5.8 billion) and reasonable levels of domestic borrowing. These estimates were similar to indicative to Bank projections shown

in the Table above. The Finance Minister proposed a series of revenue measures to finance this gap. The President decided, however, to give priority to reductions in expenditures and the Finance Minister indicated at the Annual Meeting that major cutbacks are now being planned in projected expenditures in the 1975-76 biannual budget. He also referred to several revenue measures which are still planned and expected to generate S/.7-8 billion of additional revenues during the biennium. He did not, however, give current estimates regarding targets for the expenditures and revenues in the budget and, instead, suggested that a mission visit Peru in early December to obtain this information. At that time we plan to review the feasibility of restraining expenditures within the budgetary limits, taking into account the prospect that the Peruvian price level will continue to increase by at least 15 percent annually, and the adequacy of the planned revenue measures.

C. EXPORT PROSPECTS AND EXTERNAL CAPITAL REQUIREMENTS

16. The next three years will be a difficult period for Peru's balance of payments, although the long-term prospects are good. While import requirements will be large because of the high level of investment expected, export volume (mainly in mining and petroleum) is projected to expand little and debt service will rise rapidly. In spite of large capital inflows, international reserves, which amounted to almost \$410 million at the end of 1973, can be expected to be under pressure. The magnitude of the pressure on reserves will depend partly on the success of government policies aimed at compressing non-essential imports and increasing savings, and partly on the availability of foreign loans. As the investment of 1973-76 starts to generate a large rise in exports after 1977, the international reserve position should improve, although Peru will most likely remain dependent on large inflows of capital at concessionary terms at least until the mid-1980's. In sum, the immediate balance of payments issue is how to finance investment without incurring excessive amounts of debt that would mortgage too much the future benefits of the large growth of exports expected after 1976.

17. During 1974-76 export value will be mainly determined by prices. Only fishmeal and non-traditional exports are expected to achieve any substantial increase in volume. During 1974, the anchovy catch has gradually recuperated and at least three million tons are expected to be fished. Although it is still very uncertain how much more the anchovy catch will be able to expand, there is a consensus in Peru that it will not reach the extremely high levels of 1970-71. The mission has projected a gradual growth of anchovy catch from three million tons in calendar year 1974 to six million tons by calendar year 1980. This should allow fishmeal exports to total over 600,000 tons in 1974 and 1.2 million tons by 1980. Non-traditional exports are expected to continue growing rapidly in the next few years. Furthermore, world commodity price developments are expected to favor Peruvian exports in 1974. The extremely high prices of minerals which prevailed in the first months of this year should allow the average prices for the year to be well above 1973, even if prices remain at the present low level for the rest of the year. The balance of payments projections (Attachment S2)

are on the basis that average prices of Peru's exports will rise by over 30 percent in 1974. During 1975-76 prices are projected to remain at the same level of 1974 or fall; in real terms most export prices are expected to fall.

18. The large expansion of exports after 1977 will mainly depend on the completion of a series of mining projects and on the success of petroleum explorations. The main mining projects are:

- (a) the refineries of copper, zinc and lead. These refineries, now under construction, are expected to produce yearly 150,000 tons of refined copper, 80,000 tons of refined zinc and 180,000 tons of refined lead by 1977-78. Although these projects will not expand volume of mineral production, they will increase markedly the domestic value added and export value.
- (b) the Cuajone and Toquepala copper mining project. The project consists of the development of a mine and a smelter capable of producing 170,000 tons of blister copper by 1977 at a total cost of almost \$650 million. Construction is already well underway while the financial package was recently completed. IFC participated with a loan of \$15 million. The net foreign exchange earnings should rise from \$90 million in 1977 to \$150 million in 1982.

19. The magnitude of Peru's petroleum reserves will be better known at the end of this year. Both PETROPERU and the foreign oil companies with concessions in the Amazon basin are now in the drilling phase of their explorations. Although the geological studies suggested the existence of a sizeable amount of petroleum reserves, only after a large number of wells have been drilled can a more certain judgment be made. Based on the level of reserves already discovered, it is estimated that the production level may reach a maximum of 210,000 barrels daily by 1978. This would allow the country to become self-sufficient in 1977, thus saving around \$150 million and, in addition, have net exports of some \$120 million in 1977 and \$230 million in 1978. If present reserves in the Amazon basin areas are increased three-fold, the country's production could reach 290,000 barrels daily by 1978. In this optimistic case, taking into account the foreign exchange saved by not importing petroleum, the total balance of payments' impact may reach \$320 million in 1977 and \$680 million in 1978. 1/

20. Given the large import requirements of capital goods and the still considerable petroleum imports, the trade deficit is expected to widen during 1974-76, even assuming that imports of non-essential goods can be compressed and that volume of food imports does not expand at more than 3 percent yearly. In addition, the balance on services is likely to show rising deficits mainly on account of higher interest payments on public debt, and increasing profit-remittances following the growing value of mineral exports. Hence, the current account deficit is expected to rise from \$156 million in 1973 to over \$580 million in 1976.

1/ The projections in Attachment S2 assume the first alternative of net exports of \$120 million in 1977 and \$230 million in 1978.

21. Gross capital requirements (i.e., including amortization but excluding prepayment of loans) are expected to total over \$2,200 million in the 1974-76 period. New private foreign direct investment is expected to more than double in 1974-76 mainly owing to petroleum explorations and the Cuajone Copper Project. During 1974, however, the foreign disinvestment caused by the rationalization of the Cerro de Pasco mines and other foreign owned assets will depress net private sector capital inflows.

22. Gross disbursements of foreign loans to the public sector will have to total over \$2,000 million during 1974-76 (or an average of over \$650 million per year compared to \$520 million in 1973) to ensure that net international reserves remain at no less than 1-1/2 months of imports. Disbursements of project loans should total \$1,450 million (of which \$500 million can be drawn from the undisbursed balances of loans signed by the end of 1973). Of this total around \$800 million are expected to be absorbed by the oil pipeline, petroleum exploration and mining development. More than \$400 million of financing for the oil pipeline is at the final stage of negotiations, mainly with Japan. Around \$550 million of non-project borrowing would be required, of which around \$250 million have already been contracted in 1974. ^{1/} Of course, to the extent that the level of reserves is allowed to be drawn below 1-1/2 months of imports, gross annual capital requirements may be reduced through 1976.

23. In 1977 the combined impact of the Cuajone Copper Project and net petroleum exports should increase exports sharply and allow a contraction of the current account deficit. However, unless new major additional petroleum reserves are found, Peru will remain a net capital importer. Our projections suggest that to maintain a 7 percent annual real GDP growth rate and a sustained level of investment, gross disbursements of loans to the public sector will have to average \$750 million a year during 1977-80. Even with this level of capital inflows, the coverage by net international reserves of imports will remain below three months by 1980.

PROJECTED PUBLIC SECTOR BORROWING, 1973-80 ^{1/}

	1973	Annual Averages	
		1974-76	1977-80
<u>Commitments</u>	<u>573</u>	<u>707</u>	<u>914</u>
IBRD	49	98	116
Other official sources	144	194	262
Commercial banks and suppliers	380	456	536
<u>Disbursements</u>	<u>518</u>	<u>653</u>	<u>762</u>
IBRD	9	26	91
Other official sources	132	131	151
Commercial banks and suppliers	377	496	520

^{1/} Excludes (i) borrowing used for prepayment of other loans, and (ii) the unclassified debt. Both are included in Attachment S2.

Source: IBRD estimates.

^{1/} Net of borrowing for prepayment of loans.

24. To achieve the required level of disbursements projected in the above paragraphs, foreign loan commitments should average annually over \$700 million in 1974-76 and \$900 million in 1977-80. As in the past few years, the predominant source of future commitments are expected to be commercial banks and suppliers. The Peruvian Government is now negotiating the possibility of assistance from Venezuela and Iran. Assistance from these or other petroleum exporters and/or more support from official lending agencies may become necessary should the present tight conditions prevailing in the international capital markets continue much longer. The Japanese Government is now making a \$330 million loan to Peru for the pipeline construction and petroleum exploration, and is actively involved in the preparation of some mining projects. The lending programs of the other official lending agencies based in Washington are not yet well defined. USAID is now in the final negotiations for a \$10 million loan to support the development of small scale industries. For the future, besides continuing technical assistance programs, USAID tentatively plans to lend around \$15 million yearly, directed mainly to the agricultural sector. IDB has already made two loans this year for urban water supply (\$4.7 million) and tourism (\$29.3 million), and may approve an additional loan for a water supply scheme for medium-sized cities before the end of the year. IDB's future plans are still in the process of internal discussion, but a tentative level of \$60 to \$70 million per year is being considered, mostly for power (Macchu-Picchu and Sheque projects), agricultural credit and irrigation, regional development in the Southern Sierra, and industry (cement).

25. With the high level of commitments required to achieve a sufficient capital inflow over the next years, external debt outstanding (excluding undisbursed) is projected to triple between the end of 1973 and 1980. However, expressed as a share of export earnings, the debt service should fall from almost 24 percent in 1973 to 17 percent in 1974-75 and remain at 15-16 percent for the rest of the decade.

26. In sum, while immediate additional fiscal measures are needed to ensure the financing of the public investment program during 1974-76 and prevent the interruption of Peru's development program, our projections indicate substantial improvement both in the balance of payments and public finances towards the end of the decade. These would result from the substantial increase in mineral exports from the Cuacone and Cerro Verde copper projects, the increase in the proportion of refined copper and zinc exported and the expected development of petroleum, as well as from the gradual recovery of fishmeal and fishoil exports. These developments would substantially boost both foreign exchange earnings and fiscal revenues. If the authorities are able to keep current expenditure growth under control, national savings could appreciably increase, reaching about 17 percent of GDP in 1978, compared to about 13 percent estimated for the current year.

D. BANK LENDING STRATEGY

27. The proposed program is geared to assisting the Government in achieving its objectives of expanding production in key economic sectors and implementing structural and institutional reforms, which will provide a framework for future growth and for a broad distribution of the benefits of development. Specifically, the strategy of the lending program is aimed at aiding in:

- (a) the expansion of production and productive capacity in crucial sectors such as mining, agriculture and industry;
- (b) the creation of a physical and social infrastructure in such sectors as transport, power, and education capable of sustaining and fostering the positive evolution of the nation's productive capacity; and
- (c) the consolidation of structural and institutional reforms which will help in the socio-economic transformation now underway.

At the same time, we hope to be a catalyst of new sources of funds for major investment projects, particularly in the mining sector.

28. Under the program, as projected in Attachment 1, Bank lending to Peru would increase from the actual level of \$75 million in FY74 to an annual average of \$114 million for FY75-80. At 1974 prices average annual lending for the period would only increase to \$87 million. The level of lending planned peaks in FY78 and declines sharply in FY80. This plan has been made under the assumption that oil revenues will become significant in the early 1980's and that the need for external capital at concessionary terms would then be considerably reduced. The projected lending program, together with undisbursed balances under outstanding loans, will result in disbursements of about \$380 million during the six-year period, which would represent less than 10 percent of total gross disbursements under foreign loans to Peru. Debt service to the Bank as a share of total public sector debt service, which was 5.2 percent in 1973, should remain at no more than 5 percent during the rest of the decade.

29. This recommended lending program rests on the assumption that measures to deal with the fiscal problem described earlier in this document are taken by the end of 1974. As indicated in paragraph 15 we plan to review in early December the Government's fiscal program for 1975-76. The results of the review will be summarized in a memorandum to Management supplementing this CPP, making recommendations on any changes which may be called for in our lending program for Peru, as well as on our position in the next Consultative Group Meeting.

30. Under our current operations program for Peru, 28 percent of our loans would be in the field of agriculture, a substantially higher portion than foreseen in the last CPP, as indicated in the following table:

Sector	1974-78 as in last CPP		1975-80 Proposed	
	\$million	%	\$million	%
Agriculture	120	20	245	28
Transportation	165	28	160	18
Industry ^{1/}	90	15	100	12
Mining	80	14	150	17
Power	60	11	100	12
Education	49	8	70	8
Sites and Services	-	-	40	5
Unallocated	25	4	-	-
TOTAL	589	100	865	100

^{1/} Includes DFC's.

E. BANK PROGRAM

31. Peru's agricultural problem has been brought increasingly into focus during the past two years with a steep increase in the food import bill and the increasing burden of food subsidies on fiscal revenues. Growing food imports reflect the basic deficiencies of the agricultural sector and the low elasticity of domestic production to increased demand arising from population growth, urbanization and rising incomes. The inelasticity of domestic food supplies is to a large extent due to several structural and long-standing deficiencies, particularly a limited agricultural land base and difficult topography and soil conditions which, together with variable climatic conditions and deficient physical infrastructure, make the expansion of production in general extremely costly. Moreover, up to the advent of effective agrarian reform, which was initiated by the present Government in 1969, the distribution of farm land was very uneven with widespread minifundia and unstable forms of land tenure.

32. Given these conditions, the problems of Peru's agriculture need to be faced with two quite distinct objectives in mind: on the one hand, the alleviation of structural deficiencies and, on the other, the urgent need to rapidly increase output, particularly of food. Unless the long-standing neglect and backwardness of traditional agriculture are corrected, there cannot be any hope of appreciably reducing the poverty of the rural population.

33. The expanded lending now planned for agriculture would:

- (a) help increase food production as rapidly as feasible in order to alleviate the pressure of increasing food imports on the balance of payments; and
- (b) help develop depressed rural areas.

The backbone of the proposed lending program for agriculture consists of three irrigation rehabilitation projects to expand production on good agricultural lands in a relatively short period at a modest cost, and of three rural development projects with emphasis on improving the standard of living of three depressed areas through a multisectoral approach providing infrastructure, technical assistance, credit, improved seeds, fertilizers and marketing facilities. The irrigation rehabilitation project proposed for FY76 is already being prepared with the assistance of FAO and no major difficulties are anticipated. Arrangements for the preparation of the initial rural development project -- in Cajamarca -- are now being worked out and current prospects are that project preparation and the appraisal process will be completed for a loan in FY77. The program envisaged for the rest of the period also includes further loans to the Banco de Fomento Agropecuario (BFA) and a forestry development project in the Pucallpa area which would be served by past and proposed Bank transport projects.

34. Peru's transport system reflects the staggering topographic conditions and the economic geography of the country. The present system is reasonably adequate for the needs of the coastal region where most of the economic activity takes place, but it is inadequate for the development needs of the Andes and the Amazon basin. During the next few years the expansion of economic activity will create a greater demand for road transport. The current Government sector strategy is to be quite selective in its investment plans in the short-run, concentrating on providing facilities needed to expand economic activity in key sectors, such as to open new agricultural areas or permit increased output in industry and mining. Bank lending in transportation is designed to help carry out the Government's strategy and to strengthen institutions and improve road maintenance and transport planning through technical assistance. The Transandean Corridor project, which is proposed for FY75, includes the last works needed in the Lima-Pucallpa road for which the Bank has made three loans in the past, and the construction and/or improvement of the river ports in the Amazon basin area being opened up by this road. The ocean ports project, proposed for FY76, would provide financing for the expansion of capacity required to accommodate the increased traffic in Chimbote to be generated by the planned iron and steel works expansion. Once the highway investments being financed under our 1971, 1974, and the proposed 1975 loans are completed or near completion, a highway project consisting in the reconstruction and improvement of a road to support the development of the central region, to which the Government attaches a high priority, is proposed for FY78 and a further highway loan is proposed for FY79. Given the extremely difficult topography of Peru and the key role of air transport, an aviation loan is also foreseen for FY77 to facilitate domestic traffic and national integration.

35. Peru's known mineral resources are abundant and the long-term price outlook is favorable. Structural and institutional reforms in this sector have been aimed at expanding the role of the public sector by nationalization and by taking part in major projects in the form of joint ventures in order to expand mineral production and its processing. Bank assistance in this sector can be instrumental in mobilizing external technical and financial support to

exploit the known deposits and strengthen the enterprises involved. Initial Bank involvement would be with Centromin-Peru, the former Cerro de Pasco, which was nationalized in late 1973. The company has remained administratively strong and is planning an expansion program in the next few years which can be carried out without major delays. The primary consideration here is to expand output quickly. Projects under consideration by Centromin-Peru include expanding copper mining and refining capacity, expansion of the zinc refinery at La Oroya and the construction of a new lead refinery. The proposed amount of the loans to Centromin (\$100 million) will only cover a part of the foreign exchange component and has been estimated on the basis that joint or parallel financing arrangements will be worked out. As staff work proceeds on our lending to Centromin, we are starting to explore with Minero-Peru -- the other state mining enterprise -- the identification of a project for an initial loan which is currently envisaged for 1980. Minero-Peru is a new company which is planning a very ambitious investment program but has a weak organization and executing capacity. In this sector IFC has recently made a \$15 million loan to Southern Peru Co. for the \$650 million Cuajone copper mining project.

36. Bank assistance in the industrial sector would be channelled through COFIDE, the recently established state development finance company which is the main source of financing resources for public and mixed enterprises, the designated financial intermediary for the social property sector enterprises and a potentially important source of finance for the private industrial sector. Strengthening this institution might be a meaningful assistance to the process of establishing the new economic order in industry and will contribute to the establishment of viable enterprises in the social property and public sectors of industry. Bank loans to COFIDE would also provide us with a good opportunity to discuss with the Government those industrial policies, within the context of the basic structural reforms, where we believe or hope a fruitful dialogue may emerge. Uncertainties regarding the future of the private sector have led so far to low levels of commitments of new risk capital by the private sector. At the same time, however, due to the reluctance of the sector to distribute profits in order to postpone employee ownership under the industrial community system and to the strong incentives to reinvest profits as a means of avoiding taxes under existing Peruvian legislation, private investment as a whole has picked up considerably in 1973. The current private sector expansion is being partially financed by borrowing from foreign sources at onerous terms (principally the Eurodollar market). Our present plan is for the initial loan to help foster the role assigned to the private sector, as well as meet the needs of the social property and public sectors enterprises -- if necessary through the establishment of quotas for each sector within the total amount of the loan. Repeater operations every two years are also envisaged to ensure, through a continuing relationship, the institutional impact of our assistance.

37. The development of the power sector in Peru was characterized by its fragmentation as numerous entities were formed gradually to meet public and private needs in various parts of the country. The basic objective of the

Government in the sector is to achieve the integration of the numerous systems into a single interconnected network that provides the basis for future coordinated power development and improved efficiency of operations. Basic legislation to that effect has already been issued and a state enterprise --ELECTROPERU-- has been established to implement it. The general electricity law which is supposed to formulate the details of the basic sector legislation, including a unified national power tariff, is still pending and expected to be published by the end of 1974. In the short-run Bank lending to this sector would consist first of financing a badly needed project of Empresas Electricas Asociadas (EEA) to expand distribution systems serving the Lima area. This project was appraised in April 1973 but our proceeding with a loan has been deferred pending the refinancing of EEA's short-term debt and a power tariff increase. Refinancing of EEA's debt has now taken place and power tariffs are expected to be reviewed in October 1974. Current prospects are that the rate action would be taken in advance of final approval of the new basic power sector legislation thus permitting us to consider this project. In the future, the program would aim at helping the Government to achieve its objective of an integrated power system and to assist ELECTROPERU in becoming an effective public utility enterprise responsible for the development of the sector by helping finance some of its projects. A first loan to ELECTROPERU of about \$35 million is programmed in FY76, and a further loan for FY78. Currently, it is expected that the first loan will be made to cover part of the foreign exchange cost of the power generation component of the multipurpose Sheque project and that parallel financing will be provided from other sources including IDB.

38. Education is another sector of the economy where the Government is implementing a major reform aimed at establishing an educational system more suitable to the country's economic needs and which provides more educational opportunities outside Lima. The reform involves substantial institutional changes in administration, curricula, teacher training and rural education. As in the case with structural reforms in other sectors, some important aspects concerning the change in the educational system remain to be worked out. Nevertheless, Bank assistance can be important in terms of carrying out those aspects of the reform which are being implemented and assisting the Government with those which have to be clarified. Such assistance has been initiated with a first education loan in FY74 and continuing support in this area is being envisaged through two more loans in FY77 and FY80, which we expect will be directed to rural education, although other priority needs may also be identified with additional sector work to be done next year in the context of the basic economic mission.

39. One important development problem to which the Peruvian authorities have addressed themselves is that of rapid urbanization. The rural population migrating from the subsistence economy of the highlands to the urban centers of the coast has posed a major problem to the orderly growth of the cities and has created undesirable social consequences. The Government has made commendable efforts to attack this problem by providing basic services and utilities to the new urban settlements in the outskirts of the major cities ("pueblos juvenes")

and by encouraging efforts of the new communities to improve their standards of living and take advantage of the technical services, credit and other facilities made available to them. The magnitude of the problem, however, has proven that the present governmental schemes are insufficient, greater inter-departmental coordination is needed, and that perhaps more innovative solutions ought to be sought and carried out. This is a field in which the Bank could assist both in financing and designing suitable sites and services projects to alleviate directly the inequalities of income distribution in the urban centers. They would be complementary to the efforts being made in the rural areas. We plan to initiate discussions with the Government shortly relating to the preparation of the initial sites and services project envisaged for FY77. A repeater operation is also planned for FY79.

F. CONCLUSIONS AND RECOMMENDATIONS

40. During the last two years the Government has continued to implement the important economic and social reforms initiated in 1968 and economic growth has remained satisfactory. Further progress has been made in strengthening the public administration and improving the tools for economic management. The resolution of the investment disputes has created a better climate for foreign investment and official external lending, while the completion of major mining projects in 1976-77 and the promising petroleum prospects should allow Peru to have a stronger balance of payments position in the early part of the eighties. The Peruvian Government is now preparing a development plan for 1975-78 that will consolidate the reforms implemented while concentrating on expanding mining, industry and agriculture. These commendable long-term development objectives deserve full Bank support. However, the fiscal situation has been deteriorating in recent years and this has been reflected in large increases in non-project foreign borrowing. The policy of dampening the impact of rising world prices for food and petroleum on consumers through Government subsidies has further aggravated the fiscal problem. A much greater domestic resource mobilization effort to increase public savings has become crucial to the attainment of Peru's ambitious economic and social development targets. The Ministry of Finance is fully aware of these problems and the Minister has indicated to Bank staff his intention to obtain governmental approval of a series of measures to restrict expenditures and increase revenues. We intend in early December to review the Government's fiscal program for 1975-76. The results will be summarized in a memorandum to Management supplementing this CPP, making recommendations on any changes which may be called for in our lending program for Peru, as well as on our position in the next Consultative Group Meeting.

