Statement by Yahya Alyahya  
Date of Meeting: December 7, 2004

**Peru: Country Assistance Strategy Progress Report And Second Programmatic Decentralization and Competitiveness Structural Adjustment Loan And Fourth Programmatic Social Reform Loan**

We can endorse the findings of the CAS Progress Report and support the two accompanying loans. In each case, we have some brief and selective comments.

**CAS Progress Report:**

We agree with the key statement in paragraph 52 that the Bank Group strategy laid out in the 2002 CAS remains “fully viable” and that implementation in support of the authorities’ objectives of improving competitiveness, increasing equity and access to services, and strengthening institutions and governance, has been “highly successful.” The efforts of the authorities in implementing their macroeconomic policies, resulting in solid economic growth of around four percent in the last three years, are to be commended, and stand out as an example of good practice in the region. We agree that the economic outlook remains positive, though there are downside risks both externally (exposure to terms of trade shocks) and internally (fiscal slippage, potential for lack of popular support, effects of impending elections). However, the CAS seems to have an appropriate focus on supporting consolidation of reforms during FY04-06, implying responsiveness to the Government’s request for additional emphasis on development policy loans, while being ready to use other innovative modalities such as an infrastructure guarantee facility.

We have just two comments, both related to the poverty situation. We found Annex D on poverty and macroeconomic developments very interesting, especially the finding that poverty is less responsive to economic growth (where as noted Peru has done quite well) than in other countries. This may be in part a temporary phenomenon, given the capital-intensive nature of mineral resource endowments, the employment-inelasticity of this type of growth, and the deflection of employment creation to the large informal sector. But it may also reflect longer-term rigidities. It is sobering to note that real GDP per capita is equal, in real terms, to that of 1970 despite growth episodes. These factors may impact the prospects going ahead of meeting the MDG poverty reduction goals set out in Table 2 on page 10, given that more than half the population is stuck below the poverty line and a fifth are trapped in extreme poverty. *Some staff additional comments on this structural challenge and how to meet it would be appreciated.*
The second point relates to targeting of Government programs to disadvantaged and at-risk groups, such as the indigenous and Afro-Peruvian communities, as mentioned in paragraph 22. However we noted from a reference source on the Bank’s own website for Peru that the Amerindian population accounts for 45 percent of the population, and the mestizo population for an additional 37 percent. Can staff comment further on the issue of mainstreaming assistance when indigenous groups are a plurality, rather than a small minority, of the population?

**Second Programmatic Decentralization and Competitiveness Structural adjustment Loan:**

This is an ambitious package, but the significant progress recorded under the predecessor loan offers grounds for optimism. The continued focus on protecting fiscal sustainability, subnational capacity building, and especially on improving the investment climate is an appropriate one. Of course, making local administration work remains a challenge, even allowing for the politically sensitive nature of the decentralization process.

We noted with interest that new export-oriented financial instruments are targeting small and medium-sized firms with export potential (para. 125) and the high level of informality in that sector. Indeed, according to para. 175, the informal sector accounts for 60 percent of GDP. It is to be hoped that a real breakthrough can be made to capture the potential of this sector. As far as export potential is concerned, receptivity on the part of potential trading partners in the industrial countries to the goods exported will as usual be critical.

**Fourth Programmatic Social Reform Loan:**

In the case of this loan there are three predecessors and a wealth of experience has accumulated over the last four years. The main lesson as we see it has been the positive experience in the social sectors within overall fiscal restraints. The record shows that the decision to expand the original PSRL operations to four was well-grounded. However, with this final loan the main risk, as the document itself recognizes, is that of ensuring sustainability of the process, especially given the complexities of decentralization. From the Bank side, it will be essential to keep up the multisectoral momentum through continued dialogue and more specific interventions.

In conclusion, we wish the Peruvian authorities well in tackling development challenges in the future, with the track record of the last few years providing comfort that the needed reform process will continue to advance.