Attachments:

1. Actual and Proposed Lending through FY80.
2. Cumulative Estimated and Actual Disbursements on Loans and Credits.
3. Country Data.
4. Economic Work Program FYs 75-76.
5. Map
- S1 Selected Economic Development Data
- S2,p.1 Balance of Payments - Part I: Import Detail
- p.2 Part II: Export Detail
- p.3 Part III: Summary

Latin America and the Caribbean Regional Office

Population: 14.9 million (1973)
 Population Growth: 2.9 percent
 GNP Per Capita: \$520 (1972)
 GNP Per Capita Growth: 1.7% (1961-69); 2.9% (1970-73)
 Area: 1,265,215 Km²
 Adult Literacy Rate: 72 percent (1972)

PERU: ACTUAL AND PROPOSED LENDING THROUGH FY80
 (\$ million)

ATTACHMENT 1

	Through FY68	Actual						Current FY75	Projected					Total FY69-73	Total FY74-78	Total FY76-80
		FY69	FY70	FY71	FY72	FY73	FY74		FY76	FY77	FY78	FY79	FY80			
Agricultural Credit I-IV	30.0						25.0									
Agricultural Credit V									30.0							
Agricultural Credit VI																
Agricultural Credit VII																
Agricultural Equipment I-II	3.0														35.0	
Irrigation I-II	29.0															
Irrigation Rehabilitation I									20.0							
Irrigation Rehabilitation II											25.0					
Irrigation Rehabilitation III												25.0				
Rural Development I (Cajamarca)										20.0						
Rural Development II (Huallaga Central)											25.0					
Rural Development III (Undetermined)													40.0			
Forestry and Forestry Industry I									25.0							
DPC I								30.0								
DPC II										30.0						
DPC III													40.0			
Education I (Reformed Secondary)							24.0									
Education II										30.0						
Education III														40.0		
Water Supply																
Industry I	2.5									25.0						
Mining I (Centromin-Peru)										50.0						
Mining II (Centromin-Peru)									4.0			50.0				
Mining III (Minero-Peru)														50.0		
Power I-IV	66.5															
Power V (Empresas Electricas)										20.0						
Power VI (Electroperu-Generation)									35.0							
Power VII (Electroperu-Generation)									36.0			40.0				
Roads I-IV	53.5															
Roads V																
Roads VI				30.0												
Transandean corridor (Roads and river ports)							26.0									
Roads VII (Central highway)								50.0								
Roads VIII (Panamerican highway)										76.5		40.0				
Ports V (Ocean ports)										40.0			40.0			
Airports																
Sites and Services I										20.0						
Sites and Services II																
Operations Program	IBRD No.						75.0	85.0	172.5	90.0	180.0	170.0	125.0			780.0
							3	2	4	4	5	5	3			23
Lending Program	IBRD No.						75.0	85.0	120.0	125.0	130.0	140.0	85.0	30.0	535.0	600.0
							1	2	4	5	4	4	2	1	17	16
Lending Program (Constant FY74 dollars)							41.8	75.0	76.9	88.2	98.5	103.5	100.6	55.3	41.8	442.1
Deflator (FY74 = 100)								100.0	110.5	119.0	126.9	135.3	144.2	153.7		446.1
IDB Gross Commitments	46.2	12.2	44.3	35.1	35.0	6.1	18.3	41.0	65.0	65.0	65.0	75.0	75.0			
IBRD o/s incl. undisbursed	170.2	164.6	157.0	179.6	179.9 ^{2/}	186.9 ^{3/}	208.4 ^{4/}	323.9	418.5	513.0	661.5	791.4	858.9			
excl. undisbursed	115.8	121.0	122.2	127.2	138.9 ^{2/}	154.8 ^{3/}	169.6 ^{4/}	154.8	176.8	221.3	282.4	364.4	453.3			
IBRD Gross Disbursements	159.9	10.6	8.8	12.5	11.3	8.1	8.3	14.8	32.4	54.9	72.6	97.1	106.6	51.3	183.0	363.6
Net Disbursements	115.8	5.2	1.1	5.1	4.0	0	-0.5	5.3	22.0	44.5	61.1	82.1	89.1	15.4	132.4	298.8
Net Transfer	79.2	-1.4	-6.0	-2.0	-3.6	-8.2	-9.5	-4.1	11.1	30.6	42.9	58.1	58.5	-21.2	71.0	201.2

1/ As of end of fiscal year.
 2/ The exchange adjustment of \$7.6 million, as of June 1977, has been included in these figures.
 3/ The exchange adjustment of \$15.9 million, as of June 1973, has been included in these figures.
 4/ The exchange adjustment of \$4.7 million, as of June 1974, has been included in these figures.
 NOTE: All data in this table reflect o/s amounts and transactions of loans sold to third parties.

Latin America and the Caribbean Regional Office
 October 21, 1974

NOTE: This lending program is out of date.
 Our current one is presented under G-3.

ATTACHMENT 2

PERU: CUMULATIVE ESTIMATED AND ACTUAL DISBURSEMENTS ON LOANS AND CREDITS
(\$ millions)

Project & No.	Amount:			Date:		Closing Date	Forecast Date	FY'73	FY'74				FY'75				FY'76	FY'77	FY'78	FY'79	FY'80	FY'81	FY'82
	- Original	- Cancelled	- Net	- Approved	- Signed				- Effective	1	2	3	4	1	2	3								4
San Lorenzo Irrigation IRRD 416	11.0			4/20/65		Orig: 12/31/67	9/30/70 (1st)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
	4.5			6/18/65		Rev: 12/31/74	2/15/74	-	5.8	5.9	6.0	6.1	-	-	-	-	-	-	-	-	-	-	
	6.5			11/24/65		Act: -	-	5.4	5.6	5.6	5.7	5.8	6.3	6.5	-	-	-	-	-	-	-	-	
La Oroya-Aguaytia Highway IRRD 425	33.0			8/31/65		Orig: 6/30/71	9/30/70 (1st)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
	-			9/17/65		Rev: 12/31/73	2/20/71	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
	33.0			11/30/65		Act: -	-	31.8	32.7	32.9	33.0	33.0	-	-	-	-	-	-	-	-	-	-	
Highway Reconstruction IRRD 706	30.0			9/ 8/70		Orig: 9/30/75	8/21/70	14.9	16.4	18.0	19.6	21.2	22.8	24.4	25.8	27.2	30.0	-	-	-	-	-	
	-			9/14/70		Rev: -	2/28/73	3.0	4.0	5.0	7.0	10.0	13.0	16.0	19.0	22.0	30.0	-	-	-	-	-	
	30.0			10/26/70		Act: -	-	2.1	2.8	3.9	6.5	6.9	-	-	-	-	-	-	-	-	-	-	
Agricultural Credit IRRD 933	25.0			8/14/73		Orig: 12/31/77	6/20/73	-	-	.2	.4	.6	.8	1.8	3.3	5.0	13.5	22.0	25.0	-	-	-	
	-			9/12/73		Rev: -	6/20/74	-	-	-	-	-	.1	.5	1.0	3.0	13.5	22.0	25.0	-	-	-	
	25.0			12/12/73		Act: -	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Education Project IRRD 949	24.0			11/13/73		Orig: 6/30/79	10/ 4/73	-	-	-	-	-	.1	.2	.3	.5	2.8	8.3	17.2	23.7	24.0	-	
	-			12/ 5/73		Rev: -	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
	24.0			3/ 5/74		Act: -	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	

Controller's
8/2/74

ATTACHMENT 3

COUNTRY DATA - PERU

AREA
1,285,215 km²

POPULATION
14.1 million (mid-1972)

DENSITY
400 Per km² of arable land

SOCIAL INDICATORS

	Peru		Reference Countries		
	1960	1970	Mexico 1970	Chile 1970	Sweden* 1970
GDP PER CAPITA US\$ (ATLAS BASIS) /1	..	520 /a	750 /a	800 /a	4,480 /a
DEMOGRAPHIC					
Crude birth rate (per thousand)	44-45 /b	42 /c	43 /a	30	13.8 /a
Crude death rate (per thousand)	12-14 /b	11 /c	10	9	10.4 /a
Infant mortality rate (per thousand live births)	91 /d	73 /e	58 /a,f	79	11.1 /a
Life expectancy at birth (years)	52 /h	58 /c	64 /c	62 /i	72 /j
Gross reproduction rate /2	3.1 /b	2.9 /c	3.1 /c	2.2 /c	1.1 /c
Population growth rate /3	2.9 /k	2.8 /l	3.5 /l	2.3 /l	0.7 /l
Population growth rate - urban	5 /m,n	5 /n,o	5 /p	3 /q	1.9 /r
Age structure (percent)					
0-14	43 /h,s	45 /a	46	39	20.8
15-64	53 /h,s	52 /a	50	55	65.5
65 and over	4 /h,s	3 /a	4	6	13.7
Dependency ratio /4	1.5 /h,t	1.5 /c	1.9 /t	1.5 /g,t	0.8 /q,t
Urban population as percent of total					
Family planning: No. of acceptors cumulative (thous.)	47 /h,n,u	54 /a,n,y	59 /p	76 /q	81 /r
No. of users (% of married women)	..	..	..	..	..
EMPLOYMENT					
Total labor force (thousands)	3,200 /h	4,300	13,000	3,000 /g	3,600 /k
Percentage employed in agriculture	50 /h	45	39	19 /g	8.1 /g
Percentage unemployed	3 /h	5	4	5 /g	2 /g,r
INCOME DISTRIBUTION					
Percent of national income received by highest 5%	50 /h,v	34 /w,x	36 /a,y	30 /y,z	18 /a,a,b
Percent of national income received by highest 20%	69 /h,v	60 /w,x	64 /a,y	57 /y,z	44 /a,a,b
Percent of national income received by lowest 20%	3 /h,v	2 /w,x	4 /a,y	5 /y,z	4 /a,a,b
Percent of national income received by lowest 40%	9 /h,v	7 /w,x	11 /a,y	13 /y,z	14 /a,a,b
DISTRIBUTION OF LAND OWNERSHIP					
% owned by top 10% of owners	..	93	..	..	..
% owned by smallest 10% of owners	..	0.1	..	..	..
HEALTH AND NUTRITION					
Population per physician	2,200 /ac	1,920 /a	1,440	2,010 /ad	730
Population per nursing person	..	3,200 /a	1,570	5,320 /ad	200
Population per hospital bed	490 /ae	470	930	250	70
Per capita calorie supply as % of requirements /5	88 /af	88 /a	107 /ag	102	108 /w
Per capita protein supply, total (grams per day) /6	54 /af	55 /a	66 /ag	66	80 /w
Of which, animal and pulse	25 /af	24 /a	28 /ag	32	56 /w
Death rate 1-4 years /7	10 /ac	..	11	3 /i	0.4 /g
EDUCATION					
Adjusted /8 primary school enrollment ratio	89 /ah	115 /ah,ai	104 /ai	119 /ai,aj	97
Adjusted /8 secondary school enrollment ratio	18 /ah	41 /ah	23	29	102 /ai
Years of schooling provided, first and second level	12	12	12	12	12
Vocational enrollment as % of sec. school enrollment	20 /ah	17 /ah	24 /a	33	35
Adult literacy rate %	61 /h,ak,al	72 /a,al,am	84 /al	90 /a,al,am	99 /al,am
HOUSING					
Average No. of persons per room (urban)	2.0 /h,an	..	2.5 /an,ao	1.4 /a,an	0.7 /ao
Percent of occupied units without piped water	85 /h,an,ap	..	61 /an,ap	40 /a,an	3
Access to electricity (as % of total population)	26 /h,an	..	59 /an	..	..
Percent of rural population connected to electricity	4 /h,an	..	..	..	..
CONSUMPTION					
Radio receivers per 1000 population	101	134	276	143	38 /g,ag
Passenger cars per 1000 population	8	17	25	18	291 /a
Electric power consumption (kwh p.c.)	297 /h	392	586	772	8,042
Newspaper consumption p.c. kg per year	1.8	3.2 /g	3.1	4.3 /g	31.8 /g

Notes: Figures refer either to the latest periods or to the latest years. Latest periods refer in principle to the years 1956-60 or 1966-70; the latest years in principle to 1960 and 1970.

/1 The Per Capita GNP estimate is at market prices for years other than 1960, calculated by the same conversion technique as the 1972 World Bank Atlas.

/2 Average number of daughters per woman of reproductive age.

/3 Population growth rates are for the decades ending in 1960 and 1970.

/4 Ratio of under 15 and 65 and over age brackets to those in labor force bracket of ages 15 through 64.

/5 FAO reference standards represent physiological requirements for normal activity and health, taking account of environmental temperature, body weights, and distribution by age and sex of national populations.

/6 Protein standards (requirements) for all countries as established by USDA Economic Research Service provide for a minimum allowance of 60 grams of total protein per day, and 20 grams of animal and pulse protein, of which 10 grams should be animal protein. These standards are somewhat lower than those of 75 grams of total protein and 23 grams of animal protein as an average for the world, proposed by FAO in the Third World Food Survey.

/7 Some studies have suggested that crude death rates of children ages 1 through 4 may be used as a first approximation index of malnutrition.

/8 Percentage enrolled of corresponding population of school age as defined for each country.

/a 1972; /b 1960-65 UN estimate; /c 1965-70 UN estimate; /d 1965; /e 1967; /f registered only; /g 1971; /h 1961; /i 1969; /j 1969-70; /k 1955-61; /l 1960-72; /m 1950-61; /n Capitals of districts and those populated centers with such urban characteristics as streets, plazas, water supply systems, sewerage systems, electric lights, etc.; /o 1961-72; /p Localities of 2,500 or more inhabitants; /q Populated centers which have definite urban characteristics contributed by certain public and municipal services; /r Built-up areas with at least 200 inhabitants and usually not more than 200 meters between houses; /s Data exclude adjustment for underenumeration, and Indian jungle population; /t Ratio of population under 15 and 65 and over to total labor force; /u Excluding Indian jungle population; estimated at 100,830 in 1961; /v Population; /w 1970-71; /x Economically active population; /y Households; /z 1968; /aa 1963; /ab Income recipient; /ac 1964; /ad Government only; /ae 1962; /af 1960-62; /ag 1964-66; /ah Including evening schools; /ai Including overage students; /aj Estimate; /ak 17 years and over; /al Definition unknown; /am 15 years and over; /an Data refer to housing units; /ao Urban and rural; /ap Water piped inside; /aq Data is not comparable.

* Sweden has been selected as an objective country for Peru because of its high level of income accompanied by an active socio-economic policy aimed at attaining a more equitable income distribution; and an economic policy which stresses the important role of the state in the economy.

PERU: ECONOMIC WORK PROGRAM FY75-76

• October 1974

- Technical assistance on external debt data processing and analysis.
- Industrial Sector Review: Review of industrial policies and recent developments and prospects of the sector. (Done as part of a pre-appraisal mission for a proposed DFC loan).

December 1974 - Agricultural Sector Survey.

Review with Peruvian Government a report of an 11-men Sector Survey mission will be completed in early December 1974. Survey focused on reviewing development strategy for the sector and suggesting investment priorities.

June 1975 - Basic Economic Mission.

Comprehensive review of economy with special attention to developments, prospects and policies in major productive and infrastructure sectors.

Latin America and the Caribbean Regional Office
October 21, 1974

SELECTED ECONOMIC DEVELOPMENT DATA

	Actuals			Est. 1973	Projections					Growth rates ^{1/}				As % GDP			
	Aver. 1968-69	1970	1972		1974	1975	1976	1977	1978	1965-70	1970-73	1973-76	1974-78	1972	1974	1976	1978
National Accounts (constant 1970 prices; millions US\$)																	
GDP	5606	6103	6837	7235	7669	8129	8617	9220	9866	3.7	5.8	6.0	6.5	100.0	100.0	100.0	100.0
Gains from terms of trade	-146	-	-204	96	140	63	57	78	120	..	..	..	..	-3.0	1.8	0.7	1.2
Gross domestic income	5459	6103	6633	7331	7809	8193	8674	9298	9985	4.6	6.3	5.8	6.3	97.0	101.8	100.7	101.2
Imports (incl. NFS)	916	972	1027	1145	1356	1461	1574	1698	1830	3.6	5.6	11.2	7.8	15.0	17.7	18.3	18.5
Exports (import capacity)	1040	1224	1047	1113	1142	1227	1366	1675	1781	7.6	-3.1	7.0	11.7	13.3	14.9	15.9	18.1
Consumption	4592	5107	5815	6347	6735	7066	7360	7618	8110	5.3	7.5	5.1	4.8	85.0	87.8	85.4	82.2
Investment	724	744	798	1016	1148	1297	1465	1626	1805	-3.4	11.0	13.0	12.0	11.7	15.0	17.0	18.3
National savings	785	985	767	923	948	981	1140	1461	1640	0.9	-2.2	7.3	14.7	11.2	12.4	13.2	16.6
Domestic savings	867	996	818	984	1073	1127	1314	1681	1876	1.2	-0.4	10.2	15.0	12.0	14.0	15.2	19.0
Price Indices (in percentages)																	
Domestic price index ^{2/}	90.1	100.0	110.1	128.5	147.8	169.9	195.4	224.7	258.5	11.1	8.7	15.0	15.0	..	..	..	..
Import price index	98.5	100.0	110.3	120.6	155.1	168.8	178.2	190.1	203.1	-1.0	6.4	13.8	7.0	..	..	..	..
Export price index	85.4	100.0	92.3	131.9	174.1	177.5	185.7	198.9	216.7	6.9	9.6	12.1	5.6	..	..	..	..
Public Finance ^{3/} (current prices; millions US\$)																	
Public revenues ^{4/}	n.a.	1321	1700	2068	2646	3087	3879	4683	5594	n.a.	16.1	23.0	21.0	22.6	23.6	23.6	22.8
Current expenditures	n.a.	1062	1512	1887	2396	2882	3575	4248	5051	n.a.	21.0	24.0	20.0	20.1	21.3	21.7	20.6
Public savings ^{5/}	n.a.	259	209	190	271	213	312	443	550	n.a.	-11.9	18.1	19.4	2.8	2.4	1.9	2.2
Public investment ^{6/}	n.a.	213	367	460	819	846	1016	1081	1254	n.a.	29.0	30.0	12.0	4.9	7.3	6.2	5.1

1/ 1965-70 based on three year end point averages; others based on single year.

2/ Implicit GDP deflator.

3/ Consolidated public sector.

4/ Projections for 1975 and 1976 do not include the additional revenue measures suggested in the text.

5/ Includes capital revenues.

6/ Gross fixed investment only.

(-) Nil or negligible

(..) Not applicable

(n.a.) Not available

BALANCE OF PAYMENTS
PART I: Import Detail
(millions of US\$)

	Aver. 1968-69	1970	1972	1973 ^{2/}	1974 ^{3/}	1975	1976	1977	1978
I. IMPORTS F.O.B.									
A. Constant 1970 prices									
Food ^{1/}	n.a.	119.2	135.9	133.7	137	142	146	151	155
Petroleum	n.a.	22.0	33.0	30.0	34	40	46	56	64
Capital goods	n.a.	186.8	178.9	244.6	338	382	432	475	523
Other goods	n.a.	371.3	413.3	444.9	526	557	590	631	675
Total goods F.O.B.	n.a.	699.6	807.5	853.2	1035	1121	1214	1312	1417
Non-factor services	n.a.	272.0	265.3	291.9	321	340	361	386	413
Total goods and NFS	916.0	971.6	1026.7	1145.1	1356	1461	1574	1698	1830
B. Price Indices (1970 = 100)									
Food ^{1/}	n.a.	100.0	122.4	157.1	299.2	299.2	284.9	277.8	277.8
Petroleum	n.a.	100.0	135.1	189.3	457.8	507.8	544.8	587.0	629.6
Capital goods	n.a.	100.0	104.0	120.6	137.5	152.5	163.9	176.1	189.2
Other goods	n.a.	100.0	96.1	105.0	119.7	132.7	142.6	153.2	164.6
Non-factor services	n.a.	100.0	104.0	120.6	137.5	152.5	163.9	176.1	189.2
Implicit total goods and NFS	98.5	100.0	110.3	120.6	154.1	168.8	177.9	190.0	203.1
C. Current Prices									
Food ^{1/}	n.a.	119.0	166.0	210.0	412	424	416	413	431
Petroleum	n.a.	22.3	45.0	56.8	156	201	249	326	403
Capital goods	171.2	186.8	197.4	295.0	465	583	708	836	989
Other goods	n.a.	371.3	431.1	467.2	629	739	841	967	1111
Total goods F.O.B.	665.9	699.6	839.8	1029.0	1650	1947	2210	2547	2934
Non-factor services	236.1	272.0	292.6	352.0	441	519	591	680	782
Total goods and NFS	902.0	971.6	1132.4	1381.0	2103	2466	2805	3227	3716

- ^{1/} Data for food imports are rough mission estimates and should be viewed as indicative orders of magnitude.
^{2/} 1973 data for total imports are preliminary official estimates, which in the mission's view underestimates the "other goods" category.
^{3/} 1974 data at current prices are official Peruvian projections.

PART II: Export Detail
(millions of US\$)

	Aver. 1968-69	Actual			Projected				
		1970	1972	1973	1974	1975	1976	1977	1978
II EXPORTS									
A. Constant 1970 prices									
Copper	235.0	246.7	240.8	233.0	253.0	265.7	345.9	521.7	534.8
Lead	34.0	35.3	37.5	38.9	39.6	40.9	42.1	43.3	48.9
Silver	56.0	62.3	69.5	62.0	65.0	70.6	73.9	74.6	76.5
Zinc	45.2	48.7	54.5	49.9	52.6	61.0	65.3	78.2	83.7
Iron ore	66.1	72.1	64.1	65.0	74.4	71.4	70.7	70.0	70.7
Fishmeal	302.9	303.5	246.9	56.4	100.1	129.6	147.1	164.4	181.6
Other fisheries	49.6	43.2	61.0	7.9	12.7	13.3	14.1	14.7	15.5
Coffee	45.1	43.8	54.7	58.8	56.7	57.3	57.8	58.4	59.0
Sugar	54.7	60.7	72.4	61.3	62.5	63.0	63.3	63.4	63.6
Cotton	61.8	52.1	38.9	37.0	37.6	37.6	37.6	37.6	37.6
Wool	11.2	3.3	5.0	5.6	5.8	5.8	6.0	6.0	6.2
Petroleum	8.5	6.8	5.1	6.6	10.6	15.4	20.5	91.8	122.6
Other	43.0	55.8	69.0	90.6	118.3	130.1	143.1	157.4	173.1
Total goods	1013.1	1034.3	1019.4	773.0	888.9	961.7	1087.4	1331.5	1473.8
Non-factor services	172.9	189.5	231.4	244.4	252.9	265.5	278.8	292.8	307.4
Total goods and NFS	1186.0	1223.8	1250.8	1017.4	1141.8	1227.2	1366.2	1674.3	1781.2
B. Price Indices (1970=100) ^{1/}									
Copper	100.7	100.0	78.1	144.5	188.4	174.8	181.3	173.0	186.6
Lead	93.5	100.0	89.3	120.3	172.0	174.3	178.9	172.5	179.6
Silver	113.4	100.0	88.1	127.3	120.2	131.9	141.7	152.3	163.4
Zinc	83.6	100.0	129.2	210.4	453.4	411.3	392.0	344.1	340.0
Iron ore	103.5	100.0	105.3	101.8	127.4	125.0	143.3	163.1	193.7
Fishmeal	67.5	100.0	88.9	244.1	246.3	248.8	244.4	243.2	253.1
Other fisheries	45.0	100.0	76.1	233.1	224.0	230.6	237.6	244.7	252.3
Coffee	71.6	100.0	90.0	109.8	131.2	152.6	177.1	176.6	174.0
Sugar	90.0	100.0	118.6	127.3	226.6	212.1	226.6	239.5	264.1
Cotton	100.8	100.0	120.7	173.7	211.7	202.8	199.7	202.8	217.9
Wool	80.4	100.0	122.1	178.7	250.3	228.0	222.0	193.2	185.8
Petroleum	94.1	100.0	126.0	155.9	376.2	417.4	448.0	482.6	517.4
Other	91.4	100.0	92.3	111.2	126.8	140.6	151.1	162.4	174.5
Non-factor services	92.3	100.0	90.5	85.9	101.4	112.5	120.9	129.9	139.6
Implicit total merchandise export price index	85.4	100.0	92.7	144.9	194.3	195.5	202.3	213.7	236.9
C. Current Prices									
Copper	236.7	246.7	188.1	336.8	476.7	464.5	627.1	902.7	997.8
Lead	31.8	35.3	33.5	46.8	68.1	71.3	75.3	74.7	87.8
Silver	63.5	62.3	61.2	78.9	78.1	93.1	104.7	113.6	125.0
Zinc	37.8	48.7	70.4	105.0	238.5	250.9	256.0	269.1	284.6
Iron ore	68.4	72.1	67.5	66.1	94.8	89.3	101.3	114.2	136.9
Fishmeal	204.3	303.5	219.4	138.8	246.6	322.4	359.6	399.9	459.6
Other fisheries	22.3	43.2	46.4	18.5	28.4	30.7	33.5	35.9	39.0
Coffee	32.3	43.8	49.1	64.7	74.4	87.4	102.4	103.1	102.7
Sugar	49.2	60.7	85.9	78.1	141.6	133.6	143.4	151.8	168.0
Cotton	62.3	52.1	47.0	64.4	75.6	76.3	75.1	76.3	81.9
Wool	9.0	3.3	6.1	10.0	14.5	13.2	13.3	11.6	11.5
Petroleum	8.0	6.8	6.5	10.2	39.9	64.3	91.8	443.0	634.2
Other	39.3	55.8	63.7	100.8	150.0	183.0	216.3	255.6	302.1
Total goods	864.9	1034.3	945.0	1120.0	1727.2	1880.0	2199.8	2951.6	3491.3
Non-factor services	159.5	189.5	209.5	222.0	256.4	298.7	337.1	380.3	429.1
Total goods and NFS	1024.4	1223.8	1154.5	1342.0	1983.6	2178.7	2536.9	3331.9	3920.4

^{1/} Price Index from "Commodity and Export Projections Division" dated April 18, 1974, adjusted by the historical difference between the international price and the Peruvian f.o.b. price.

PART III: Summary Balance of Payments

	Average 1968-69	1970	1972	1973 ^{1/}	1974	1975	1976	1977	1978	1979	1980	1985
Imports (including NFS)	-902.0	-971.6	-1132.4	-1381.0	-2103	-2466	-2806	-3228	-3717	-4304	-5001	-9637
Exports (including NFS)	1024.4	1223.8	1154.5	1342.0	1988	2179	2537	3332	3860	4403	5162	9777
Balance of goods and NFS	122.4	252.2	22.1	-39.0	-116	-288	-269	104	143	99	161	140
Factor services, net	-166.9	-148.5	-134.2	-174.6	-226	-279	-350	-454	-515	-575	-654	-1088
Interest on Public M+LT debt	(-41.3)	(-49.8)	(-60.5)	(-83.0)	(-106)	(-157)	(-206)	(-259)	(-300)	(-338)	(-373)	(-474)
Other	(-125.6)	(-98.7)	(-73.7)	(-91.6)	(-120)	(-122)	(-144)	(-195)	(-215)	(-237)	(-281)	(-614)
Current transfers	34.2	82.0	40.6	32.2	32	34	35	36	36	36	36	50
Balance on current account	-10.3	165.7	-71.5	-181.4	-309	-533	-583	-314	-336	-440	-458	-897
Private direct investment	-7.2	-69.6	47.2	65.3	43	99	99	116	136	158	186	300
Public M+LT loans (net)	98.4	58.7	112.9	333.5	442	408	486	424	414	418	438	939
Disbursements ^{2/}	(217.0)	(220.2)	(300.9)	(671.8)	(779)	(621)	(674)	(620)	(711)	(810)	(914)	(1608)
Amortizations ^{3/}	(-118.6)	(-161.5)	(-188.0)	(-352.3)	(-337)	(-213)	(-188)	(-196)	(-297)	(-392)	(-476)	(-669)
Capital n.e.i. ^{4/}	-54.8	82.3	-53.5	-204.2	-126	54	60	66	73	80	89	142
Changes in reserves	-26.1	-257.1	-35.1	-13.2	-50	80	58	-160	-141	-55	-77	-198
Uncovered gap	..	..	..	..	-	-	-	-	-	-	-	-
Meso items												
Imports after cuts in uncovered gap	902.2	971.6	1132.4	1381.0	2103	2466	2806	3228	3717	4304	5001	9637
Reserves (net end of period)	130.8	408.8	388.6	401.8	452	372	314	474	615	670	747	1547
Debt service ratio ^{3/}												
Public	15.6	17.3	21.5	23.6	16.5	17.0	15.5	13.7	15.5	16.5	16.4	11.6
External debt O+D (end of period)												
Public	855.0	899.0	1152.0	1485.0	1984	2407	2903	3327	3741	4159	4597	8164
IBRD	119.8	124.6	131.3	131.7	132	137	159	203	264	346	435	935
IBRD debt service as percent of total public debt service ^{3/}	8.3	7.0	6.3	3.7	5.2	4.9	4.9	4.8	4.6	4.8	5.4	10.9

- ^{1/} During 1973 various internal problems in the customs bureau have delayed publishing of final import figures. Various Peruvian authorities concurred with the mission's view that the official import figure of \$1381 million highly underestimates real movements. This explains in part the unusually large figure for capital n.e.i.
- ^{2/} The projections assume that as was done in recent years, a large share of public sector amortization payments due in 1975-76 will be refinanced: \$100 million in 1974 and \$150 million in 1975 and in 1976.
- ^{3/} 1973 and 1974 amortization figures include large pre-payment of loans (\$127.9 million in 1973 and \$115 million in 1974). These were not included in calculating the debt service ratio.
- ^{4/} Includes medium and long-term borrowing by private sector: drawings of SDN's; subscription to international agencies; foreign exchange remittances related with nationalization of foreign companies; short-term capital movements and errors and omissions.

1. The military have been in power in Peru since 1968. The major economic and social reforms undertaken by the military regime and the progress and outstanding problems after more than five years in power are summarized in an article in the July 1974 issue of Foreign Affairs, which is attached.

A. Developments during 1975 before the change of Government in August.

2. During the first half of 1975, the political situation markedly deteriorated in Peru. As General Velasco struggled to develop a popular political base for the regime, he became increasingly fearful of criticism in the press. Dissenters were deported and public sector employees pressured for loyalty to the Government's positions. An ambiance of uncertainty and paranoia developed which resulted in a gradual paralyzation of public administration. At the same time the traditional unity between the top generals of the army came apart. At least three factions appeared: (a) On the left General Graham and General Rodriguez, supported by the rural poor pushed for a further radicalization of the regime and the acceleration of reforms; (b) General Tantalean and General Richter, with the support of the fisheries sector workers (small in number but well organized and prone to violent tactics) pushed for a more populist approach, greater centralization of power and repression of dissenters; and (c) In the middle was General Morales Bermudez.

3. President Velasco gradually became more arbitrary and erratic in his decision making; many times with little consultation with his Cabinet. (The Marcona nationalization was a case in point, it apparently being decided without the knowledge or approval of General Fernandez Maldonado, the then Minister of Energy and Mines). At the same time discord increased within the Cabinet because of the growing evidence of corruption of some of the top Government and military staff.

B. The takeover strategy of General Morales Bermudez

4. General Morales Bermudez forged his way into power in a series of well calculated steps. During 1967-73 as Minister of Economy and Finance he established himself as a brilliant technocrat in managing the country's finances and as a relative moderate with respect to the revolutionary objectives of the Government. He was highly respected abroad and by the local private sector. During 1974 as chief of staff of the army he made a low key but intensive campaign to gain the support and respect from the grassroots military officers throughout the country. Their support was crucial against the resistance of left-wing generals to his nomination to become Prime Minister in February 1975. Once Prime Minister, he took over personal control of economic management, with regular "mini" cabinet meetings with the ministers in the "economic sectors". Through this

mechanism he was successful in getting the July package of price and salary measures approved, in spite of the political uncertainties involved. He next took control of the country's foreign policy, mainly through his initiative for a tri-partite non-aggression pact between Chile, Bolivia and Peru. Many observers believe that the bloodless coup that brought General Morales to power in August 1975 was actually planned for later in the year, but that the erratic way in which the Marcona nationalization was handled and a series of radical decrees which General Velasco was on the verge of promulgating prompted General Morales to take over the presidency.

C. The New Government

5. The takeover by General Morales in August 1975 was a victory for the moderate center-left factions within the military. General Morales declared that the basic objectives of the revolution would remain unchanged but that various adjustments would be made (in what he called "the second phase of the revolution"). The main changes he has been pursuing in recent months are:

- (i) Increased participation by the people at the grassroots in the development process. To accomplish this he has eliminated press censorship, given amnesty to all imprisoned or deported political foes, and started an intensive personal dialogue with the various interest groups. This dialogue is to be institutionalized by creation of various committees throughout the country reporting directly to the Prime Minister on how Government strategy should be designed. Social property enterprises are being given higher priority in order to promote rapid development of entrepreneurial activity outside the public sector.
- (ii) Greater efforts toward decentralization of economic activity and public administration. Major legislation is now being prepared that would give more power to local governments and would regionalize the administration of public enterprises and government ministries. Although strongly opposed by the Lima bureaucracy, General Morales is considering moving towards a more federal and less centralized political organization of the country. This objective is consistent with the desire to broaden popular participation.
- (iii) The elimination of corruption at all levels of government. With a widely accepted reputation of scrupulous rectitude and honesty, General Morales has pushed the Ministry of Justice to audit the operations of public enterprises. The investigations have not spared the military, and a previous Minister of Agriculture, among others, has been indicted.
- (iv) Improving the quality of the government's technocrats. A civilian, (with much experience in macrofinancial and business management)

was appointed as Minister of Finance, and other offices have gradually been filled with technocrats as well. An example was the appointment of Mr. Santistevan to President of the Central Bank.

- (v) The preparation of a new plan of long-term Government objectives. This plan, to be prepared before the end of March 1976, will replace the Plan Inca prepared before the 1968 coup which has provided the broad guidelines for political action during the last seven years.
 - (vi) Additional measures to those effected last July to face the rapidly deteriorating financial position of the economy. These have included a devaluation in September and another set of price and tax measures in January 1976 (see Tab-3 for details).
 - (vii) The modification of price policies to subsidize less the urban areas and encourage production in rural areas.
6. General Morales has stated that the "second phase" of the revolution will last about six years and has hinted at the possibility of a transfer of power to civilians at some later date.

7. In spite of the above actions, General Morales has been up to now unsuccessful in consolidating his political power and is attacked by both the right and the left. The left accuses him of slowing down the revolution because of the tough economic austerity measures approved, the forced retirement of the most radical elements within the army and his statements that the reforms already approved should be consolidated before taking further steps. His efforts to shift the regional terms of trade in favor of rural areas and to decentralize the political administration have not been favored by the urban pressure groups, particularly the trade unions. The right, on the other hand, accuses him of not moving fast enough to improve the prospects of the private sector. They also fear the presence of General Fernandez Maldonado (previous Minister of Energy and Mines and one of the most vociferous members of the first Revolutionary Junta) as Prime Minister because of his strong left wing views. Keeping General Fernandez in the Cabinet was nonetheless essential to placate the doubts of the extreme left.

8. The position of APRA and "Alianza Popular", -- the only two parties who have a strong base of political support -- in the present difficult political situation is not clear.^{1/} Throughout General Velasco's regime they were vociferous in opposing the government.^{2/} Since

^{1/} APRA, the American Revolutionary Popular Alliance, led by Mr. Haya de la Torre has been a traditional enemy of the Army. Founded in the 1920s on a nationalistic left wing platform, it gradually has become more conservative. APRA has a strong political support from the coastal rural and urban middle class. "Alianza Popular" is the party of Mr. Belaunde, the president that preceded General Velasco.

^{2/} Political parties in Peru are not outlawed.

General Morales took power, these parties have officially remained silent, although it is not known what role their political organizations have had in the labor unrest of recent months. Mr. Belaunde, who lives in Washington, D.C., returned to Lima for one week last January. He has however not made any major political declarations either in Lima or after his return to Washington, D.C.

9. The Marcona nationalization (see Tab G-3 for specifics), which was inherited from the previous government, further complicates the political panorama. If a speedy compensation agreement is not signed, General Morales is aware that serious repercussions will be felt in foreign economic and political relations. However, if an agreement openly awards substantial compensation, the left could use it as proof that General Morales has betrayed the basic objectives of the revolution.

10. Peru's future political course may depend on how well its immediate economic difficulties are resolved. The solution will require: (i) the improvement of international economic conditions, and hence Peru's export earnings, and the availability of foreign capital, in order to reduce the pressures for further unpopular austerity measures; and (ii) the success of General Morales in convincing labor unions, on the other hand, to reduce strikes and improve worker discipline, and on the other hand, the private entrepreneurial sector that it can invest and flourish under the "economic pluralism" policy of the Government.^{1/} A major political question is the ability of General Morales to build-up a permanent and institutionalized base of political support.

11. The Peruvian Government is at a crucial crossroad. If it is unsuccessful in achieving the above, and the political and economic situation further deteriorates, the result may be a sharp radicalization of the regime either to the extreme left or extreme right.

^{1/} For details see Tab F-3.

1. This section briefly describes the main thrust of the development strategy followed by the Military Government since 1968, summarizes its principal successes, and sketches the main problems and bottlenecks that the Government will have to solve in coming years to achieve its development objectives. (Details on sectoral issues are presented in Tab F-5).

2. It is important to place the discussion in the context of Peru's economic history and the socioeconomic situation that has evolved in order to appreciate the challenge that must be faced by any government wishing to pursue a policy of social and economic transformation. While it is true that many of the same problems also exist in other Latin American countries, the combination and intensity of the negative factors found in Peru are more pronounced.

A. Background: Socioeconomic Development Before the 1968 Military Revolution

dual economy

3. Peru's economic history is marked by three fundamental characteristics: (a) intermittent spurts of growth based on the export of a few primary commodities; (b) extreme concentration of the resulting benefits; and (c) extensive participation of foreign ownership in key sectors of the economy. This pattern of development has derived in part from the special characteristics of the country's natural and human resource base. The exploitation of Peru's vast mineral resources have had limited linkage effects on the rest of the economy and only small direct employment effects. At the same time, cultivable land is scarce and of poor quality although a large share of the population is employed in agricultural activities. The sociopolitical structure of the country also affected the development pattern. The rural population, largely Indian, is only imperfectly integrated into the Spanish-speaking modern sector of society. The landowning elite was able to stop most efforts to incorporate a larger share of the population into the economy. At the same time, although they did provide what entrepreneurship there was, they did not evolve into a broadly-based, dynamic entrepreneurial class.

4. Economic growth has been based mainly on a few primary export crops. During colonial and early republican days, growth came from the extraction of precious metals and plantation-type agriculture, with labor being provided largely by conscripted Indians. Then in the mid-1800s vast guano deposits were exploited almost in "gold-rush" fashion, spurred by the international demand for fertilizers. At the beginning of the present century intensive, irrigated agriculture for export crop production (sugar and cotton) in the coastal valleys and the beginning of systematic exploitation of the large deposits of copper and other minerals in the Sierra provided new avenues of expansion. More recently, during the 1950s, the resource base was expanded by the large-scale fishing of anchovy.

5. While a high economic growth rate was achieved, wide disparities were created in productivity, employment opportunities and welfare between the modern and the traditional sectors, between the coast and the rest of the country and between the urban and the rural populations. The modern sector, located mainly along the coast, included large-scale export-oriented enterprises in mining and agriculture and a limited manufacturing sector with its related transport, trade, power and financial services. The traditional sector in the Sierra, dominated by peasant minifundia and large feudal ranches, employed most of the population. The capital intensive technology and the high productivity of the modern sector contrasted with the low investment levels, primitive technology and severe scarcity of arable land in the Sierra. The country's extreme topography and difficult climate limited the economic links between the two regions and reinforced the geographical concentration of economic activity at coastal urban centers (mainly Lima). Most of the talented and entrepreneurial population of the Sierra was attracted away, effectively relieving the build up of pressures there for socioeconomic change and modernization.

6. A large share of the economic growth generated by the modern sector was promoted, owned and controlled by foreign enterprises. Among export industries, foreign ownership covered all large-scale and most medium-scale mines, many of the fishmeal processing plants and some of the sugar estates. Foreign interests were also strong in the petroleum sector, power, telephones, railways, commercial banking and in most of the larger firms in the manufacturing sector.

7. The pressures for change and modernization of the country grew rapidly in the postwar period, and in 1962 Fernando Belaunde was elected President on a platform that called for large socioeconomic reforms with emphasis on rural development. He rapidly expanded public investment and public services and began the process of agrarian reform. Belaunde --whose grasp of economic constraints was limited-- had strong political support from the rural population, but was unable to overcome the power of the traditional ruling elite. The latter were successful in blocking both the implementation of the agrarian reform and the urgent revenue measures required to finance the growing level of public services. In 1967 the country fell into a deep financial crisis.

8. For various reasons, the Peruvian military establishment had developed a strong sensitivity to the socioeconomic problems afflicting the country (see Lowenthal's article, attached to Section F-2, for details). They had supported, if not engineered, Belaunde's election but with his failure, they became convinced they were the only institution possessing sufficient power to change the basic structure of the country, and in September 1967 they took power.

B. Development Thrust of the Military Government after 1968

9. Upon assuming power, the Military Government announced plans for basic changes in the pattern of development. Economic growth was to be linked directly to broader popular participation in the country's economic, social and political life. Among other things, this meant effectively drawing the rural poor into the modern development process, improving the distribution of income and wealth and increasing the participation of Peruvians in the ownership and management of the economy. Also important was the decentralization of economic activity and political administration away from Lima. The guiding vision that has shaped development strategy consists of three essential elements: (a) the role of the military as the guarantor of order, equity and progress; (b) the goal of an ideal society consisting of a mixture of socialism, cooperativism, and residual capitalism; and (c) the achievement of independence from outside economic pressures.

10. A major objective of the Junta is the emergence of a new society through the fundamental transformation of the ownership structure of the economy. In the new Peruvian model five sectors are to co-exist in what is called "economic pluralism". In the first place the state is increasing its direct participation in the development and exploitation of the country's basic productive resources and the marketing of its main products. The second sector is the "reformed" private sector. Here, in an arrangement called the "industrial community", workers in a firm will gradually acquire up to half of the enterprise's ownership, have a proportionate voice in management and share in the profits. The third sector, the "social enterprise sector", is composed of fully labor owned and managed enterprises that are intended to eliminate labor-management conflict, tap the entrepreneurial potential of the population, and broaden access to asset accumulation. Social enterprises receive financial and technical assistance from the state during the first years of operation. Once on their feet, a share of the profits of social enterprise are to be channelled to finance the development of new social enterprises. The fourth sector is composed of the agricultural cooperatives which will later have the option of joining the social property sector. The fifth sector, small private agricultural, commercial and industrial enterprises, remain as they are but may receive special incentives to promote their development.

11. The nationalistic orientation of the Government is manifested in various policies. Direct foreign ownership has been reduced in strategic sectors. Industrial policies, including high levels of protection, tax incentives, interest subsidies, etc., favor import substitution, with particular preference given to the creation and expansion of heavy capital and intermediate goods industries.

12. There were no detailed blueprints when the process began, and the experience has been mixed. An ambitious land reform in the coastal areas is almost completed, with relatively little disruption of output. Despite efforts to organize cooperatives, however, the Government has up to now been unsuccessful in substantially changing the lot of the Sierra peasants. Most of the large mining companies and the fishmeal industry were nationalized and are now run by public sector institutions. The excess capacity of the fishing industry has since been reduced and efficiency has increased. Most industrial enterprises have complied with the Industrial Community law. The Social Property law was approved, and several social enterprises are now in operation. Some flexibility has been shown in dealing with foreign investors. A large mining project, Cuajone, is under development, petroleum exploration contracts have been signed with various foreign contractors, and the Government has entered into various industrial ventures with foreign partners (e.g. trucks, tractors, and pharmaceuticals).

13. The institutional transformation is farther advanced in the agricultural sector than in the industrial sector. The main efforts in both sectors have been on implanting the new institutions, rather than on achieving immediate gains in production. Although output, surprisingly, has not fallen as a consequence of the significant transformations taking place, neither have the more important obstacles to future growth--shortages of capital and of managerial and technical skills--yet been dealt with effectively; indeed the transformation to social ownership and the enlarged direct role of government have probably increased the demand for these resources at the same time that the uncertainties which have been created in the still important private sector inhibit--at least in the short term--their supply.

MAJOR ISSUES AND PROBLEMS

14. The Peruvian experiment is now at an important crossroad. As detailed in the Political Brief (and in Lowenthal's article) the Military Government has with relative success maintained a broadly consistent policy line despite distinctly ambiguous political and ideological positions. During the first phase of change there was strong popular support for many of the reforms implemented and a high rate of income growth was achieved. Now, however, the expectations of the poorer groups have been raised, and adequate growth of employment and income will require a much higher level of investment by the non-public sector. But financing a sustained high level of public investment and increased public services will require the politically difficult raising of the burden of taxes and prices borne by the urban middle class. The following paragraphs summarize some of these problems; more details are provided in the sector briefs (particularly F-5a and c). These issues will also be studied in greater depth by the basic mission to Peru in March 1976.

Issue I. Investment and Production

15. Reconciling the objective of economic pluralism with the need to expand investment and output rapidly is probably the most serious medium- and long-term problem that the Government faces. During the last few years, the public sector has been the only dynamic investor. However, a limited human resource base and lack of experience has impeded efficient management and resulted in poor investment decisions. Moreover, as discussed below, the policies have failed to mobilize sufficient internal resources to finance the large investment program. Although the social property enterprises (see Industrial Annex, F-5c, for details) are the most interesting experiment in the Government's efforts to mobilize indigenous entrepreneurial abilities and provide for a better distribution of wealth, they will have to go through a long transitional process of acquiring experience and managerial skill during which they cannot be expected to contribute significantly to output expansion. The same is true for the agricultural cooperatives. Thus, at least in the short run, the country will have to rely on the private sector for much of the increase in production and employment. However, private sector investment has remained depressed mainly because of the uncertainties created by the structural changes. It remains to be seen if the Government has the political will and strength to provide the private sector with a more secure environment in which to invest without modifying its main development goals. If the industrial sector is to operate efficiently, it may also be necessary to change substantially such politically sensitive policies as absolute job security, negative real interest rates and the fixed exchange rate (see particularly briefs on Agriculture and Industry, F-5a and c, respectively).

Issue II. The Macrofinancial Constraint

Developments During 1968-74

16. Following two years of financial consolidation in 1968-69, GDP grew at an annual rate above 5.5% during 1970-74. Gross domestic investment rose from less than 13% to almost 17% of GDP between 1970 and 1974, largely because of the increase of both public and private investment in mining and petroleum. However, as consumption also grew faster than GDP and heavy losses were incurred by public enterprises marketing imported petroleum and foodstuffs, gross national savings fell from 15% to 11% of GNP between 1970 and 1974. The excessive growth of aggregate demand, combined with the sharp rise in Peru's import prices since 1973, resulted in both an acceleration of the annual rate of domestic inflation--from an average annual rate of 7.2% during 1969-73 to over 16% in 1974--and an increase in the deficit of the balance of payments on current account from 0.5% to 6.2% of GDP between 1972 and 1974. Net long-term capital inflows rose from \$110 million in 1972 to \$840 million in 1974. This inflow went to both public and private sectors, including substantial credits for mineral resource development. This inflow permitted a \$290 million increase in net international reserves in spite of the widened resource gap.

Developments During 1975

17. During 1975, the Government strove to reverse the deteriorating financial trends through a series of tax and price measures. In January 1975 indirect taxes were increased and subsidies on food were reduced. On June 30 a second set of measures included: (a) increases in prices of basic foodstuffs, petroleum (ranging from 25% for diesel fuel to 100% for premium gasoline), and other basic goods such as steel and cement; (b) a 40% reduction in the price of fertilizers; and (c) strict controls on salary adjustments in the public and private sectors. Subsequently, on September 26, the Sol was devalued by about 14%.

18. The measures taken in 1975 were directed at attacking some of the basic causes of Peru's financial difficulties: excessive growth of aggregate demand with the resulting fall in national savings, the stagnation of food output and the slow growth of export volume. However, the country's financial position remained under strong pressures largely because of two factors. In the first place, export earnings fell because of the contraction in world demand for, and prices of, Peru's exports, adverse weather conditions and labor strikes. The decline in export demand, together with work stoppages, resulted in a drop in mining output;

abnormal ecological conditions limited the recovery of fishmeal output and contracted the catch of food fish; while bad weather conditions, inadequate supply and high prices of fertilizers and other production inputs, and inadequate price and marketing policies followed in previous years affected agricultural output. Secondly, while gross domestic investment rose to 19% of GDP, the measures taken were not able to stop the fall in savings and the resource gap widened to over 9% of GDP. The fall in savings was principally caused by the large losses of state enterprises marketing petroleum, foodstuffs and fertilizers. The deterioration of incentives for private sector financial savings, caused by the increasingly negative real interest rates and the intensification of inflationary expectations, also contributed to this erosion. Import demand grew rapidly not only because of the expansionary financing of public sector deficits but also because of the sharp increase in food and petroleum imports and because the new investments (mainly in petroleum and mining) had a high import content. Net long-term capital inflows totalled an estimated \$1.2 billion in 1975, but were not sufficient to finance the current account deficit and net international reserves fell from \$690 million in December 1974 to around \$150 million, equivalent to less than four weeks of merchandise imports.

Future Prospects

19. In the next few years Peru's finances--external and domestic--will be under considerable pressure. Maintaining the development momentum while at the same time restoring financial equilibrium will depend primarily on: (a) additional measures to reduce the growth of consumption and increase the rate of savings; (b) a rapid expansion of export volume, not only from mining and petroleum, but also from manufacturing, tourism and fisheries; and (c) the availability of long-term foreign capital on softer terms than in 1975.

A. Short-Term Prospects for 1976

20. In 1976 much of the effort to restore financial equilibrium--by reducing the balance of payments deficit and the rate of inflation--will have to be made internally. Although export volume may recover from the sharp fall in 1975, it will remain well below the 1972 level, while terms of trade this year are not likely to improve much. At the same time, Peru may have difficulty in obtaining large net additional funds on suitable terms from commercial banks because of their already high exposure in Peru and the generally tight conditions of international capital markets. Even if Peru is successful in obtaining as much as \$1 billion in new commitments (of which half would have to come from commercial banks), import volume will have to be cut by around 15% to avoid

further losses of net international reserves. Since the level of investment is not expected to rise above the record levels achieved in 1975, capital imports may drop somewhat. However, the largest import contractions will have to come in petroleum consumption and in imports of consumer and intermediate goods. The Government is now negotiating a stand-by agreement with the IMF that would allow Peru to make use of its first credit tranche, the oil facility and possibly the compensatory finance facility. Total IMF resources may thus increase gross international assets by some \$100 million. Peru's interest in seeking a stand-by is to a large extent motivated by pressures from commercial banks who consider it a precondition for substantial new lending. (Tables IV and V show projections of the balance of payments and capital flows for 1976).

21. Aware of the above factors, the Government on January 10, 1976 approved additional austerity measures aimed at reducing the public sector deficit, discouraging imports and stimulating agricultural production. The measures approved include: (a) further increases in prices of petroleum products and basic foodstuffs; (b) increases in taxes on income, property and consumption abroad; (c) addition of agricultural cooperatives and public enterprises to the income tax rolls; (d) a 5% cut in central government budgeted current expenditures; and (e) licensing for all imports. The January measures will have an estimated financial impact of 2.1% of GDP and thereby substantially reduce the public sector deficit (see Table III). The measures should also reduce the growth of petroleum consumption and help contract imports.

22. Although the January action was a clear sign of the Government's determination to resolve the present financial crisis, additional measures may be required in 1976 to increase savings still further in the public and private sectors. In the first place, even after taking into account a maximum level of banking system credit, the unfinanced gap of the public sector may still amount to 1.5% of GDP ^{1/} (see table IV). Secondly, measures should also be taken to stop capital flight abroad and to stimulate the growth of banking system liabilities with the private sector. As part of the stand-by agreement now being negotiated with the IMF, the Government is reportedly ready to increase taxes further, streamline public investment, raise interest rates and place ceilings on domestic credit to the public sector.

^{1/} Table IV attached shows a projection of banking system accounts consistent with the balance of payments projection discussed above. These monetary projections provide, as a residual, the amount of credit that could be granted to the public sector without restricting credit to the private sector for productive purposes. The projections assume that the velocity of circulation of money will not increase much during 1976.

B. Long-Term Prospects

23. Starting in 1977 the balance of payments situation is likely to begin to improve as the volume of mining exports will increase substantially. In addition, it is likely that Peru will virtually eliminate its dependence on imported petroleum by the end of 1977 and will thereby save some \$350 million per year by 1981 (at 1975 prices). The extent of the improvement beyond 1976 will depend on actions in various fields. To ensure a high GDP growth rate, investment outside the public sector should be stimulated and the efficiency of production increased. At the same time, since it is now considered unlikely that Peru will become a substantial net exporter of petroleum in the foreseeable future, new exports will have to be developed. Peru has a large potential to develop tourism, has excellent natural conditions to expand an export-oriented food fish industry and could rapidly expand its level of manufacturing exports. However, as discussed in detail in the agricultural and industry sector briefs, raising investment, productive efficiency and exports will require important changes in policies. Maintaining a solid balance of payments position and reducing inflation growth will also require continued efforts to increase savings and reduce dependence on foreign borrowing.

TABLE I: PERU: NATIONAL ACCOUNTS INDICATORS, 1973 - 1975

(Percentages)

	SHARE OF GDP (Current Prices)				AVERAGE ANNUAL GROWTH RATES (Constant Prices)			
	1968-70	1971-72	1973-74	1975 ^{1/}	1969-70	1971-72	1973-74	1975
Consumption	83.7	84.6	87.1	90.5	6.9	4.7	10.4	5.1
Investment (GDI)	13.3	14.6	16.0	19.0	5.6	11.9	17.9	17.6
Gross fixed investment	(12.6)	(12.7)	(14.7)	(17.5)	(7.2)	(8.5)	(18.6)	(18.2)
Change in stocks	(0.7)	(1.9)	(1.3)	(1.5)	(-21.0)	(75.0)	(10.0)	(11.1)
Resource Use	97.0	99.2	103.1	109.5				
Gross Domestic Product	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>5.7</u>	<u>5.5</u>	<u>6.0</u>	<u>3.9</u>
Resource Balance	3.0	0.8	- 3.1	- 9.5				
Exports of goods and n.f.s.	(20.0)	(15.7)	(15.6)	(12.1)	(- 1.3)	(1.5)	(-10.1)	(- 3.1)
Imports of goods and n.f.s.	(17.0)	(-14.9)	(-18.7)	(-21.7)	(2.5)	(1.9)	(23.0)	(17.0)
Gross Domestic Savings	16.3	15.4	12.9	9.5	-	9.1	-16.7	- 5.4
Gross National Savings (GNS) ^{2/}	14.7	14.5	11.8	8.1	3.3	8.4	-18.7	-10.7
G N S - G D I ^{3/}	1.4	- 0.1	- 4.2	-10.9				
Terms of Trade Index (1970 = 100)	91.3	87.6	114.8	100.5				
Domestic Inflation (yearly % change) ^{4/}					7.6	4.9	16.4	22.6

^{1/} Preliminary estimate.

^{2/} Includes net foreign current transfers.

^{3/} Gross national savings (including net current transfers) minus gross domestic investment equal to the balance of payments current account balance.

^{4/} Implicit GDP deflator.

TABLE II: PERU: PUBLIC SECTOR FINANCES, 1973 - 1976 ^{1/}

(Percent of GDP)

	E S T I M A T E D		PRELIMINARY ESTIMATE	PROJECTED
	1973	1974	1975 ^{2/}	1976 ^{3/}
Public Sector Savings	<u>1.4</u>	<u>2.3</u>	-2.5	-1.5
Central Government	1.7	2.8	1.8	1.3
Public Enterprises	-0.4	-0.5	-4.3	-2.7
Social Security	0.9	1.1	1.2	1.1
Other	-0.8	-1.1	-1.2	-0.3
Capital Revenues	-	0.3	-	-
Capital Expenditures	6.6	8.3	7.8	8.3
Fixed Investment	(5.5)	(7.7)	(6.9)	(7.5)
Overall Deficit	<u>-5.2</u>	<u>-5.7</u>	<u>-10.3</u>	<u>-9.8</u>
Amortization of Foreign Debt ^{4/}	2.5	1.9	1.8	1.4
Total Funds Required	-7.7	-7.6	-12.1	<u>-11.2</u>
Foreign Borrowing, Gross ^{4/}	5.8	6.9	7.5	5.9
Domestic Financing, Net	1.9	0.7	4.6	1.6
Initial Unfinanced Gap	-	-	-	<u>3.7</u>
January 1976 Measures ^{5/}	-	-	-	2.1
Remaining Unfinanced Gap	-	-	-	<u>1.6</u>

^{1/} These are IBRD estimates since Government official figures are not available. Estimates are particularly rough for state enterprises and the social security.

^{2/} Except for the Central Government, IBRD staff estimates based on cash flow projections of enterprises based on actuals to September 1975.

^{3/} IBRD staff projection. For assumptions on GDP estimate see Table III.

^{4/} During 1973-74 Peru prepayed various loans with new borrowings with better terms. These are excluded from both gross disbursements and amortization of foreign debt to highlight the basic trends.

^{5/} See Table III.

SOURCE: Central Bank, Ministry of Economy and Finance, various state enterprises, IMF and IBRD staff estimates.

TABLE III: PERU: FINANCIAL YIELD OF JANUARY 1976 MEASURES

	Soles Billion	Share of GDP <u>1/</u>
Total financial impact	<u>15.0</u>	<u>2.1</u>
Tax measures <u>2/</u>	5.0	0.7
Increase in revenues of state enterprises from rise in prices of petroleum and foodstuffs <u>3/</u>	8.0	1.1
Central government current expenditure cuts <u>2/</u>	6.0	0.8
Increase of public sector current expenditures due to wage increases decreed <u>3/</u>	-4.0	-0.5

1/ Assumes in 1976 no real growth of GDP, but a 25% rise in inflation.

2/ Government estimate.

3/ Preliminary IBRD staff estimate.

SOURCE: Ministry of Economy and Finance and IBRD staff estimates.

TABLE IV PERU: PROJECTIONS OF BANKING SYSTEM CREDIT TO THE PUBLIC SECTOR, 1976

	END OF YEAR BALANCES						YEARLY CHANGES (FLOWS)				
	ACTUALS				EST. 1/	PROJECTIONS 2/	ACTUALS			ESTIMATED	PROJECTIONS
	1971	1972	1973	1974	1975	1976	1972	1973	1974	1975	1976
----- (In Millions of Soles) -----											
Net International Reserves	13.9	15.4	15.9	26.8	6.9	6.9	1.5	0.5	10.9	-19.9	-
Net Domestic Assets	51.4	62.5	80.7	92.9	134.4	163.5	11.5	18.2	12.2	41.5	29.1
Credit to public sector	15.3	17.7	27.6	26.3	51.4	61.6	2.4	9.9	- 1.3	25.1	10.2
Credit to private sector	48.0	59.0	73.2	85.2	106.0	131.0	11.0	14.2	12.0	20.8	24.9
Capital and reserves	-15.2	-16.5	-20.0	-24.4	-29.0	-35.0	- 1.3	- 3.5	- 4.4	- 4.6	-6.0
Other	3.3	2.3	- 0.1	5.8	6.0	6.0	- 1.0	- 2.4	5.9	0.2	-
Foreign Liabilities, Medium and Long Term	2.2	2.6	6.2	9.4	13.0	13.0	0.4	3.6	3.2	3.6	-
Private Sector Liabilities	63.2	75.2	90.4	110.3	128.3	157.4	12.0	15.2	19.9	18.0	29.1
Money	36.4	43.9	53.1	67.4	n.a.	-	7.5	9.2	14.3	n.a.	-
Quasi-money	16.4	17.3	19.6	22.7	n.a.	-	0.9	2.3	3.1	n.a.	-
Bonds and other	10.3	14.0	17.6	20.2	n.a.	-	3.7	2.6	2.6	n.a.	-
G D P	264.4	294.7	355.9	448.6	572.4	715.5					
Annual Inflation Rate (percent)	4.5	5.3	14.6	18.2	22.6	25.0					
----- Shares of G D P -----											
Net Domestic Assets	19.4	21.2	22.7	20.7	23.4	22.8					
Credit to public sector	5.8	6.0	7.8	5.9	8.9	8.6					
Credit to private sector	18.2	20.0	20.6	19.0	18.5	18.3					
Private Sector Liabilities	23.9	25.5	25.4	24.6	22.4	22.0					
Money	13.8	14.9	14.9	15.0	n.a.	-					
Quasi-money and other	10.1	10.6	10.5	9.6	n.a.	-					

1/ Preliminary estimate.

2/ 1976 projections assume: (i) no GDP growth in 1976; (ii) no change in reserves; (iii) credit to the private sector (as a share to GDP) would fall slightly from 18.5 to 18.3 percent, reflecting the stagnation of the economy; and (iv) that the velocity of circulation of money will not increase much and liabilities to the private sector (as a share to GDP) would fall only from 22.4 to 22 percent. The projection then obtains as a residual the maximum amount of credit that could be granted to the public sector assuming an inflation rate of 25 percent. Of course, these would be minimum inflation rates since the assumption of a small growth in velocity may be unrealistically optimistic.

Source: D.F., Central Bank, and IBRD staff estimates.

TABLE V: PERU: BALANCE OF PAYMENTS INDICATORS, 1973 - 1976

(In Millions of Dollars)

	A C T U A L S		ESTIMATED	PROJECTED
	1973	1974	1975 <u>1/</u>	1976 <u>2/</u>
Exports of Goods and n.f.s.	1,347	1,842	1,745	2,105
Merchandise	(1,112)	(1,506)	(1,379)	(1,700)
Other	(235)	(336)	(375)	(405)
Imports of Goods and n.f.s.	-1,400	-2,442	-3,110	-2,948
Merchandise	(-1,033)	(-1,909)	(-2,482)	(-2,303)
Other	(- 367)	(- 533)	(- 628)	(- 645)
Resource Balance	- 53	- 600	-1,356	- 843
Net Factor Income Payment	- 163	- 173	- 252	- 256
Net Transfers Received	42	48	46	46
Current Account Balance	- <u>174</u>	- <u>725</u>	-1,563	-1,053
Long-Term Capital, Net	<u>406</u>	<u>839</u>	<u>1,155</u>	<u>953</u>
Private	72	126	329	217
Public	334	713	826	736
Disbursements	(690)	(1,093)	(1,120)	(1,014)
Amortization	(- 357)	(- 380)	(- 294)	(- 278)
Capital n.e.i.	- <u>219</u>	<u>168</u>	- <u>132</u>	<u>100</u>
Net International Reserves	- 13	- 282	540	-
<u>Memorandum Items</u>				
Stock of Net International Reserves	405.1	687.1	147.1	147.1
Coverage of Imports (weeks)	20	19	3	3
Debt Service, Total	<u>366</u>	<u>467</u>	<u>551</u>	<u>555</u>
Public Debt	312	406	493	485
Private Debt	54	61	68	70
Debt Service Ratio, Total <u>3/</u>	<u>27.2</u>	<u>25.2</u>	<u>31.0</u>	<u>26.4</u>
Public Debt	23.2	22.0	28.1	23.0
Private Debt	4.0	3.3	3.9	3.3
Debt Outstanding and Disbursed	<u>1,338</u>	<u>2,051</u>	<u>2,877</u>	<u>3,613</u>

1/ Preliminary IBRD staff estimate.

2/ IBRD staff projection.

3/ Ratio of debt service to exports of goods and n.f.s.

SOURCE: Central Bank and IBRD staff estimates.

The Consultative Group Meetings

1. Starting in 1972, the Bank has chaired three meetings of the Consultative Group for Peru. The meetings have helped to promote better understanding of Peru's development objectives and public investment program. This has resulted in an increase of official bilateral assistance and of the awareness and interest of export financing agencies and potential suppliers in specific projects. Preparation for the meetings has also helped gradually to build up expertise within the Peruvian Government in establishing investment priorities and in designing sound financial plans.

2. The last meeting of the Consultative Group was in April 1975. The meeting recognized the considerable effort made by the Government in recent years to modernize the economy, lay the foundations for rapid economic growth, and improve the capacity to generate development projects. The need to increase the savings rate was also emphasized. The meeting reviewed the list of projects presented by the Peruvian Government, concluded that project loan commitments of the order of \$950 million annually would be required during 1975-76, recommended that external financing be provided on terms as favorable as possible (including assistance on concessional terms) and agreed that some local-cost financing was needed. To ensure that the burden of debt service does not become excessive in the late seventies and early eighties, at least one half of new loan commitments should be obtained on terms similar to those of official lending agencies. This is comparable with what was achieved during 1971-74. The next Consultative Group meeting is scheduled for Spring 1977. (The Chairman's speech and the Press Release containing more details on the 1975 meeting are attached.)

Medium- and Long-Term Foreign Loans to the Public Sector and External Public Debt

3. Attached Table I shows the sources and uses of medium- and long-term loans to the public sector during 1968-75 and projections for 1976. During 1968-70 commitments averaged less than \$200 million annually. Thereafter they rose sharply to an annual average of almost \$1.1 billion in 1973-74 and \$0.9 billion in 1975. The rapid increase was mainly the result of the improved creditworthiness for foreign borrowing of Peru, the sharp increase in public investment and during 1974-75 large requirements of commercial borrowing for balance of payments support. Other contributing factors were the settling of outstanding investment disputes and the growing interest of Western European countries in the Peruvian development experiment.

4. While total public sector external debt (outstanding and disbursed) more than tripled between 1970 and 1975 - from \$0.9 billion to \$3.6 billion -, average terms markedly deteriorated. Average maturities fell from 17 years in 1970 to 14.3 years in 1974, since over 65% of net disbursements during 1970-74 came from commercial banks. During 1975, the situation worsened since not only did commercial banks continue to account for a high 69% of net disbursements but their terms hardened. The average terms in 1975 of commitments from commercial banks were: 5.8 years maturity (including 2.3 years of grace) and a 9.5% interest rate. Thus, while actual inflows of external loans during 1975 were similar to what was expected by the Consultative Group, the average terms were much harder.

5. The public debt service ratio which was 22% in 1974 rose to an estimated 28% in 1975 reflecting both a sharp increase in interest payments and the decline in the value of merchandise exports. During 1976 the public debt service ratio is expected to fall to 23% because of the recuperation in exports projected and a small decrease in debt service payments. However, given the very serious foreign liquidity squeeze the country is now going through, this level of debt service will place a heavy burden on the balance of payments. The Government is explicitly committed to give first priority in foreign exchange allocation to debt service payments.

6. During 1977-80, debt service payments will rise rapidly. We are now preparing new balance of payments projections for 1976-85 that incorporate both the developments during 1975 and the more pessimistic prospects for petroleum production. Preliminary results suggest that the public debt service ratio may rise further to 30-32% during 1978-80, but may decline gradually in the 1980s if the Government is successful in increasing national savings and stimulating non-traditional exports and if more suitable lending terms are obtained in future years.

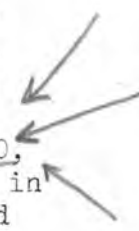


Table I

PERU: SOURCES AND USES OF MEDIUM AND LONG-TERM LOANS TO THE PUBLIC SECTOR, 1968 - 1975
(Annual Average in Millions of Dollars)

	C O M M I T M E N T S					D I S B U R S E M E N T S				
	1968-70	1971-72	1973-74	1975	1976	1968-70	1971-72	1973-74	1975 ^{1/}	1976 ^{2/}
SOURCES										
Repayable in Foreign Currency	182.0	357.1	1,065.1	852.1	1,032.0	216.2	243.5	873.2	1,102.3	1,014.1
International Agencies	17.1	-	54.4	145.4	239.0	14.6	15.2	10.2	32.0	94.0
I B R D	10.0	-	37.5	76.5	144.0	9.7	10.8	8.9	15.7	n.a.
I D B	5.3	-	16.1	45.5	80.0	3.0	4.4	0.7	13.7	n.a.
Others	1.7	-	0.8	23.4	15.0	1.9	-	0.6	2.6	n.a.
Governments	52.9	141.2	172.8	212.8	236.0	41.5	79.0	126.6	238.3	252.0
USA	6.5	58.0	31.7	28.0	n.a.	9.8	30.7	40.6	59.4	n.a.
Canada	8.7	17.9	36.9	28.9	n.a.	3.5	14.8	27.1	43.5	n.a.
Germany	30.3	-	11.0	2.7	n.a.	16.2	7.3	1.0	15.6	n.a.
Japan	-	28.6	10.0	-	n.a.	-	3.7	25.9	9.0	n.a.
Centrally Planned Economies	-	21.0	39.0	45.1	n.a.	-	3.3	15.3	27.7	n.a.
Others	7.4	15.7	44.2	107.0	n.a.	17.4	21.0	16.9	83.1	n.a.
Suppliers	11.0	71.1	208.7	45.9	60.0	65.3	33.8	153.5	172.9	112.0
Commercial Banks	26.5	123.5	547.8	448.0	497.0	29.3	65.5	489.1	590.3	556.0
Unclassified	74.5	21.3	81.4	-	-	65.5	50.0	93.8	68.8	-
Repayable in Local Currency	17.6	23.6	12.7	-	-	13.3	22.7	18.3	17.7	-
T O T A L	199.6	380.7	1,077.6	852.1	1,032.0	229.5	266.2	891.5	1,120.0	1,014.0
USES										
Petroleum Imports	-	-	-	65.0	100.0	-	-	-	16.0	133.0
Food Imports	10.1	58.8	53.8	52.3	65.0	6.2	51.0	56.2	52.8	65.0
Debt Refinancing	45.2	58.9	92.6	180.0	250.0	37.5	51.0	121.0	200.0	250.0
Debt Prepayment	2.2	-	114.0	-	-	3.4	-	114.0	-	-
Other	142.1	263.0	817.4	551.8	517.0	182.4	164.2	600.3	851.2	566.0
Memorandum Items										
NET DISBURSEMENTS						101.6	64.2	523.4	826.4	736.0
International Agencies						5.6	5.2	3.1	17.1	80.0
Governments						33.8	45.8	36.1	148.1	106.0
Suppliers						18.6	8.8	99.0	98.7	57.0
Commercial Banks						7.7	41.2	341.5	568.3	515.0
Repayable in Local Currency						13.3	22.7	18.3	23.3	-
Unclassified						22.6	41.9	31.6	29.1	23.0
NET TRANSFERS						56.9	2.2	418.8	634.8	518.0
International Agencies						- 2.7	- 5.4	- 13.4	7.7	69.0
Governments						27.4	33.4	8.1	126.1	75.0
Suppliers						- 2.5	- 24.8	95.4	30.2	33.0
Commercial Banks						- 3.0	30.9	298.4	466.4	366.0
Repayable in Local Currency						13.3	22.7	18.3	23.3	-
Unclassified						24.4	54.6	12.0	68.9	25.0

1/ IBRD staff estimate

2/ IBRD staff projection

SOURCE: Ministry of Economy and Finance, Central Bank and IBRD staff estimates.

Table II: EXTERNAL PUBLIC DEBT INDICATORS 1970-76

(in percentages except as otherwise indicated)

	Actuals			Est.	Proj.
	1970	1973	1974	1975 ^{1/}	1976 ^{2/}
Public external debt outstanding and disbursed (million \$)	910.9	1,338	2,051	2,877	3,613
Public external debt/GDP	17.1	16.9	20.6	22.6	22.7
Debt service, total (million \$)	<u>260</u>	<u>366</u>	<u>467</u>	<u>561</u>	<u>555</u>
Public debt	199	312	406	493	485
Private debt	61	54	61	68	70
Debt service ratio, total ^{3/}	<u>21.4</u>	<u>27.2</u>	<u>25.2</u>	<u>31.0</u>	<u>26.4</u>
Public debt	16.4	23.2	22.0	28.1	23.0
Private debt	5.0	4.0	3.3	3.9	3.3
Average terms of debt ^{4/}				<u>4/</u>	
Maturity (years)	17.0	14.7	14.3	9.1	na
Grace (years)	3.5	4.1	4.4	2.5	na
Interest	5.4	6.6	7.3	8.7	na
Grace element	28.0	20.0	16.0	na	na

^{1/} IBRD staff estimate.^{2/} IBRD staff projection.^{3/} Ratio of debt service to exports of goods and non-factor services.^{4/} For 1975, average terms of commitments.

PRESS RELEASE

Meeting of Consultative Group for Peru

A meeting of the Consultative Group for Peru, sponsored by the World Bank was held in Paris on April 16 and 17, 1975, with the purpose of coordinating external financing of the development efforts of Peru. The meeting was chaired by Mr. Enrique Lerda, Director of Country Programs Department, Latin America and the Caribbean Regional Office of the Bank.

The delegation of the Government of Peru was headed by General Amilcar Vargas Gavilano, Minister of Economy and Finance, and included the Head of the Planning Office, General José Loayza Amezcuita and several other high officials of the administration.

The meeting was attended by the representatives of the Governments of Belgium, Canada, Finland, France, Federal Republic of Germany, Italy, Japan, the Netherlands, Spain, the United Kingdom and the United States. Representatives of the International Monetary Fund, the Inter-American Development Bank, the Permanent Executive Commission of the Economic and Social Inter-american Council (CEPCIES), the United Nations Development Programme, and observers from Switzerland and the Organization for Economic Cooperation and Development also attended.

The Group discussed the development prospects of Peru and its needs for foreign financing, on the basis of a report prepared by the World Bank. The Head of the Peruvian delegation made a comprehensive presentation setting forth the objectives of Government development strategy and the policies which will be pursued during the next several years. He emphasized the twin goals of increasing domestic food production and rural incomes, and developing at an accelerated pace basic industries, petroleum, mining and

essential infrastructure. The Minister described the recent measures for reducing non-essential consumption and for increasing domestic savings, in the fields of taxation and curtailment of consumption subsidies. He indicated that the Government was considering measures to mobilize additional domestic resources in the near future, including readjustment of the domestic price of petroleum products.

The Group agreed that Peru had made substantial progress in achieving the objectives of structural socio-economic change and laying foundations for rapid economic growth. The Group noted the increase in Peru's capacity to generate development projects. It noted Peru's efforts to diversify its production and export structure and its success in expanding non-traditional exports. The Group noted the progress in the implementation of agrarian reform, and indicated its readiness to support investment programs in the rural areas, particularly in the depressed Andean highlands. The Group expressed its readiness to cooperate with the Peruvian authorities in the preparation of feasibility studies in the rural sector, considered of high priority for economic and social development.

The Group reviewed Peru's external capital requirements and agreed that to achieve the necessary disbursement levels, project loan commitments of the order of US\$950 million annually would be needed in the three-year period 1975-77, compared to an average of \$530 million achieved in the two years 1973-74. It was of particular importance to assure that the required commitment level be reached in 1975 and 1976. The Group discussed the list of projects prepared by the Government, amounting to \$3.5 billion for 1975-77, an amount which should enable the project loan commitments to reach the desirable level. The Group further agreed that some local cost financing of projects was needed. The Group also agreed that it was important that suitable technical assistance be provided to enable the project financing to be used to maximum advantage. In addition, financing not tied to specific projects will continue to be necessary.

The Group noted that Peru was successful in mobilizing financing from the commercial markets, despite the deterioration in the world financial situation. It agreed, however, that the cost of this borrowing was such that it could only be relied upon as a supplementary source of finance, and emphasized the need for intensification of efforts at domestic resource mobilization.

The Group noted the hardening in Peru's average terms of borrowing, and recommended that external financing should be provided on as favorable terms as possible including assistance on concessional terms. It was suggested that efforts should be made to blend government-to-government assistance with the credits made available under the export credit guarantee arrangements. The Group also agreed that for several of the large projects included in the project list, cofinancing would be desirable. The Group noted the Government's determination to pursue a careful debt management policy, and supported the Government's intention to ensure that borrowing decisions are consistent with project priorities and sound financial planning.

A noteworthy feature of the meeting was the lively interest expressed by Group members in many of the projects included in the project list.

It was agreed that the Group would meet again in approximately eighteen months.

THE AGRICULTURAL SECTOR

1. Although contributing only 15% of Peru's GDP, agriculture employs more than 40% of the labor force. In addition, agro-based industries account for around 30% of employment and 40% of value added in manufacturing. Agricultural output, and especially food production, has lagged behind population growth for at least the past 15 years. The resulting growth of food imports has placed increasing pressures on the balance of payments, and, furthermore, government subsidies are a serious drain on the public sector budget and national savings. At the same time that raising the sector's poor performance has become increasingly critical for future economic progress and for providing employment for the rapidly growing rural population, success of the agrarian reform has taken on crucial political significance as a symbol of the Government's program for transforming Peruvian society.

The Resource Base

2. Any discussion of Peruvian agriculture must distinguish between the very different conditions of the country's three major regions: (a) the narrow Coastal Zone along the western edge of the country; (b) the Sierra or Highland Zone that separates the coast from the western jungle; and (c) the jungle itself. Coastal agriculture encompasses only about one-fourth of arable land but produces around two-thirds of the value of agricultural output. Rainfall is near zero, and virtually all the land is irrigated. Limited possibilities exist for expanding land under cultivation in the Coastal region. Approximately 150,000-200,000 hectares of land have been wholly or partially lost because of excess salinity, and relatively modest investments in drainage and improved water utilization could bring these lands back into full production. The sector is highly productive and commercialized, offers good conditions for a variety of crops and livestock, and is close to the major urban markets. Prior to the land reform, coastal agriculture consisted of large sugar and cotton plantations using mostly wage labor, large rice estates, and small truck farms. Rapid mechanization in the 1960s was producing increasingly serious problems of labor displacement and urban migration. The plantations and large estates have since been converted to worker-owned cooperatives. (see below). Cotton, sugar, and coffee are the major export crops.

3. In contrast, the Sierra is characterized by very low productivity and subsistence agriculture. Climate, soils, and water availability are poor, and the man-land ratio is extremely high. Commercialization is further inhibited by high transport costs to major markets and opportunities for non-farm employment are limited. Prior to the agrarian reform, the land tenure pattern consisted of (a) large feudal haciendas in which the peasants (colonos) enjoyed usufruct rights to small plots of land in exchange for cash rents, labor obligations and/or a share of the crop; (b) the communally owned lands of the Indian communities; and (c) smallholder cropping. Cereals, tubers, and livestock are the major products. In the past, only lip service has been paid to the Sierra. Most of Peru's rural population subsists there, often under the most precarious conditions. Although increasing numbers have left the Sierra in recent decades to crowd into the urban slums of the coast, the predominantly Indian peoples of the region are traditionally passive and politically apathetic. Very little land suitable for agriculture remains idle, although some productivity gains are possible.

4. The jungle covers two-thirds of Peru but currently accounts for less than 10% of total population. The region has become increasingly important strategically because of oil discoveries and the completion of the Transamazonic Highway across Brazil. Nevertheless, because of the difficulties of transport, its inhospitable climate, health risks, and poor soils, the jungle offers very limited long-term potential for agriculture. The most promising area for development in the jungle region lies along lower eastern slopes of the Andes. (See the discussion below of the Huallaga projects).

Land Reform

5. The slow growth of agricultural output and the extreme poverty of Peru's rural masses, particularly in the Sierra, came increasingly to be blamed on the unequal distribution of land and the feudal land tenure system. The first land reform law was passed in 1964, but its major results were uncertain among landowners, with the consequent deterioration of investment and conservation, the expulsion of many colonos, and the frustration of peasant expectations. Large-scale land invasions became increasingly frequent. The land reform launched by the Military Government in 1969 has substantially reduced the amount of land in private hands and eliminated the hacienda or colonato system. By the end of 1976, some 10 million hectares are to have been redistributed in favor of an estimated 400,000 peasant families, or roughly one-third of the rural population 1/. By the end of October 1975, 7.3 million hectares had been expropriated, of which 6.1 million hectares had been adjudicated and assigned to 251,000 families.

1/ This represents a substantial scaling down of the 13 million hectares originally targeted for the end of 1975.

6. The principal institution of the Coastal reform sector is the producer cooperative (CAP), a large-scale enterprise run by its worker-owners. Management decisions are, at least in theory, democratically taken. Approximately 13% of agricultural land is now operated under the CAP form of organization. Another 12% of land, chiefly in the Sierra, is organized along similar lines referred to as the agricultural society (SAIS), except that for largely political reasons the surrounding peasant communities share in the cooperative's profits and management (but not in its work). Peasant communities continue to occupy some 32% of agricultural land. Efforts to restructure the communities more along CAP lines have been strongly resisted and, at least for the time being, largely abandoned. The remaining 43% of the land is farmed by small and medium-sized private landowners, frequently associated in primary or secondary-level cooperatives.

7. The institutional structure of Peruvian agriculture has been dramatically changed by the agrarian reform program. The results achieved in terms of output, employment, and income distribution have thus far been positive but small. The best performance in absolute terms has been on those plantations and estates which had been most efficiently run prior to the reform and which have kept their former manager. Problems of decapitalization and inefficiencies due to the lack of managerial experience and technical expertise were, of course, to be expected. In addition, the cooperative model imposed by government planners has in many cases conflicted with the aspirations for independence of Peruvian peasants. The model was most easily accepted by the wage labor force of the old coastal plantations, but strikes have frequently disrupted production there, too, over issues of worker control.

8. Coastal plantation workers have improved their income shares with both increased output and the redistribution of the profits formerly accruing to the individual or corporate owners. Even as wage laborers, however, these workers were among Peru's best paid prior to reform. Gains also have been made by many former colonos in the Sierra livestock cooperatives. They now share in the profits and no longer pay rent. Although real incomes have also risen for the former colonos now organized in Sierra crop cooperatives, performance in this sector has been hampered by greater peasant resistance to collectivization, the poor resource base and abject poverty of the Indians, and by real diseconomies of large scale in highland crop production, thus far inadequately perceived by reform planners. Frustrated expectations will be an increasing problem in the Sierra and the success of the Revolution may ultimately be judged on the effectiveness of the Government's response.

The Incentive to Invest

9. A major problem currently in the agricultural sector is the uncertainty that the reform has created for the remaining small and medium private landowners, who still account for most of the food supplied to the urban markets. The Government has attempted to assuage their doubts by issuing certificates of exemption from expropriation, but these "guarantees" are heavily conditioned ^{2/}. Moreover, all public programs--e.g. credit, technical assistance--give preference to the reform sector at the expense of services previously provided the small private farmer, and much of the Government's rhetoric continues to berate the private farmer. Production incentives and possibilities are also hampered by extensive price controls at all levels of distribution. Recent price increases for farm products are a step in the right direction. The marketing system of crops for the domestic market is seriously inadequate, and the Government's reaction to frequent bottlenecks tends to be more uncoordinated state intervention that complicates rather than solves the problem and further weakens the investment climate.

10. A general criticism of the agrarian reform, implicit in the above discussion, is that almost the entire attention has been given to the process of expropriation and structural reorganization at the expense of technical assistance and other programs in both the reform and private sectors. Long-term credit for investment, for example, has been severely constrained by the shortage of qualified field personnel in the national Agrarian Bank. The recent division of the Agriculture Ministry into two ministries, one charged with responsibility for production-oriented programs, has not succeeded in resolving the problem and has created additional difficulties of coordination. At the same time, little has been done to alleviate the plight of minifundistas who, particularly in the Sierra, represent the most extreme rural poverty.

Government Policy

11. Consistent with its autarkic philosophy, a principal policy objective of the Government is import substitution. Meat imports have been significantly reduced through a combination of restrictions on consumption and the promotion of alternative foods. In addition, farmers are legally obliged to devote at least 40% of their arable land to foodcrops, regardless of comparative advantage. Nevertheless, Peru is not richly endowed for agriculture, and despite these efforts, the growth of food imports is likely to continue, at least through the medium term. Continuing efforts must be made to raise agricultural output in order to minimize the balance of payments impact of food imports in the face of rapid population growth,

^{2/} The Government has recently issued a blanket exemption to private holdings of 15 hectares or less. While thereby increasing the security of these farmers, the move may paradoxically have increased the uncertainties felt by the owners of larger farms, now limited to 50 hectares.

and because the reduction of poverty in Peru is closely tied to progress in the agricultural sector. Any viable long-term growth strategy, however, must include the expansion of mineral and manufacturing exports to pay for food imports.

Bank Lending Strategy

12. The Bank lending strategy in the agricultural sector is aimed at helping the Government achieve two principal objectives: (a) increased production in the coastal areas; and (b) improved productivity and income conditions in the Sierra. Toward these ends, the Bank has in the past granted loans for irrigation projects and agricultural credit; we have recently appraised an irrigation land rehabilitation project and are now assisting in the preparation of rural development projects in the Sierra.

Historical Background

1. Peru is a mineral rich country with important proven deposits of copper, zinc, silver, iron ore and lead. Exploitation of these resources dates back to pre-Columbian days with the Incas mining gold, silver and copper to fashion them into adornments, weapons and utensils. During the nearly three centuries of Spanish colonial rule, mining--particularly of precious metals--continued but after independence in 1821, its importance to the economy was overshadowed by the exploitation of nitrates and guano. Several important developments accounted for a resurgence of the mining industry. The first was the War of the Pacific with Chile in 1879 which cost Peru its nitrate-rich Atacama desert provinces and forced the country to look to other minerals to make up for lost nitrate-generated revenues. The second was the construction in the late 1800s of a railroad opening up the Sierra region, where most of the mineral deposits lay. The enactment of the 1890 mining law, offered liberal tax incentives and attracted capital--particularly from overseas sources--to the sector. A third important factor was the development of modern extraction techniques permitting the exploitation of lower grade ore bodies.

2. The 1950s were years of particularly impressive growth for Peruvian mining. The enactment of a simplified mining code with a clear and favorable tax regime greatly improved the investment climate, and foreign capital flowed into the sector. Copper production increased from 30,000 MT to 180,000 MT during the decade, the output of lead, zinc and silver more than doubled, and exploitation of Peru's iron ore potential began. In total, the value of mineral production rose from \$41 million in 1950 to almost \$200 million by 1960.

3. In contrast to the previous decade, the 1960s were years of relative stagnation in the sector, characterized by decreasing investor confidence and little investment. After the 1968 coup, the Government began to assume a more active role within the sector. The Cerro de Pasco Corporation, now CENTROMIN, was nationalized in early 1974 and the Marcona Mining Company, now HIERROPERU, in mid-1975. The Government has also taken over all marketing of metals and has developed an ambitious expansion program (detailed below). Compensation has been paid for Cerro de Pasco, and a compensation package for Marcona is being negotiated.

Importance to the Economy

4. Today, mining accounts for almost half of the country's export earnings, 7 percent of GDP, and up to 10 percent of

government revenues. Moreover, it provides direct employment for approximately 50,000 persons. Although this is only 2 percent of Peru's work force, mining is an important source of employment in the remote and less developed Andean region.

5. Export volume has increased in recent years only marginally and export value has been determined mainly by world prices. Export value rose from \$465 million in 1970 to \$875 million in 1974 but fell back to an estimated \$567 million in 1975. Peru accounts for about 12 percent of world exports of zinc and lead, 1% of silver and 5% of copper. Since copper constitutes roughly 40 percent of Peru's mineral exports, variations of its price have a strong impact on the country's exports. Despite large fluctuations, copper prices followed a long-term upward trend in real terms from 1929 through early 1974 reaching an all-time high of US \$1.52/lb. on the London Metal Exchange, in early 1974. Since then, copper prices have fallen sharply to below US \$0.55/lb., mainly because of the rapid slowdown in world economic growth. In November 1974 the Conseil Intergouvernemental des Pays Exportateurs de Cuivre (CIPEC)--of which Peru is an important member--agreed to reduce exports temporarily by 10 percent in an attempt to halt the decline in copper prices. A further cutback of 5 percent was agreed to in April 1975. In November 1975, the cutbacks were extended through June 1976. Some of the major U.S. and Canadian copper companies have also reduced production.

Structure of the Sector

6. Four companies--CENTROMIN, HIERROPERU, Southern Peru Copper Corporation (SPCC) and MINEROPERU--constitute the large-scale mining group which accounts for 65 percent of the country's mining output and almost 45 percent of the sector's workforce. CENTROMIN has the most diversified output producing copper, silver, zinc, lead and other metals at seven mines in Peru's central sierra. The company accounts for around one-third of the sector's output and employment. HIERROPERU operates Peru's major iron ore mining complex and SPCC, the most efficient of the large mines, is the single largest producer and exporter of copper in Peru. SPCC is the only remaining private company in large-scale mining; it is owned by four U.S. mining firms--ASARCO, Cerro Corporation, Phelps-Dodge and Newmont Mining. The fourth large-scale mining company, MINEROPERU, was established in 1970 and is entrusted with developing a series of large, high priority mining projects. To date, however, its only operation consists of a new copper refinery at Ilo.

7. Peru's medium-scale mining operations consist of a heterogenous collection of some 60 companies producing partially-treated copper, lead, zinc and silver ores. These operations, which account for 30 percent of Peru's mining output and employ 40 percent of the sector's workforce, are almost all privately owned. The small mining operations comprise more than 1,000

privately-owned small mines, most of them poorly mechanized, labor-intensive operations. A large portion of the concentrates produced by the small and medium miners is sold to CENTROMIN for smelting and refining. Expansion of medium and small-sized mines is expected to be much slower than for the large companies during the seventies, and their present share of output, will probably decline.

8. Investment planning in the sector, needs strengthening. All mining operations come under the jurisdiction of the Ministry of Energy and Mines, which is responsible also for the petroleum and power subsectors. The Ministry's Planning Department establishes investment priorities but leaves to Corporación Financiera de Desarrollo (COFIDE), the primary responsibility for financing the investment projects of the state-owned enterprises. COFIDE is relatively inexperienced in the mining industry and has shown little initiative in helping the public sector companies with planning their investment programs. Similarly, the planning Department of the Ministry of Energy and Mines has not proven to be effective enough in establishing realistic priorities and programs for the industry's expansion.

9. The overseas marketing of mineral production has been recently centralized through a state enterprise, MINEROPERU COMERCIAL (MINPECO). The United States is still the principal market although sales to both Western and Eastern Europe have increased in recent years.

Sectoral Constraints and Investment Program

10. Labor unrest and difficulties in retaining qualified executive staff are important problems in the sector. Government policy has raised the wages of workers and miners, but has limited the salaries of executives. This has resulted in substantial increases in operating costs and has made it difficult to attract experienced senior executive staff, particularly expatriates. Despite the improvement in worker benefits, labor unrest has continued. Besides disputes over wages and working conditions, there continues to be controversy and uncertainty over the management participation of the mining communities, i.e. the associations representing the mine workers. In the private mining sector, this participation takes the form, as has been the case in the private industrial sector since 1970, of profit-sharing and a mechanism for increasing share ownership up to a maximum of 50 percent.^{1/}

11. The effects and future structure of this experiment in worker participation are still uncertain. In the case of CENTROMIN, the Government has resisted any influence over decision making by the mining community or other agencies. Although CENTROMIN is nominally a subsidiary of MINEROPERU, it is effectively controlled by the Ministry of Energy and Mines.

^{1/} The mechanics of worker participation is described in greater detail in the sector paper on industry. As in that case, miners associations in state-owned enterprises accumulate perpetual bonds rather than equity shares.

12. Underinvestment since 1960 is another important constraint on the mining sector. To remedy this situation, the Government has formulated an investment program aimed at substantially increasing the volume of Peru's mineral output and at raising the percentage of ore processed in Peru. At the same time the Government attributes high priority to improvements in the housing, health and educational facilities of Peru's mining community and to strict control of environmental standards. The major elements comprising the sector's investment program over the next 5 - 6 years are the expansion and modernization programs of three of the four large companies--MINEROPERU, CENTROMIN and SPCC. HIERROPERU will probably proceed with some further expansion, but on a smaller scale than the three other companies and details at this stage are uncertain.

13. Originally, the consolidated investment program of Peru's four large-scale mining companies called for investments in excess of \$3.5 billion during the 1975-80 period. The limited project preparation and executing experience of the companies, coupled with likely financial constraints, have caused the earlier, ambitious program to be scaled down. In its place, a more realistic program has been drawn up. It calls for \$2 billion in investment during 1976-80, 60 percent of which would be public. Even this, however, depends on the country's ability to raise the necessary financing. Given this investment rate, the value of Peru's mineral exports could reach some \$2.5 billion in current prices by 1980 or about 70 percent above the 1974 value, with about half of the increase resulting from increased production. The largest single project is SPCC's development of the Cuajone mine, which is scheduled for completion by the end of 1976. Cuajone will effectively double Peru's copper producing capacity. After 1980 sector growth is expected to be fueled primarily by investment in copper and to a lesser extent in zinc, phosphates, lead, and silver.

Bank Group Operations

14. In support of the Government's investment program in the mining sector, we are planning to recommend to the Executive Directors a \$40 million loan to CENTROMIN in late March or early April. This project, which will also receive a \$33.6 million loan from the IDB, aims at replacing obsolete facilities, expanding copper production and processing facilities, strengthening company management, and reducing environmental pollution. More specifically, it consists of:

- (i) expanding the output of copper concentrates from CENTROMIN's Cobriza Mine from 50,000 to 222,000 tons a year;
- (ii) replacing an existing copper cementation plant at Cerro de Pasco with a solvent-extraction/electro-winning and waste neutralization plant which would produce about 7,000 tons per year of refined copper by 1978. Its construction would virtually eliminate the severe pollution caused by the existing plant and produce refined rather than cement copper at a lower cost; and

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- (iii) hiring a number of senior staff experienced in the execution of mining projects to oversee CENTROMIN's expansion program and strengthen the existing management team.

15. Looking beyond FY76, the Bank's present plans call for continued financial support for the mining sector's development. A follow-up loan to CENTROMIN in FY78 is contemplated as are two loans for as yet unidentified projects--probably to be carried out by MINEROPERU--in FY80 and FY81. With regard to CENTROMIN, our aim is to strengthen an already going concern by providing funds for plant modernization and expansion and management improvement. In the case of MINEROPERU, on the other hand, institution building will be an important feature of our loans since the company is virtually starting from scratch. In each of the mining loans, the Bank plans to play a catalytic role in mobilizing funds from other sources for the sector.

THE INDUSTRIAL SECTOR

1. Value added in manufacturing, which currently accounts for more than 21% of the GDP, has been growing faster than 7% per year since 1960. This rapid rate of growth has been stimulated by highly protective import barriers, powerful direct incentives to investment, and generally expansive demand management and income redistributive policies. Manufacturing employment, on the other hand, has been growing about 4% per year, and the sector occupies only slightly more than 5% of the labor force. Some 72 percent of value added and 75 percent of employment in manufacturing are concentrated in the Lima-Callao metropolitan area. Growth in the manufacturing sector slowed markedly in 1974 and 1975 as firms were increasingly hampered by shortages of foreign exchange and tight domestic credit.

The Drive for Economic Independence

2. As part of its program to reduce Peru's foreign dependence, the present Government has divided the manufacturing sector into four priority categories. These categories, or levels of priority, determine the degrees of preference or subsidy to which a given activity is entitled via income tax exemptions on reinvestments, reduced tariffs on imported inputs, credit subsidies, etc. First priority is given to some 151 industries, 38 of which --grouped under the headings iron and steel products, non-ferrous metal products, basic chemicals, fertilizers, cement, and pulp and paper-- are defined as "basic industries" and reserved for state ownership or joint ventures. In 1972, "basic industries" accounted for about 20-25% of value added in manufacturing. As present investment plans are realized, both the share of basic industries in the economy and the heretofore small share of government in manufacturing investment are expected to rise sharply. Some \$3 billion of public sector investments in industry are planned to be carried out over the next five years.

3. The second priority category is broken down into two groups defined as "essential" consumer goods (e.g. selected food, clothing, transport) and "sectoral industries" producing intermediate goods such as animal feed, synthetic fibers, and glass. Third priority is given to industries which are in broad terms similar to second priority items --e.g. some food, textiles, etc.-- but are deemed to be nonessential or complementary. Finally, the fourth, or no priority category consists of industries, such as candy, alcohol, perfume, furs, etc. considered to be luxuries. Additional preference, independent of industry category, is given to investments outside the Lima-Callao metropolitan area and to firms organized as "social property enterprises" (see below).

4. Incentives in the form of transferable tax credits and special credit facilities are offered also to stimulate nontraditional exports; but these are offset to some degree by an overvalued exchange rate, the poor quality of domestically produced (and protected) components, and the

more attractive incentives granted to import substitution activities. Nevertheless, nontraditional exports rose more than five times to \$157 million between 1970 and 1974.


5. The elaborate and generous incentives offered to investors have undoubtedly generated a higher level of investment than otherwise would have been sustained in the general atmosphere of private sector uncertainty created by the Government's rhetoric and social reforms. ^{1/} The program, however, is subject to several criticisms:

(i) The priorities established bear no relation to Peru's real cost advantages in international trade and may be worsening rather than helping to alleviate the increasingly serious foreign exchange constraint on the nation's growth.

(ii) By the same token, while inefficient industries are being encouraged, some investments that need no subsidization are being subsidized at considerable cost to the Treasury. To some extent, the subsidies merely offset the disadvantage created by the overvalued exchange rate.

(iii) While Peru gives rhetorical support to the integration of the Andean market and could benefit from the economies of scale that market would open up, its growing vested interest in highly protected, inefficient industry has made it increasingly resistant to the intrazonal liberalization of trade.

(iv) Finally, the incentives offered are attached largely to the use of scarce capital and thus bias product and process selection against the absorption of labor. The need to provide productive employment to Peru's rapidly growing labor force may also be in conflict with existing worker protection and job security legislation which raises the relative cost of hiring labor.

6. Many Peruvian officials privately acknowledge the apparent internal contradictions in the Government's current policies. Serious consideration is being given to the rationalization of industrial policies taking into account some of the above factors, but the strong political-ideological commitment to economic independence may constrain important changes. Outside criticism on industrial policies usually brings quick and bitter reaction, although we have during the last year had some success in opening up discussions. 

Worker Participation

7. The growing participation of workers in the ownership and management of enterprises is being accomplished through two devices: the Industrial Community and the Social Property Enterprise.

^{1/} Investments in the "basic industries" depend directly on the Government and are therefore not affected by the various incentive schemes.

8. Each industrial enterprise ^{2/} is required to form an Industrial Community (IC), an organization to represent the firm's employees. In addition to the 10% of profits which by law must be distributed in cash each year to the employees, 15% of profits are paid to the IC for the purpose of buying equity shares in the enterprise. ^{3/} Once an IC has accumulated 50 percent of a company's shares, distribution is to be made to the individual workers in proportion to length of service. The IC will continue to receive 15 percent of the profits, the funds being used to buy back shares from departing employees, to maintain the IC's equity position as the firm's overall capital is increased, and to make other investments outside the firm. The average participation of IC's in their firms' equity now exceeds 10%, and the Government expects the 50% target to be reached in 20 years on the average.

9. Not only has the Industrial Community itself become an important source of investment funds, but reportedly it is also acting as a stimulus to capital expansion on the part of the original owners of the firms as they seek to dilute the IC share. On the other hand, the Government's objective of eliminating the labor-management conflict inherent in capitalist enterprise is still far from realization. Given their still small equity share and the slowness with which traditional attitudes are changed, workers continue to look to wage increases rather than profits as their source of income gains.

10. In contrast to the Industrial Community, the Social Property Enterprise (EPS) entails full worker ownership and management. An EPS may be formed from scratch or, under certain specified conditions and procedures, an existing enterprise may be converted into an EPS. The EPS form of organization may operate in any sector not reserved to the state.

11. The initial capital for an EPS is provided as a loan from COFIDE or from the National Social Property Fund to be repaid out of future profits. COFIDE loans are generally in foreign currencies which COFIDE borrows abroad. The Fund is initially financed by the Government but is to be funded in the future through mandatory contributions from the profits of existing EPSs. Social property enterprises are given first priority treatment in the various investment incentive schemes and, for a period of five years, preferential access to government contracts if their bids are competitive.

12. All management positions within an EPS are filled by worker ballot. A National Commission (CONAPS), with an advisory board consisting of four cabinet ministers, is responsible for overseeing the development of the

^{2/} Firms with fewer than six employees are excluded.

^{3/} In the case of basic industries, the 15% is invested in perpetual bonds.

sector and reports directly to the Office of the President. Investment proposals are reviewed at several levels, the major responsibility for technical-financial inputs belonging to COFIDE, the state development bank. In its first year of implementation, there has been a predictable friction between CONAPS and COFIDE, the former interested in getting the sector into operation, visible and credible, and the latter approaching proposals from a more rigorous and cautious banker's point of view.

13. The first EPS was formally constituted in April 1975. By the end of the year, only two social property enterprises had been formally constituted, and 19 others were functioning on a provisional basis while final feasibility studies are completed, workers recruited and trained, and a constitution drafted and adopted. Total employment in these 21 enterprises was about 2,000. A major problem impeding the growth of existing EPSs, as well as the formation of new ones, is the shortage of technical and managerial skills both at the firm level and in the government agencies charged with assisting them. Although a primary objective of the concept of participatory enterprise is to open the system to the heretofore suppressed entrepreneurship, ideas, and innovative potential of the Peruvian masses, these people so far lack the skills necessary to translate their ideas into sellable project proposals. Several of the EPSs currently operating were transformed from pre-existing firms in financial difficulty. Despite the prescription in the regulating legislation that only financially sound firms be approved for transformation, the government is put in a difficult political situation when the alternative to transformation is liquidation of the firm and disemployment of its labor force.

14. Despite the sector's difficulties and the essentially cautious and measured implementation of the industrial reform, social property is the keystone of Peruvian socialism and will continue to receive preferential treatment so long as the present Government is in power. Policy intentions regarding the remaining private sector are less certain. The Government has repeatedly stated its intention of maintaining a pluralistic industrial sector, but its preferential treatment of the EPS, the state's own increasing direct role, and the often scathingly anti-private enterprise tone of its rhetoric continues to create uncertainty.

15. In summary, despite the healthy growth rates of the past two decades, Peru's industrial sector may not, in the context of current policies, be able to play the dynamic role it must play in Peru's medium-term development. Current policies aimed at economic autarky are not consistent with the efficient use of scarce capital, the employment of a rapidly growing labor force, and the solution of the balance of payments constraint. Crucial technical and managerial skills are to some degree demobilized in the traditional private sector, while development in the public sector industries and social property enterprises is constrained by the shortage of those very skills. It is not clear how these problems

can be resolved quickly. The long-term growth and diversification of the Peruvian economy will depend very heavily on industry. Given Peru's size and resource base, however, industrial development is not consistent with the autarkic model now being applied. Contrary to its intended economic independence, unless the political and ideological inhibitions to changing its present policies can be overcome, Peru's growth will continue to be tied to the vagaries of the world market for its basic minerals. Furthermore, for industry to grow even within the constraints of a closed economy, the Government's vision for the future structure of ownership in industry must be clearly delineated and consistently communicated. If it is serious about retaining a significant private sector, steps must be taken to satisfy mutual uncertainties and to define the rules of the game.

Bank Involvement in the Sector

16. The Bank's first operation in the manufacturing sector will be a \$30 million loan to COFIDE (Corporacion Financiera de Desarrollo). Its main objective is to improve the balance of payments situation by supporting projects which either contribute to exports or to efficient import substitutes. The loan will also be available to finance tourism projects. Its impact will be felt beyond those projects directly benefitting from it to the extent that it succeeds in spreading the use of economic efficiency tests within COFIDE and possibly to other entities concerned with investment decisions. Training of project analysts in the use of economic evaluation techniques therefore is a crucial aspect of the project. Up to forty percent of the loan will be available to finance worker-managed projects in the social property sector.

17. In connection with the appraisal of the project, Bank staff have had discussions with Peruvian authorities on the revision of industrial policies. A particular concern of these discussions has been the cost and effectiveness of current incentive policies. This dialogue will be pursued further in the hope of inducing a revision of incentives which would complement the loan's emphasis on efficient use of the country's resources.

18. The project is expected to be repeated after the first loan has been committed in about 2 1/2 years.

Chimbote Steel Mill

19. SIDERPERU, the state steel company, is operating an integrated steel complex in Chimbote 400 km north of Lima. The plant will have a capacity of approximately 700,000 t of liquid steel, after a minor expansion program has been completed later this year. SIDERPERU is now

planning to double capacity by 1980 at a cost estimated to exceed US\$1 billion. The plant uses Peruvian iron ore and efforts are under way to eventually exploit domestic deposits of coking coal as well. Production would be for the Peruvian market.

20. SIDERPERU has approached the Bank informally in October 1975 about possibilities for obtaining a loan. We indicated our interest in receiving basic data concerning the project when they become available in early March. A decision whether to pursue SIDERPERU's request further will be made at that time.

The Bayovar Industrial Complex

21. The Government is now planning the development of a large mining and industrial complex at Bayovar, a stretch of desert in north-west Peru about 80 km. south of Piura. The Bayovar complex is an important element in the Government's strategy to create new growth poles that decentralize economic activity.^{1/} The complex consists of a large group of interrelated projects including: mining and processing of phosphates and brine; an oil refinery and a petrochemical complex; and copper and zinc refineries. The petroleum pipeline from the northern jungle (scheduled to be completed in late 1976 or early 1977) would terminate at Bayovar. A town for 120,000 people is planned, together with the infrastructure needed for the mining and industrial operations. Total investment requirements between 1976 and 1985 are roughly estimated at \$2.5 billion. A special government entity, CECOB (Executive Committee of the Bayovar Complex) has been charged with planning and coordinating the development of the complex.

22. Besides the port facilities for the oil pipeline, the only project now in execution is the first stage of a rock phosphate mine. This first stage aims at producing 865,000 tons per year of phosphates (30.5% P₂O₅) by the end of 1977. Subsequent stages will triple production to 2.5 million tons per year. Total cost is estimated at around \$65 million. A loan for \$17.4 million from the Andean Development Corporation has already been secured and IDB financing for the rest is now at an advanced stage of negotiation. The other projects in the complex are still at a preliminary stage of preparation.

23. The Bank has not been approached for financing of projects in the Bayovar complex. However, given the large magnitude of the complex, the Government may request in the future assistance from the Bank and IDB for co-financing of specific projects. We are following developments closely and, if requested, would be interested in exploring this possibility once projects in the complex are at a more advanced stage of preparation.

^{1/} Former President Velasco referred to the Bayovar complex as "the most important industrial development in Peru's history".

1. The cold waters of the Humboldt Current supply the Peruvian coast with an abundance of fish food that make it one of the world's most productive fishing grounds. From modest beginnings during World War II, the fishing industry expanded so rapidly that by 1963 Peru was the world's largest fishing nation in terms of tonnage of catch, and the foremost producer and exporter of fishmeal. Although more than 50 species of fish are caught commercially, the sector's rapid growth, as well as its recent difficulties, has been linked to the anchovy which is processed into fishmeal. By 1970, fishmeal was Peru's major export, contributing one-third of foreign exchange earnings.

2. Anchovy meal is the highest protein feed available for livestock and poultry, and, consequently, world demand has grown rapidly. Moreover, the fish is relatively inexpensive to process. However, the industry suffers from the periodic incursion of warm water currents off the Peruvian coast which dramatically reduce the supply of fish. After peak years in 1970 and 1971, in which the anchovy catch reached 12.3 and 10.3 million metric tons, respectively, the warm waters invaded and the catch fell drastically to 4.4 million tons in 1972 and only 1.8 million tons in 1973. Recovery began in 1974 with the catch rising to 3.5 million tons, but fishing once more had to be suspended in May 1975 as water temperatures again rose and the available fish were unusually small. ^{1/}

3. The anchovy crisis accentuated the problems which had plagued the fishmeal and fishoil industry: excess capacity in both the fishing fleet and the processing facilities and high indebtedness. Under these conditions the Government decided early in 1973 to nationalize the fishing sector. Through PESCAPERU, a new State-owned enterprise, it is implementing a fundamental structural reform to consolidate and rationalize the operations of the sector. Since nationalization, the fishing fleet has been cut in half, and further reductions are planned. At the same time, the number of processing plants has been reduced from 104 to 56, and it is expected to be cut to 40 by the end of 1976. With the elimination of high-cost plants and the consolidation of others, processing yields have been increased.

4. Peru's potential for the harvesting of fish for direct human consumption has thus far been underexploited. These resources represent an important source of animal protein in a country for which meat is scarce. The catch of such fish as tuna and bonito reached 315,000 metric tons in 1973 but has diminished since then. In addition to ecological

^{1/} The authorities are now extremely cautious concerning the level of catch that may be allowed and rigorous in enforcing the strict regulations governing the actual operations of the fishing fleet. The highly competent "Instituto del Mar" continues the periodic study of oceanographic conditions to ensure that the level of catch does not endanger the rebuilding of the stock, and the Government is strictly adhering to the recommendations of the "Instituto". Current indications are that it will take several years before the pre-1972 level of catch is again reached.

problems, present Peruvian consumption habits tend to favor species in relatively short supply, rather than others such as hake, striped tunny, and jurel which are abundant. A further obstacle has been the inadequacy of fishing terminals, cold storage houses, and processing plants which, along with the lack of proper freezing equipment on all but a few modern trawlers, raise substantially the costs of landing and marketing the catch. Finally, the fishing fleet is prevented from operating at full capacity by the underfinancing of the state marketing organization and of the fishermen's cooperatives, as well as by chronic shortages of spare parts and other inputs.

5. Recent and planned investments in the fishing sector reflect the importance the Government attaches to stimulating the catch, processing, and marketing of fish for direct human consumption. The Government's investment program includes the construction of five large fishing complexes for canning, freezing, and smoking fish; the expansion of regional distribution facilities; and the modernization of the fishing fleet. In addition, an intensive consumer education effort is being made to foster demand for nontraditional species in the coastal cities, and fish are being introduced into the Andean markets where the protein deficiency is particularly severe.

1. Surface deposits of tar and asphalt have been exploited in Peru since pre-Inca days. The first major oil discovery occurred in 1869, and Peru was a net exporter of petroleum during most of the period prior to the mid 1960s. During the past decade, however, the growth of demand has out-paced domestic production, and by 1973 imports supplied one-third of Peru's oil consumption and had become a major item in the balance of payments. Currently, although most electricity is generated hydroelectrically, Peru's industrial and transport sectors are heavily dependent on oil, and consumption has been growing around 7 percent per year.
2. The traditional production area is found along the northwest coast and offshore. These fields have produced at a rate of around 70,000 barrels per day in recent years, and are expected to sustain or improve slightly on that level through 1985 with new drilling and the application of secondary recovery techniques. By 1975, however, consumption exceeded 125,000 b/d.
3. In 1971, oil was found in the northern jungle region, and the very high success rate of the initial drillings brought exuberant expectations that Peru within a short time would again be a major exporter of petroleum. In addition to its own direct exploration activities, PETROPERU, the very capable state oil monopoly, has entered into 18 exploration contracts with foreign private companies, covering in total more than 23 million hectares of Peru's Amazon Basin. ^{1/} Dry holes and changing U.S. tax legislation, however, have apparently caused many of these companies to suspend their operations in Peru, and expectations regarding future production are now considerably more conservative.
4. Successful drilling, principally by PETROPERU and Occidental Petroleum, had proven reserves by the end of 1975, of some 516 million barrels of oil with an additional 200 million barrels considered probable. From these wells, approximately 10,000 b/d are being exported to Brazil by way of the Amazon River. Major exploitation, however, must await completion of the 900 km Transandean Pipeline currently under construction from PETROPERU's jungle site at Saramuro to the port city of Bayovar, and the connecting branch with Occidental's field.
5. The Transandean Pipeline was begun in August 1974, and completion is now expected by the end of 1976. The last published cost estimate is \$634 million, \$330 million of which was financed by Japan in exchange for a long-term oil supply agreement. The pipeline will have an initial carrying

^{1/} The contracts with foreign companies, which have come to be known as the Peruvian Model, specify that the Government retains full ownership of the land and its resources. The company is granted exploration and drilling rights for a specified period of time, usually four years. If oil is discovered, the company receives a share of the output (contract terms have varied from 44 to 50 percent), the rest belonging to the state. If no oil is found, the concession expires and the company absorbs the full loss.

capacity of 200,000 barrels per day with capability of expansion to 500,000 b/d with the introduction of additional pumping stations. PETROPERU hopes to be moving 100,000 b/d through the pipeline by the end of 1977. For the pipeline to pay for itself at today's prices, at least 80,000 barrels per day will have to flow. It is not yet certain the required production level can be reached and sustained.

6. For political reasons, the price of petroleum products in Peru has until recently been held at a fraction of the world market price and below PETROPERU's cost of production. The low price has contributed to the growth of demand, and the company has been operated at a loss. Consequently, its very substantial investments in exploration, the pipeline, refining, and the petrochemical industry have been financed principally through foreign borrowing. Recent price increases ^{1/} may permit PETROPERU to cover its operating costs in the coming year, but, unless further increases are accorded, its sizeable investment program will continue to depend on the increasingly doubtful availability of external loans.

7. In summary, the quintupling of world oil prices and the heavy dependence of Peru on petroleum as its primary energy source have made the slowing of consumption and the resurgence of domestic production crucial to its development plans. Although oil discoveries in the Amazon basin may not provide the major new source of export revenues originally hoped for, the savings even if Peru only reestablishes self-sufficiency will be substantial. Two conclusions are clear, however. First, Peru cannot go on mortgaging future oil earnings with foreign debt; a substantial proportion of the sector's future investment must be domestically financed, preferably through higher domestic prices for petroleum products. Secondly, inasmuch as Peru apparently cannot finance its autarkic growth strategy out of expanding oil revenues, the need to rethink that strategy and to seek vigorously to promote industrial and other exports including tourism, is becoming increasingly imperative.

^{1/} Between June 1975 and January 1976, the price of regular gasoline rose 156 percent and the price of premium rose 180 percent. Nevertheless in dollar terms the present price of premium is still only 93¢ per gallon and that of regular 51¢ per gallon.

POOR URBAN SETTLEMENTS AND THE MINISTRY
OF HOUSING AND CONSTRUCTION

Ministry of Housing and Construction

1. The Ministry of Housing and Construction is responsible for housing, urban development and construction policies and programs. Three semi-autonomous agencies are under the supervision of the Ministry: two water and sewerage authorities, ESAL in Lima and ESAR in Arequipa; and a real estate agency which is responsible for all public housing and industrial sites in Peru, EMADI.

2. The Ministry administers a two-year housing program (S/. 3,000 million in 1975-76) which includes sites and services, core housing, semi-complete housing and apartment building projects. The Ministry is also responsible for urban renewal projects and has worked with the UN on experimental housing. The lowest cost of housing provided through the Ministry is about US\$6,200 per unit. Through EMADI the Ministry also extends supervised credits to families with monthly incomes between US\$138 and 230 for improvement of housing. Starting in 1975, the Ministry through the housing bank of Peru (Banco de la Vivienda del Peru) is also assisting the construction industry.

Views of the Problem of the Minister of Housing and Construction

3. One of the main objectives of the present Minister of Housing and Construction, Rear Adm. Isaias Paredes Arana, is to provide economically feasible housing solutions to the urban poor. He thinks that housing has to be considered together with other requirements that also affect the welfare of the urban poor, such as health and education. He has also emphasized the need for integrating the development of housing plans with other aspects such as: location of peripheral settlements; establishment of public services and communities facilities; land use patterns; leasehold and tributary regulations, and incentives to the construction industry. Because of the size of the problem, the Minister considers it necessary to provide an opportunity for all forms of enterprise to participate in this effort--cooperatives, social property and private firms. Another aspect of major concern to the Minister is the increasing concentration of the population in a few urban centers, particularly in Lima.

The Pueblos Jovenes 1/

4. In 1970, approximately 1.5 million inhabitants (or 10% of Peru's population) lived in pueblos jovenes, of which around 55% were concentrated in Metropolitan Lima and 7% in Arequipa, Peru's second largest city. The remainder of the population of pueblos jovenes was divided among some twenty smaller cities. By 1974, the population of Lima's pueblos jovenes had increased to 1.2 million or about 35% of the city's total population.

5. The formation of pueblos jovenes is closely related to in-migration patterns and the shifting of migrants' priorities from obtaining shelter towards acquiring a piece of land on which to build a house--a first step toward attaining a middle class status. In general, prior to land invasion, a group of squatters form an association (called "Organización Vecinal" or neighborhood organization) for the purpose of organizing the settlement, plan the land use, and allot to each family a plot of land. The association represents its members before government agencies for the legalization of the settlement and for the installation of urban services and community facilities. In some recent cases, the migrant population is moving directly into the pueblos jovenes on the city's periphery. Meanwhile the inner city slums continue to provide permanent, although deteriorating, residence for part of the low income population. In other cases, the industrial development of a city has produced a disproportionate growth of the pueblos jovenes to the point where their inhabitants far outnumber the central city population.

1/ The Pueblos Jovenes (literally, young settlements), which originated in "barriadas", are officially recognized, have a legal status and, usually, a degree of development which permits them to become integrated to cities to which they belong. Barriada is defined as: a social conglomerate constituted by a group of families that invade unoccupied state, municipal or private lands, found on the periphery of the city. Pueblo Joven is defined as: urban settlements originated by migrations (from within or without of the city) and/or the inorganic growth of the cities that have a population of more than 10,000 inhabitants. They are characterized by being located in or near the cities on private or public land and by the lack of all or part of public utilities and community facilities. They are also characterized by the lack of stable employment which in turn generates low-income levels. These settlements are in the process of being integrated to the cities in which they are located and with which they are dynamically interdependent, and have public and private support in their efforts to transform their environment.

Source: Oficina Nacional de Pueblos Jovenes, Censo de Población y Vivienda de Pueblos Jovenes, 1970.

The People in the Pueblos Jovenes

6. Although there are specific differences between pueblos jovenes in different cities, they all share basic characteristics in their relationship to the city; the socioeconomic composition and poverty level of their population. Poverty in the pueblos jovenes can be understood in terms of: (a) the level of real income of the population, depending on the combination of benefits received from shelter, utilities, employment, schools, clinics, and markets that permits the creation of assets over time; and (b) the disadvantages that the residents of pueblos jovenes have in relation to the rest of the low-income urban groups (i.e. demographic, educational, health and nutritional, and political).

7. The low median age of the population is the main demographic disadvantage of pueblos jovenes. In 1970, 45% of the population of pueblos jovenes were children under 15, as compared to the national urban average of 38% (in the 1961 census). Thus the percentage of the population in pueblos jovenes that is economically active (around 25%) is lower than the national average (30%). Around 80% of the work force in pueblos jovenes are males, since the large size of families constrains women to seek outside employment. Half of the male work force are blue collar workers, one-fourth are self-employed in the informal sector and the rest operate small stores or are employed in clerical jobs. Of the women that work, one-third are self-employed (working as washwomen, streetvendors, etc.), one-fourth are household servants, one-fifth are blue collar workers and the rest have clerical jobs.

8. Lack of adequate, inexpensive transport is a major problem in many pueblos jovenes. Located far from major areas of employment in the city, residents must spend a lot of time which might otherwise be productive simply traveling to perform work or look for it. This is particularly true in the region of Lima. Furthermore, because virtually everything needed by a pueblo joven has to be brought in from the outside, costs are high and opportunity for productive activity within the community is severely curtailed.

9. Prices of food, building materials and other goods are usually considerably higher in pueblos jovenes than in the city. Basic utilities such as water, for example, cost more than they do in the upper income residential neighborhoods of the city. The lack of an adequate water systems requires the distribution of water by trucks, which is more expensive than that provided by the Water Company. Credit has traditionally not been accessible to the low-income population, and even when available, monthly interest rates between 12% and 17%. In some instances branches of savings and loans associations have been installed in the pueblos jovenes, the net effect has been that the settlers through their savings subsidized loans to higher income groups since they themselves could not afford the terms for credit.

10. Health is another serious problem facing the pueblos juvenes. The greater availability of health facilities in the cities than in the countryside does not mean that the city facilities are suited to the needs of large numbers of urban poor. In fact the reverse is usually true. If the incidence of untreated diseases is greater in the rural areas, the density of the cities produces new health threats. Although the quality of medical care within reach of the migrant to the city is higher than any he has experienced before, the accessibility to such services continues to be a major problem and a source of frustration.

11. The inhabitants of Peru's pueblos juvenes are better educated than other residents in low-income settlements in the rest of Latin America. In fact in 1970 the level of education of pueblos juvenes was on the average, higher than that of Peru's central cities. For the age group 5-14 years old, in 1970 the percentage of children of pueblos juvenes enrolled in school was 78%, as compared to 72% for the overall urban sector and 37% for the rural sector.

12. In general, education is apparently among the least critical ← of the problems facing the pueblos juvenes in Peru. However, it should be pointed out that there is a certain educational disadvantage as far as the type and quality of the education is concerned. The quality is likely to be inferior to that of comparable schools in the city, due to, among other reasons, the inadequate facilities, travel time for teachers not leaving in the area, lack of school supplies, etc. More serious, however, is that the type of education is not necessarily job oriented.

13. The greatest resource of the pueblos juvenes is undoubtedly their degree of community organization which gives them a distinct political advantage over the tugurios of inner city slums and differentiates them from similar settlements in other developing countries of the continent. All the progress that has been achieved in the settlements can be attributed largely to the political pressure that the organizations have been able to apply to government agencies. This pressure is effectively exercised by the "organizaciones vecinales" or neighborhood organizations. The organizacion vecinal was born out of the association required to carry out and sustain the illegal invasion of public and in some cases private land. In some pueblos juvenes today, the community organization has evolved into a sophisticated, highly democratic form of self-government that has health, transportation, education, production and planning committees among others. This type of organization offers a tremendous potential for self-help and mutual aid that can be effectively employed for improving the situation of the pueblos juvenes.

Pueblos Jovenes in Metropolitan Lima

14. In 1974, there were 647 pueblos jovenes in the country, of which 320 were located in the Lima metropolitan area. About 1.2 million people --35% of the city's population--live in the pueblos jovenes of Lima and even conservative estimates indicate that 45% to 50% of the future growth of the city will be concentrated in this type of settlement. There are about 200,000 dwelling units in these settlements; this represents 40% of the units in the Metropolitan Lima. The quality of the housing stock in the pueblos jovenes is uneven but is considered adequate due to the mild dry climate of Lima. Although one of the major problems faced by the settlers has been the lack of land titles due to the slow process of legalization, the tolerant attitude of the government towards the pueblos jovenes has provided reasonably secure rights, allowing the residents to make substantial investments in the improvement of their dwellings. This is generally done as rapidly as the family's savings permits it and largely by self-help, usually over a period of 10-20 years. By 1970, it was estimated that 30% of the housing units had piped-in water, but that 44% had no water service. Only a small number of public stand-pipes are used in the pueblos jovenes and usually these function more as a backup system. For those without access to metered water supply, water is largely provided by vendors. The cost of water from vendors' trucks is extremely high and sometimes ranges up to 25 times the rate charged by the water company (ESAL). The average monthly costs to a family for water from trucks has been estimated at over US\$4.

15. The level of service for electricity is much higher than that for water supply and sewerage. In 1970, 42% of individual dwellings in pueblos jovenes around Lima had electrical service, as compared to 85% for the city as a whole. The number of housing units with electrical service in pueblos jovenes in 1972 was estimated to be about 50%. The average cost of installing electricity in these settlements in 1972, was estimated by the electrical company (E.E.E.E.A.A.) at around S/.5,000 (US\$115) per lot, with a typical pay-back period of five years at an interest rate of 10%. The monthly electrical bill for households in pueblos jovenes, which use electricity only for lighting purposes, is about S/.20 (.50 cents). The charge is 0.67 soles per kwh (1.5 cents) for the first 30 kwh consumed per month and 0.90 soles per kwh for the next 100 kwh consumed per month.

The Case of Villa El Salvador

16. Villa El Salvador which now has a population of about 120,000 persons, was established in April 1971 by organized squatter invasion by 9,000 families of about 3,000 hectares of public lands located about 30 Km South of Lima. The existence of a plan for the expansion of the southern zone of Metropolitan Lima permitted the official land subdivision to be carried out rapidly. By the end of 1971, another 7,000 families were allocated to Villa El Salvador by the Ministry of Housing.

17. Occupation of the new site was directed by experienced community leaders and the basic tasks for creating the urban infrastructure were initiated immediately. These consisted of clearing the streets, opening trenches for the water system and the construction of the first schools and public facilities. The tasks were all organized, carried out and, when necessary, financed by the settlers. The process of a formal community organization was initiated with the support of government agencies. It was based on territorial hierarchies established in the urban project: block, residential group, sector and the whole community.

18. The urbanized settlement has a capacity for up to 150,000 inhabitants and includes two basic components: a residential area and an industrial area. The industrial area (420 hectares) had already been set aside by the Development Plan for Metropolitan Lima as a future development pole, and the residential area was simply laid out along it. The residential area includes single and multi-family lots as well as lots for shop/dwellings. Twenty-four 140 m² lots form a block and 16 blocks constitute a residential group. There are 23 or 25 residential groups to a sector and a total of 67 residential groups in the whole settlement. One error in the layout of Villa El Salvador is that it was designed as an automobile oriented city when in fact the population is almost totally pedestrian. However, some of the 60 m wide streets have been improved by the appearance of long makeshift markets along the middle lane with more reasonable 20 m roads on either side. There have been other divergences from the original plan: 10% of the lots intended for dwellings are being used as shop/dwellings and the gradual settlement of population has not conformed with the projected roads and community facility sites; secondary roads are being used as main streets, and the commercial areas have developed spontaneously to serve the present distribution of population. The architects are now redesigning and adjusting their project to reality.

19. The community organization structure of Villa El Salvador has evolved from its original form as an association for invasion of land to a sophisticated self-managed urban community which has become a model for Pueblos Jovenes in Lima and throughout Peru. This process can be observed through four phases of development:

- (a) Spontaneous Organization (April to December 1972). An association started by 350 families primarily motivated by the need to obtain a piece of land and secure their subsistence, multiplied to 9,000 families and proceeded to invade the large area of private and public, rural and urban land. Later, they are relocated and supported by two public agencies: Urban Communal Promotion of the Ministry of Housing and the ONDEPJOV;

- (b) Neighborhood Organization (January '72 to May '73). The "Organización Vecinal", or Neighborhood Organization, was formally created by ONDEPJOV which was incorporated to SINAMOS. SINAMOS helped set up cooperatives that included transportation, construction, sewing, carpentry and markets. Several private, mostly religious, institutions participated by offering organizational, educational and health aid. Private banking activities were not welcomed by the community leadership, which requested the participation of a state bank instead;
- (c) Cooperative Socioeconomic Organization (May to November 1973) The desintegration of the initial cooperative movement lead to a model for an "enterprise city" by the establishment of a Self-Managed Integral Communal Cooperative. During this period, industrial development was given priority over housing by the community. The first self-census was carried out in the settlement and the population was estimated to be 20,000 families. The distribution of lots was transferred to the community by SINAMOS;
- (d) Communal Socioeconomic Organization (November 1973). The previous cooperative organization was transformed into the "Comunidad Urbana Autogestionaria Villa El Salvador", also known as CUAVES. This organizational model establishes the integral self-management of social, economic and administrative aspects of the community on a territorial basis. The CUAVES or self-Managed Urban Community is seen as a socioeconomic model of popular participation which offers land and labor resources for the establishment of socially-owned industrial enterprises, and serves as a testing ground for local self-government systems.

20. The political structure of the community follows its territorial hierarchy: 24 families in the block form a committee which elects a delegate who, together with 15 others, similarly elected forms the residential group committee. The executive council is constituted by a representative from each of the 67 residential group committees. The executive council also heads the Economic and Services Organization which includes advising agencies (planning and multi-sector committees), supporting agencies (communal savings and general administration), and five executive agencies (production, services, marketing, education, and health and social promotion).

21. Recently INCOSUR (Industries of the South Cone) was created to promote and plan the development of the industrial zone. The management committee of INCOSUR is made up of two representatives of CUAVES, one of CONAPS ^{1/} and one of COFIDE. Through the management committee which has a fully legal status, Villa El Salvador can enter into financial or technical aid agreements on its own. how

22. By 1974, 23,800 lots had been occupied, representing about 80% of the settlement's planned capacity. Fourteen percent of all dwellings were completed with permanent materials although most of them lacked sanitary facilities. Fifty-five percent of the dwellings units were of two or less rooms and 5% had more than five rooms. Most dwellings are user-built but several units have been built through public institutions. In general, the degree of consolidation of Villa El Salvador is comparable to that of settlements that are 10 or 15 years old. It is not surprising that the community has a greater priority for employment than for housing.

23. Based on the plan for the settlement, there is still a large deficiency in community facilities, including schools, markets, health centers, public buildings and parks. However, the Government has built elementary schools largely with counterpart funds and labor provided by the residential groups themselves. According to the community, the most serious deficit of facilities is in the area of health services.

24. In spite of the efforts both of the public and private sectors to alleviate the situation, health remains one of the major community problems. The Ministry of Health has provided one health center and two sanitary posts; which in all take care of 530 out-patients a day. The Ministry also runs the small hospital. The JAN and IMPROMI ^{2/} provide gynecological and pediatrical care. The private sector provides dental care and food rations through religious organizations.

25. Only 43% of the dwellings units are served with piped-in water. Most households still rely on water vendors. There is a network of stand-pipes, but due to their insufficiency, they serve largely as a backup system to water distributed by trucks. how

^{1/} CONAPS is the National Commission for Social Property (a decentralized consulting agency) and COFIDE is the Corporation for Financing Development (a decentralized financing agency).

^{2/} JAN is National Assistance Board, a decentralized agency run by the President's wife and IMPROMI is a branch of the Ministry of Health concerned with child nutrition.

26. Due to the fact that some 18,000 to 20,000 people must travel out of the settlement daily, transportation continues to be a serious problem facing the community although the city government has recently introduced a modern trailer bus system that goes from near Villa El Salvador to downtown Lima. The problems lie in the insufficiency of this system, lack of buses, and general disrepair of the internal transportation street network, as well as with the conditions of the external road system.

27. Villa El Salvador is connected to the rest of the Cono Sur and to Lima by the new Pachacutec Highway. Internally over 17 kms of roads were graded and compacted by the community. Although the layout of the system is adequate, the roads are in very bad shape due to intensive use and the poor quality of the sandy soil. This situation inhibits the development of an adequate transportation system and causes an increase in travel time for users.

28. Employment. The economically active population in Villa El Salvador was estimated in 1975 at about 20% of its 120,000 inhabitants. Less than 1% of the labor force has received any technical training; 42% have gone through primary school and 16% have completed high school. Thirty-seven percent of the labor force are occupied in largely artisan type industries, 33% in commerce, 20% in construction, 7% in services and 3% in agriculture or mining.

29. Underemployment in Villa El Salvador is estimated at 26%. Of those employed, 47% are self-employed, 32% are blue collar workers, 11% are clerks or attendants, 5% work at home and 1% are professionals. Of the 47% self-employed and 32% workers mentioned above, 33% are merchants, 10% are mechanics, 10% are construction workers, 9% are bus and truck drivers, 6% are carpenters, and 5% are tailors. A full 80% of the labor force commutes to Lima or nearby areas daily.

30. According to three different surveys carried out between 1972 and 1974, the average monthly income per family varies from S/. 3,244 to S/. 4,252. The corresponding monthly income per capita ranges from S/. 648 to S/. 850. Another survey determined that 30% of families in Villa have a potential savings margin of 80 soles per month.

31. Priorities. The Pueblos Jovenes residents rank their priorities as follows:

- (a) Employment and legal land titles. Whereas the concern for the legalization of land tenure is one that is widespread in Pueblos Jovenes throughout Metropolitan Lima, the need for employment is possibly felt more acutely in the fast growing newer settlements of Southern Metropolitan Lima;

- (b) Access to adequate health facilities is a generally felt need. This is understood to be one of the original motivations to migrate to the city;
- (c) Water and sewerage, for reasons mentioned above, rank relatively high in the list of priorities; and
- (d) Roads and electricity, due to the fact that the coastal plains around the city are mostly sand, the compacted roads within the settlements deteriorate easily and cause serious problems to internal transportation and circulation. Electricity and street lighting is a reasonably affordable service that promotes the development of the community and opens up a number of income-earning opportunities.

Bank Lending Program

32. The proposed operation described above is the first Peruvian urban project for which Bank financing is being sought. The project cost is estimated at about \$43 million of which the foreign exchange cost is about 35%. Bank financing of the equivalent of about \$20 million has been recommended. The loan should be ready for consideration by the Executive Directors in the last quarter of FY76. Implementation, which could start by late 1976; is expected to take three years.

33. The project would benefit pueblos juvenes in Lima and Arequipa, Peru's second largest city, and would include the provision of basic infrastructure for water, electricity, access roads, health, and sewerage; development of two industrial sites (one in Villa el Salvador); provision of housing and commercial sites and services and credit; and technical assistance for project management, monitoring and preparation of follow-up projects.

34. The major portion of works to be undertaken in the project would directly benefit residents in pueblos juvenes. Villa el Salvador, for instance, would experience improvement in its water, sewerage, electricity, health and road systems. Financing for an industrial site of about 50 ha would also be provided where worker-owned factories would be established. Technical assistance, both for the operation of training programs in the field of health and nutrition, as well as industrial park management would productively assist residents of the pueblos juvenes. The rate of return for this project is 30% based only on quantifiable elements of the project. Non-quantifiable benefits are just as large.

35. Looking beyond FY76, we expect to have repeater loans for sites and services projects in FY78 and FY80. In these latter operations, however, we will focus primarily on Peru's rapidly growing provincial cities, 22 of which now have over 100,000 inhabitants.

THE TOURISM SECTOR

1. Peru's archeological treasures, cultural heritage and scenic riches have long attracted tourists from around the world. Although the resulting demand has been accommodated and Peru has increased its share of foreign visitors in the last decade, it has not taken full advantage of the boom in international leisure travel. Fuller exploitation of its tourist attractions could importantly contribute to the balance of payments, as well as to the decentralization of economic activity. Such development will require considerable investment, improved organization, and better coordination within the Andean Group of promotional and complementary tourism supply activities.

2. Economic Impact. Tourism accounts for between 4 and 5 percent of exports, and approximately 0.7% of GNP, a ratio below the average for most South American countries. However, the percentage of net foreign exchange earnings to total revenues in the sector is higher in Peru than in the popular island countries because of the relatively low import content of Peru's tourist services. Approximately 45,000 jobs currently derive directly or indirectly from the tourist sector.

3. Tourism Demand. Foreign tourist arrivals to Peru increased steadily at an annual rate of almost 13% between 1963 and 1968, fell in 1969 in the aftermath of the 1968 revolution, but expanded again rapidly during 1969-74 at a rate 50% faster than the growth in worldwide tourism. About one-third of the 260,400 tourists arriving in 1974 were South American, with about one-quarter each coming from the U.S. and Europe. Promotion of tourism has been weak in the past, largely because of limited facilities. There are strong indications, however, that with expanded accommodations Peru could attract greatly increased tourist flows from the affluent markets of Europe and the U.S.

4. Tourism Accommodation. In January 1975, there were 859 registered hotel-type establishments in Peru, with a guest capacity of 34,000. Of this total, the Lima-Callao area accounts for 20% of the establishments and over 30% of capacity. The Government, which provides fiscal incentives for private hotel investment, has approved projects that would increase capacity by 12,000 over the next few years in hotels of tourist quality. Many of these projects are not currently being developed for lack of credit or complementary tourism infrastructure. On the other hand, if all projects thus far approved were developed by 1979, tourist arrivals would have to continue increasing by about 20% annually for them to be profitable.

5. Tourism Organization and Policy. Official tourism policy is set by the Ministry of Industry and Tourism. The administrative arm of the Government is ENTURPERU, which owns and manages a nationwide hotel chain. The private sector is given an important role in tourism, and the Government encourages investment in approved hotel projects and

provides limited financing through state agencies. Current policy emphasizes tourism development as a means of earning foreign exchange, a tool of regional development, and a recreational outlet for Peruvians. The priority area with the most promise is Cuzco. Here the Government is now implementing an ambitious regional development program based on tourism, the Plan COPESCO.^{1/} Peru also hopes to develop internal tourism circuits (including Lima, Cuzco, Iquitos in the Amazon Jungle, and Tumbes on the equatorial coast) that can accommodate charter and low-cost group travel. This step is necessary if Peru is to overcome the competitive disadvantage of distance from markets and to exploit the uniqueness and diversity of its resources. Thus far, these plans are having little success because of the limited funds being made available to the sector and the lack of a strong national institutional framework.

6. International Agencies in Peruvian Tourism. The first active institutions were UNDP and UNESCO in the Cuzco region, followed by a \$29 million loan from the IDB in 1975. The OAS has provided technical assistance, especially for tourism marketing. The Bank Group has had only limited involvement in the sector, having supported a UNDP mission in 1968 and negotiated that same year an IFC investment for a Lima hotel project. The latter was never developed, however. Future lending possibilities include: (1) project loans through COFIDE, (2) infrastructure support, for new integrated regional tourism development programs as well as general transport and power needs, (3) the second stage of the development program for Cuzco, and (4) IFC involvement in private sector hotel projects.

^{1/} Attached are more details on the Plan COPESCO and on general tourism developments in the Cuzco region.

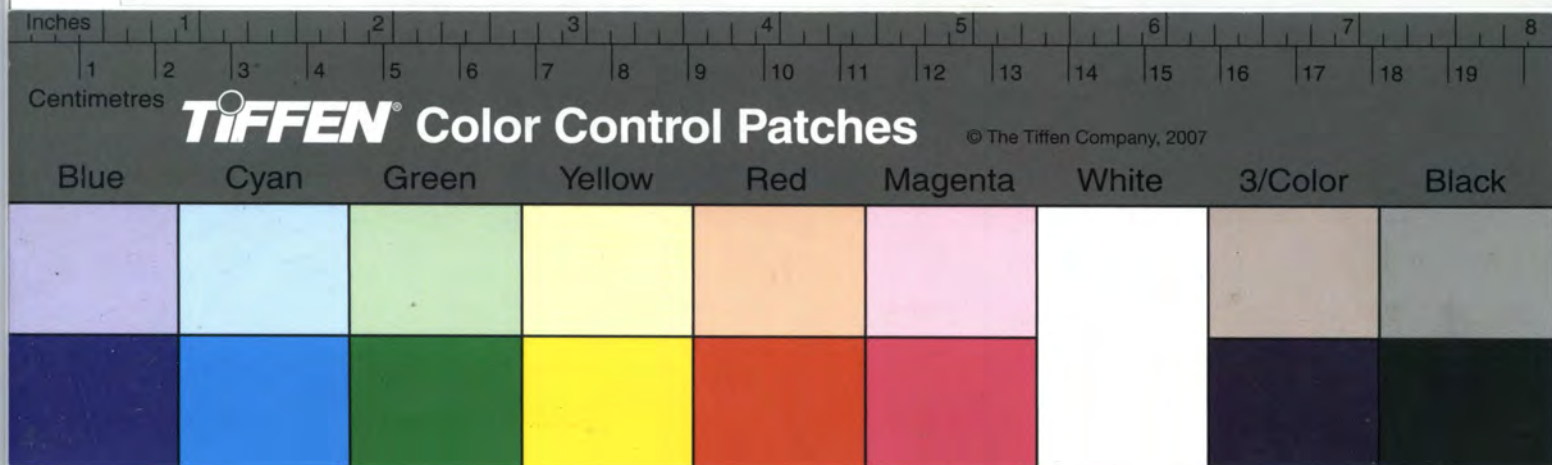
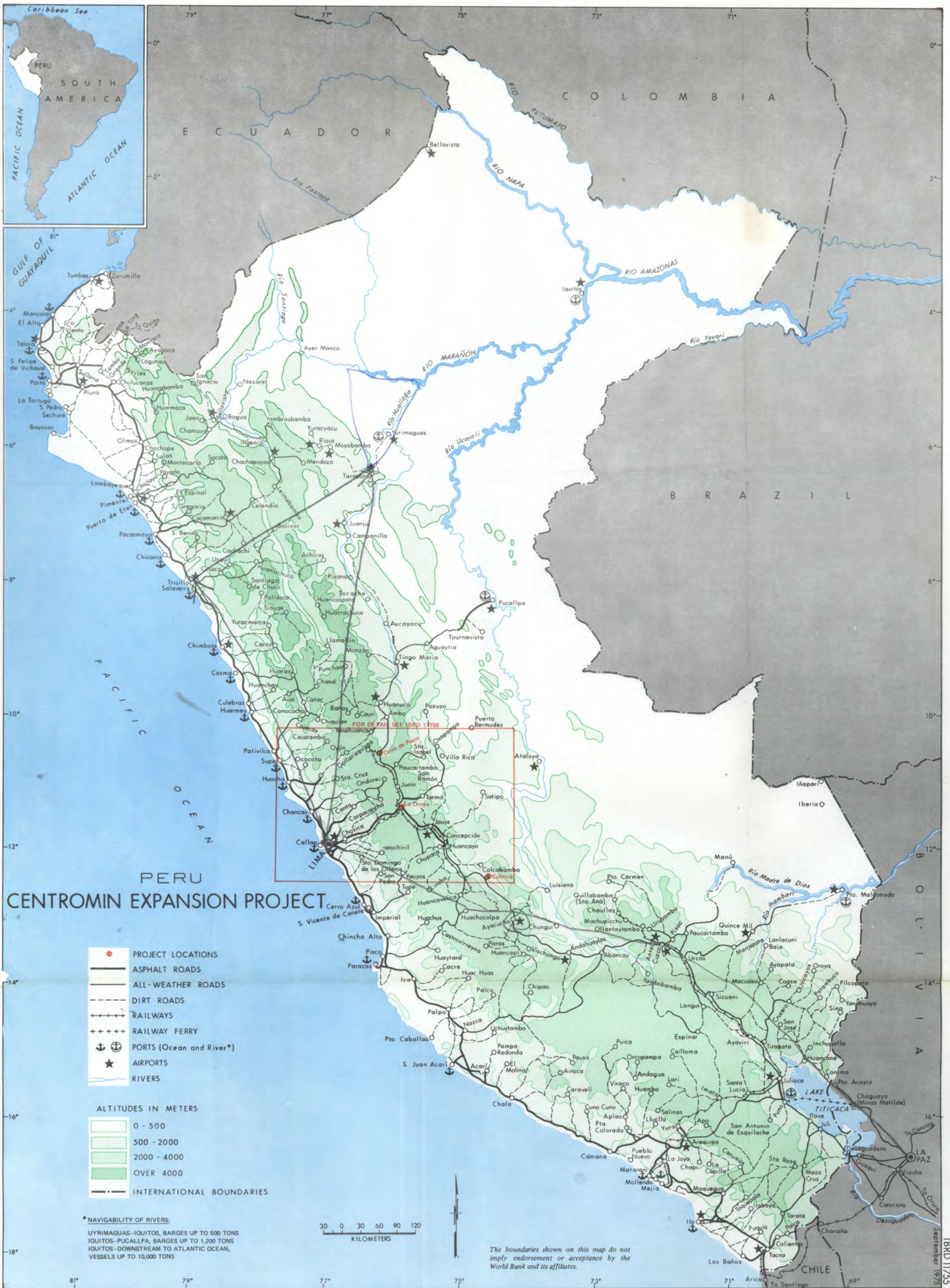
ANNEX: THE CUZCO AREA AND THE PLAN COPESCO

1. Tourism and Regional Development. Cuzco, located in one of the country's poorest regions, attracts more tourists than any other Peruvian city except for Lima. The Government has therefore designated tourism as the "growth pole" of an ambitious attempt at integrated development in the mountainous Cuzco-Puno region. The COPESCO Plan began as a joint Peruvian-UNESCO effort to restore the valuable Inca ruins of the region, but was later expanded to guide all development activities in the region.
2. Current Tourism Activity. In 1973, Cuzco received around one fifth of the foreign tourists arrivals and \$3.5 million in tourism expenditures. Some 54,000 foreign and 56,000 Peruvian visitors went to Machu Picchu, the famous "Lost City of the Incas" which can only be reached by train from Cuzco. The Department of Cuzco had 59 registered hotel establishments in 1974 which could accommodate 2,664 guests, and many more small guest-houses and family-run hotels which cater to seasonal traffic. Almost all travelers come by way of Lima's international airport, and technical studies are being made to determine whether Cuzco's airport facilities could be upgraded to accept large planes (it can now take only B-727s) or to extend its hours of operation (limited by mountain winds to 5:00 AM - 1:00 PM). International flights are not now permitted to land in Cuzco, although many feel this policy discourages would-be tourists from stopping in Peru.
3. The COPESCO Plan. The Plan attempts to increase tourism activity to provide employment opportunities and earnings in the tourism sector and, indirectly, to regional artisans, construction teams, suppliers of food and transport, etc. It will also provide direct benefits to the poor, largely rural population, in the form of improved water systems, expanded access to electrical energy and long-needed roads, all designed to improve the standard of living in the region. Public works and technical assistance are to be administered by a number of ministries and specialized institutions, who enter into agreements with the COPESCO directorate in Cuzco. This decentralization of authority to Cuzco is a widely-heralded experiment, but officials there indicate that, until sectoral and financial agencies also decentralize their operations, COPESCO's ability to coordinate public activities outside of Lima is greatly hindered.
4. Plans call for raising hotel guest capacity to over 6,000 in Cuzco by 1980. Some hotels will be built by COPESCO and run by ENTURPERU, the publicly-owned hotel chain, while others are to be developed privately with Government approval and fiscal incentives. Promotional activities (including package tours) are being designed to attract a larger number of tourists to the area.
5. The COPESCO Plan is to be realized in two stages. The first-of the Plan to be executed between 1975 and 1978 is budgeted to cost \$73 million, of which \$29 million is financed by the IDB. Total first-stage costs, by function, are:

	<u>S/. 000</u>	<u>US\$ 000</u>	<u>%</u>
a. Tourism Superstructure	831,315	21,481	29.5
b. Transport	1,449,431	37,453	51.4
c. Electrical Energy	49,110	1,269	1.7
d. Water Systems	16,408	424	0.6
e. Monument Restoration	211,999	5,478	7.5
f. Technical Assistance	30,418	786	1.1
g. Financial Costs	<u>229,607</u>	<u>5,933</u>	<u>8.2</u>
TOTAL	2,818,288	72,824	100.0

The second-stage of Plan COPESCO (1979-82) is to be prepared by early 1977 and may include projects designed to link the COPESCO tourist circuit with similar ones in Bolivia and Argentina, and to provide equipment and rehabilitation for the region's railroads. The second stage of the Plan will be presented to several international credit agencies, including the Bank Group, to solicit their financial support.

C



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			APPROVAL DATE	AGREEMENT DATE	CANCELLATIONS	DISBURSED	EXCHANGE ADJUSTMENT	REPAID 3RD PARTY	IBRD COMMITMENT		
			EFFECTIVE DATE	CLOSING DATE	CURRENT PRINCIPAL	PRINCIPAL REPAID	BORROWER'S OBLIGATION	DUE 3RD PARTY	EFFECTIVE LOANS HELD		
REPUBLIC OF PERU PORT OF CALLAO		57-0	4 1/2%	J/J-01	54-67	2.5	.0	.0	1.1	.0	57-0
			08 JAN 52	23 JAN 52	.1	2.4	.0	1.1	.0		
			04 JUN 52	31 DEC 56	2.4	2.4	.0	.0	.0		
REPUBLIC OF PERU AGRICULTURAL MACHINERY		67-0	4 1/8%	J/J-15	54-59	1.3	.0	.0	.4	.0	67-0
			08 JUL 52	09 JUL 52	.0	1.3	.0	.4	.0		
			31 JUL 52	01 JUL 54	1.3	1.3	.0	.0	.0		
REPUBLIC OF PERU SECOND AGRICULTURAL MACHINERY		98-0	4 1/4%	J/J-15	56-61	1.7	.0	.0	.4	.0	98-0
			08 APR 54	12 APR 54	.0	1.7	.0	.4	.0		
			04 MAY 54	31 DEC 56	1.7	1.7	.0	.0	.0		
BANCO DE FOMENTO AGROPECUARIO DEL PERU AGRICULTURAL CREDIT GUARANTOR - PERU		105-0	4 1/4%	F/A-01	57-63	5.0	.0	.0	.7	.0	105-0
			12 NOV 54	12 NOV 54	.0	5.0	.0	.7	.0		
			10 FEB 55	30 JUN 57	5.0	5.0	.0	.0	.0		
REPUBLIC OF PERU QUITOZ-PIURGA IRRIGATION		114-0	4 3/4%	M/S-15	59-60	18.0	.0	5.9	.5	5.9	114-0
			05 APR 55	05 APR 55	.0	18.0	.0	.5	5.9		
			23 MAY 55	30 SEP 60	18.0	12.1	5.9	.0	5.9		
CIA DE CEMENTO PACASHAYO S. A. PACASHAYO CEMENT GUARANTOR - PERU		116-0	4 5/8%	H/N-01	58-70	2.5	.0	.0	.3	.0	116-0
			18 APR 55	19 APR 55	.0	2.5	.0	.3	.0		
			05 OCT 55	31 JAN 58	2.5	2.5	.0	.0	.0		
REPUBLIC OF PERU HIGHWAY MAINTENANCE		127-0	4 1/4%	F/A-15	58-64	5.0	.0	.0	1.0	.0	127-0
			04 AUG 55	05 AUG 55	.0	5.0	.0	1.0	.0		
			08 SEP 55	31 DEC 59	5.0	5.0	.0	.0	.0		
BANCO DE FOMENTO AGROPECUARIO DEL PERU SECOND AGRICULTURAL CREDIT GUARANTOR - PERU		162-0	5 1/2%	F/A-01	59-65	5.0	.0	.0	1.5	.0	162-0
			12 MAR 57	13 MAR 57	.0	5.0	.0	1.5	.0		
			18 JUN 57	31 DEC 59	5.0	5.0	.0	.0	.0		
PERUVIAN CORPORATION LTD. RAILWAYS GUARANTOR - PERU		190-0	5 1/2%	F/A-15	**--**	15.0	.0	.0	.0	.0	190-0
			01 APR 58	03 APR 58	15.0	.0	.0	.0	.0		
			02 JUL 58	31 DEC 61	.0	.0	.0	.0	.0		
AUTORIDAD PORTUARIA DEL CALLAO PORT EXPANSION GUARANTOR - PERU		208-0	5 3/4%	M/S-01	63-78	6.6	.0	1.7	1.5	1.7	208-0
			16 SEP 58	17 SEP 58	.0	6.6	.3	1.5	1.7		
			25 NOV 58	01 JUL 63	6.6	4.9	2.0	.0	1.7		

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			APPROVAL DATE	AGREEMENT DATE	CANCELLATIONS	DISBURSED	EXCHANGE ⁵ ADJUSTMENT	REPAID 3RD PARTY	IBRD COMMITMENT		
			EFFECTIVE DATE	CLOSING DATE	CURRENT PRINCIPAL	PRINCIPAL REPAID	BORROWER'S OBLIGATION	DUE 3RD PARTY	EFFECTIVE LOANS HELD		
BANCO DE FOMENTO AGROPECUARIO DEL PERU THIRD AGRICULTURAL CREDIT GUARANTOR - PERU		257-0	6% F/A-01 63-68			5.0	.0	.0	1.2	.0	257-0
			31 MAY 60 01 JUN 60			.0	5.0	.0	1.2	.0	
			10 SEP 60 30 SEP 63			5.0	5.0	.0	.0	.0	
EMPRESAS ELECTRICAS ASOCIADAS HUINCO GUARANTOR - PERU		260-0	6% M/S-15 65-85			24.0	.0	15.3	.7	15.3	260-0
			28 JUN 60 29 JUN 60			.0	24.0	2.7	.7	15.3	
			07 APR 61 30 JUN 65			24.0	8.7	18.0	.0	15.3	
REPUBLIC OF PERU AGUAYTIA-PUCALLPA ROAD		271-0	5 3/4% J/J-01 65-75			5.5	.0	.1	1.0	.1	271-0
			16 DEC 60 19 DEC 60			.0	5.5	.0	1.0	.1	
			03 APR 61 31 DEC 67			5.5	5.4	.1	.0	.1	
REPUBLIC OF PERU HIGHWAY MAINTENANCE & IMPROV.		300-0	5 3/4% F/A-15 65-71			10.0	.0	.0	3.1	.0	300-0
			02 NOV 61 03 NOV 61			.0	10.0	.0	3.1	.0	
			16 MAY 62 31 JUL 65			10.0	10.0	.0	.0	.0	
THE PERUVIAN CORPORATION LTD. RAILWAY REHABILITATION GUARANTOR - PERU		334-0	5 1/2% J/D-01 67-79			13.3	.0	4.8	.5	4.8	334-0
			12 MAR 63 13 MAR 63			.2	13.0	.4	.5	4.8	
			26 AUG 63 31 DEC 67			13.0	8.3	5.2	.0	4.8	
EMPRESAS ELECTRICAS ASOCIADAS HUINCO II GUARANTOR - PERU		365-0	5 1/2% F/A-15 67-88			15.0	.0	10.9	.6	10.9	365-0
			21 NOV 63 22 NOV 63			.0	15.0	1.9	.6	10.9	
			20 DEC 63 31 JAN 67			15.0	4.1	12.6	.0	10.9	
REPUBLIC OF PERU PAITA PORT		373-0	5 1/2% M/S-15 68-89			3.1	.0	2.2	.2	2.2	373-0
			21 APR 64 22 APR 64			.1	3.0	-.2	.2	2.2	
			28 JUL 64 30 JUN 68			3.0	.7	2.1	.0	2.2	
BANCO DE FOMENTO AGROPECUARIO DEL PERU FOURTH AGRICULTURAL CREDIT GUARANTOR - PERU		415-0	5 1/2% A/O-01 69-80			15.0	.0	7.2	.8	7.2	415-0
			18 MAY 65 03 JUN 65			.0	15.0	.0	.8	7.2	
			22 JUL 65 31 DEC 67			15.0	7.8	7.2	.0	7.2	
REPUBLIC OF PERU LA OROYA AGUAYTIA ROAD		425-0	5 1/2% F/A-15 71-90			33.0	.0	28.1	1.0	28.1	425-0
			31 AUG 65 17 SEP 65			.0	33.0	4.2	1.0	28.1	
			30 NOV 65 31 DEC 73			33.0	4.9	32.3	.0	28.1	
REPUBLIC OF PERU PISCO PORT		446-0	6% M/N-15 71-91			8.1	.0	7.0	.3	7.0	446-0
			20 APR 66 13 MAY 66			.9	8.2	1.7	.3	7.0	
			15 JUL 66 30 MAR 73			8.2	1.3	8.7	.0	7.0	

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			APPROVAL DATE	AGREEMENT DATE	CANCELLA- TIONS	DISBURSED	EXCHANGE ADJUSTMENT	REPAID 3RD PARTY	100% COMMITMENT		
			EFFECTIVE DATE	CLOSING DATE	CURRENT PRINCIPAL	PRINCIPAL REPAID	BORROWER'S OBLIGATION	DUE 3RD PARTY	EFFECTIVE LOANS HELD		
IMPRESAS ELECTRICAS ASOCIADAS POWER DISTRIBUTION GUARANTOR - PERU		464-0	6%	J/O-01	69-85	10.0	.0	7.4	.5	7.4	464-0
			11 AUG 66	07 SEP 66	.0	10.0	1.9	.5	7.4		
			22 SEP 66	31 DEC 69	10.0	2.6	9.3	.0	7.4		
EMPRESAS ELECTRICAS ASOCIADAS MATUCANA POWER GUARANTOR - PERU		511-0	6%	M/N-15	72-92	17.5	.0	15.8	.5	15.8	511-0
			07 SEP 67	11 SEP 67	.0	17.5	3.5	.5	15.8		
			28 DEC 67	01 NOV 73	17.5	1.7	19.3	.0	15.8		
		*				223.0	.0	106.5	17.8	106.5	*
		*				16.3	206.7	16.4	17.8	106.5	*
		*				206.7	100.3	122.9	.0	106.5	*
REPUBLIC OF PERU SAN LORENZO IRRIGATION		418-0	5 1/2%	A/O-15	69-85	11.0	.1	4.2	.5	4.3	418-0
			20 APR 65	18 JUN 65	4.5	6.4	1.0	.5	4.3		
			24 NOV 65	30 JUN 76	6.5	2.2	5.2	.0	4.3		
REPUBLIC OF PERU ROAD RECONSTRUCTION		706-0	7 1/4%	J/O-15	80-88	30.0	9.4	20.6	.0	30.0	706-0
			08 SEP 70	14 SEP 70	.0	20.6	.0	.0	30.0		
			26 OCT 70	31 MAR 77	30.0	.0	20.5	.0	30.0		
BANCO AGRARIO DEL PERU AGRICULTURAL CREDIT 1973 GUARANTOR - PERU		933-0	7 1/4%	F/A-01	78-91	25.0	19.2	5.8	.0	25.0	933-0
			14 AUG 73	12 SEP 73	.0	5.8	.0	.0	25.0		
			12 DEC 73	31 DEC 77	25.0	.0	5.8	.0	25.0		
REPUBLIC OF PERU EDUCATION		949-0	7 1/4%	F/A-15	84-96	24.0	23.9	.1	.0	24.0	949-0
			13 NOV 73	05 DEC 73	.0	.1	.0	.0	24.0		
			05 MAR 74	30 JUN 79	24.0	.0	.1	.0	24.0		
REPUBLIC OF PERU SIXTH ROAD		1025-0	7 1/4%	F/A-01	80-99	26.0	25.6	.4	.0	26.0	1025-0
			23 APR 74	01 JUL 74	.0	.4	.0	.0	26.0		
			21 AUG 74	30 JUN 78	26.0	.0	.4	.0	26.0		
		**				339.0	78.2	137.6	18.3	215.8	**
		**				20.8	240.0	17.3	18.3	215.8	**
		**				318.2	102.4	154.9	.0	215.8	**
TOTAL FOR PERU											

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THE STATUS OF BANK GROUP OPERATIONS IN PERU

A. STATEMENT OF BANK LOANS (as at December 31, 1975)

Loan or Credit Number	Year	Borrower	Purpose	US\$ million	
				Amount Bank	(less cancellations) Undisbursed
		22 loans fully disbursed		206.7	
418	1965	Republic of Peru	Irrigation	6.5	0.1
706	1970	Republic of Peru	Roads	30.0	9.4
933	1973	Banco de Fomento Agropecuario	Agriculture	25.0	19.2
949	1973	Republic of Peru	Education	24.0	23.9
1025	1974	Republic of Peru	Roads	26.0	25.6
		Total		318.2	
		of which has been repaid		102.2	
		Total now outstanding		216.0	
		Amount sold	18.3		
		of which has been repaid	18.1	0.2	
		Total now held by Bank ^{1/}		215.8	
		Total undisbursed			78.2

Note: No IDA credits have been made to Peru

^{1/} Prior to exchange adjustments. A \$76.5 million loan for a Transport Corridor project was approved by the Executive Directors on December 30, 1975, and it is to be signed shortly.

B. STATEMENT OF IFC INVESTMENTS (as at December 31, 1975)

Year	Obligor	Type of Business	Amount in US\$ million		
			Loan	Equity	Total
1960*	Industrias Reunidas, S. A.	Home Appliances	0.3		0.3
1960	Luren S. A. and Ladrillos Calcareaos, S. A.	Bricks	0.3		0.3
1960	Durisol del Peru, S. A.	Building materials	0.3		0.3
1960; 1962	Fertilizantes Sinteticos, S.A.	Fertilizers	4.1		4.1
1962; 1968	Cemento Andino, S. A.	Cement	2.2	0.2	2.4
1964; 1967	Cia. de Cemento Pacasmayo	Cement	1.1	0.5	1.6
1975	Southern Peru Copper Corp.	Mining	<u>15.0</u>	—	<u>15.0</u>
	Total gross commitments less cancellations, terminations, repayments and sales		23.3	0.7	24.0
			<u>8.3</u>	<u>0.4</u>	<u>8.7</u>
	Total commitments now held by IFC		<u>15.0</u>	<u>0.3</u>	<u>15.3</u>
	Total Undisbursed		<u>5.0</u>	<u>-</u>	<u>5.0</u>

C. PROJECTS IN EXECUTION 1/

Loan No. 418-PE: San Lorenzo Irrigation Project; US\$11 million Loan of June 18, 1965; Effective Date: November 24, 1965; Closing Date: June 30, 1976

Because of inadequacy of water supply, the Bank agreed to reduce the project area; consequently, the project was redefined and the original loan amount of US\$11.0 million was reduced to US\$6.5 million. (See Memorandum to the Executive Directors "Peru; Proposed Change in Loan 418-PE", February 28, 1968-33). The Closing Date, originally June 20, 1967, was postponed four times, first to June 30, 1969, then to December 31, 1973, then to December 31, 1974, and then to June 30, 1976. The last postponement of the Closing Date was granted to allow the Borrower to use the undisbursed amount of the loan (US\$350,000) for the replacement of a valve at the San Lorenzo reservoir, which is important for the overall operation

1/ These notes are designed to inform the Executive Directors regarding the progress of projects in execution, and in particular to report any problems which are being encountered, and the action being taken to remedy them. They should be read in this sense, and with the understanding that they do not purport to present a balanced evaluation of strengths and weaknesses in project execution.

of the system. The project has encountered a number of difficulties, both administrative and technical but these problems are being overcome. Project management has been strengthened and the last part of the project related to the drainage scheme is progressing satisfactorily. The Loan is expected to be fully disbursed by the revised Closing Date.

Loan 706-PE: Road Reconstruction Project; US\$30 million Loan of September 14, 1970; Effective Date: October 26, 1970; Closing Date: March 31, 1977

This Loan was signed only three and a half months after the earthquake in the Callejon de Huaylas. However, the identification, feasibility study and final engineering of the roads to be improved have taken much longer than expected because of a too optimistic assessment at the time of appraisal, because of administrative and coordination difficulties in connection with the on-going decentralization of the Central Government, and because of problems with the consultants engaged to study and supervise the project. Construction of a short section of road near Huaraz, the capital of the region, is near completion. Work is well advanced on the two remaining sections along the Callejon; bidding for the access road has now taken place and construction of this last section has also started. The road reconstruction element of the project is expected to be completed by the end of 1976, 15 months later than the original Closing Date of the Loan, which has been extended accordingly.

Loan 933-PE: Agricultural Credit Project; US\$25.0 million Loan of September 12, 1973; Effective Date: December 12, 1973; Closing Date: December 31, 1977

The Loan was signed in September 1973 and became effective on December 12, 1973. Although the project had a slow start, progress is now satisfactory. Disbursements are slightly behind schedule.

Loan 949-PE: Education Project; US\$24.0 million Loan of December 5, 1973; Effective Date: March 5, 1974; Closing Date: June 30, 1979

This Loan became effective on March 5, 1974. Serious initial delays were caused by administrative difficulties with the Project Unit and late appointment of counterpart staff to the consultants who were to define curricula for the ESEPs (Escuelas Superiores de Enseñanza Profesional). The recent change of status of the Project Unit which has been upgraded to the rank of Directorate General and the strengthened management of the project have markedly improved the prospects for efficient implementation of the project.

Loan 1025-PE: Sixth Highway Project; US\$26 million Loan of July 1, 1974; Effective Date: August 21, 1974; Closing Date: June 30, 1978

Bids for construction works were invited in October 1974, on the basis of the official cost estimates, but contractors failed to respond. After an upward revision of the cost estimates new invitations to bid were issued in March 1975. Contractors response this time has been positive and bids for all sections have been submitted and contracts were awarded in August 1975. Project implementation is eight months behind schedule.

PROSPECTIVE OPERATIONS

1. Bank lending to Peru has varied widely from year to year and completely stopped from September 1967 to the summer of 1973 except for a road rehabilitation loan in September 1970 following a major earthquake. This stoppage of normal lending was initially due to lack of creditworthiness and then because of the issue of compensation arose following the nationalization of the International Petroleum Company in late 1968. The compensation problem subsequently became aggravated with the nationalization of properties of several other U.S. companies. Normal Bank lending was resumed with progress in the settlement of these investment disputes and loans totalling \$75 million were made in FY74.

2. The Bank then made no loans in FY75 because of problems which developed regarding projects during their appraisal. These projects which were finally ready for Bank approval in early FY76 had to be delayed because the issue of compensation again arose following the nationalization of the Marcona Corporation in July 1975. After several months of unsuccessful negotiations between the Government of Peru and the U.S. parent company regarding compensation, an interim agreement was reached in December between the Governments of Peru and the U.S. This provided that ore shipments would be resumed for a year, with shipping to be supplied by the company. The agreement also expressed the mutual intention of the two governments to reach a permanent settlement of the compensation issue within 90 days, i.e. by March 11, 1976, with the situation to be re-evaluated if this did not occur. Following this agreement the Bank proceeded with Board presentation of the \$76.5 million loan for the Lima-Amazon Transandean Corridor project, which was approved on December 30, 1975, and the \$36.0 million loan for the Fifth Power project to be considered by the Board on March 2, 1976. To date little further progress has been made toward a final settlement on the investment dispute. Current prospects are that the problem may be raised with Secretary Kissinger during his visit to Peru in the week of February 17 and intensive discussions at lower levels are likely to occur during the following week.

3. Table A below summarizes our FY76-77 lending program. Loans totalling \$172.5 million are now planned for the current fiscal year. This lending is on the basis that further progress will be made on the resolution of the Marcona compensation dispute. The FY76 total in part constitutes a "spill-over" of lending which had been programmed for FY75.

4. The proposed lending program for FY76-77 consists of:

a) 3 loans (34% of the total lending) for mining, industry, agriculture in order to help reduce the balance of payments constraint through export expansion and "efficient" import-substitution. Our lending plans in the three fields are summarized at the end of the sector summaries presented under Tabs F-5a, b and c.

b) 2 loans (17% of total lending) for sites and services and water supply projects to aid in overcoming urban problems, particularly in the Lima area. Our plans for these projects are summarized in the latter part of the urban sector summary under Tab F-5f.

c) 3 loans (49% of total lending) for transport and power to aid in economic expansion.

5. Our tentative lending program beyond FY77, which is presented in Attachment I, would continue the same general pattern as that for FY76-77. In real terms (1974 prices) our lending would average \$86.6 million during FY77-81 compared to \$72.6 annually as approved for FY76-80 in last years' CPP review, as shown in Attachment II. The increase would be mainly in FY80-81, with projected FY75-79 lending below that approved last year. The increase is justified by poorer petroleum prospects and the resulting need for larger amounts of external borrowing. Our share in total debt outstanding and in total disbursements would remain below 11-12 percent by 1980.

ATTACHMENT I

PERU: PROPOSED LENDING THROUGH FY81
(million dollars)

	Current FY76	Projected					Reserve Projects
		FY77	FY78	FY79	FY80	FY81	
Agricultural Credit VI			30.0*				
Agricultural Credit VII					35.0		
Irrigation Rehabilitation I		20.0					
Irrigation Rehabilitation II				30.0			
Irrigation Rehabilitation III						35.0	
Rural Development I			20.0				
Rural Development II					30.0		
Forestry and Forestry Industry I				30.0			
DFC I		30.0*					
DFC II				35.0			
Education II							35.0(79)
Education III						30.0	
Industry I (Steel Chimbote)				35.0			
Industry II (Unidentified)						35.0	
Tourism							25.0(80)
Mining I (Centromin I)	40.0						
Mining II (Centromin II)			50.0				
Mining III (Unidentified)					50.0		
Mining IV (Unidentified)						50.0	
Power V (Electrolima)	36.0						
Power VI (Electroperu-Generation)					35.0		
Water Supply (Mantaro)		25.0					
Transandean Corridor	76.5						
Airports			20.0				
Ocean Ports		15.0**					
Roads VIII					30.0		
Sites and Services I	20.0						
Sites and Services II				35.0			
Sites and Services III						40.0	
Lending Program	<u>172.5</u>	<u>90.0</u>	<u>120.0</u>	<u>165.0</u>	<u>180.0</u>	<u>190.0</u>	<u>60.0</u>
	4	4	4	5	5	5	2
Lending Program in constant FY74 \$	101.4	69.4	72.1	94.5	98.1	98.7	

* S projects

** Late information is that this loan may need to be deferred to FY79.

LC1DD

February 12, 1976

ATTACHMENT II

COMPARISON OF BANK LENDING PROGRAMS BETWEEN APPROVED

LAST YEAR AND PLANNED NOW, FY75-81

(In FY74 Millions of Dollars)

	1975	1976	1977	1978	1979	1980	1981	Annual Averages		
								75-79	76-80	77-81
Approved last year	59.9	79.8	78.9	78.1	80.1	46.3	n.a.	75.4	72.6	n.a.
Now planned	-	101.4	69.4	72.1	94.5	98.1	98.7	67.5	87.1	86.6