Statement by Yoshio Okubo
Date of Meeting: December 7, 2004

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

We support the CAS Progress Report and the proposed two loans. We commend the authorities for steadily reducing fiscal deficits and pursuing sound monetary and exchange rate policies despite difficult political and social situations, and thus achieving steady growth since 2002. We encourage the authorities to continue sound macroeconomic policies and to pursue further economic reforms, even though political pressure for increased spending may become higher in the run-up to the 2006 elections. We also note that recent growth has not necessarily been translated into poverty reduction and employment creation, and encourage the authorities to redouble their efforts to make the growth pro-poor and to address income and social disparities.

We believe the CAS Progress Report proposes an appropriate strategy to help the authorities in such a direction. We also support the proposed two loans, which will contribute to Peru’s sustainable decentralization process, increased competitiveness and more effective social services. Having said that, we would like to make a couple of comments on the CAS Progress Report and ask one question on the Programmatic Decentralization and Competitiveness SAL (DECSAL).

1. Investment Lending and Adjustment Lending (Development Policy Lending)

First, we note with concern that the proportion of investment lending in recent years has not been as large as had been expected. While the 2002 CAS had planned a lending program with a little less than 50% of adjustment lending, the actual proportion of investment lending during FY02-04 was 35%. We remember that staff explained at the Board meeting for DECSAL I (December 2, 2003) that the Bank’s assistance would shift towards investment lending so that a 50-50 split between adjustment lending and investment lending would be maintained over the CAS period. However, the CAS Progress Report only proposes the ratio of 50% for investment lending during FY05-06; furthermore, since this ratio includes SWAp operations, only one-third of the lending envelope is for traditional investment operations.

We think the ratio of investment lending should not contract further; rather, we would like to see more investment operations in future to strike a better balance. Although we understand the constraints of expenditure ceilings for the government, public investment is still needed for future growth of the country. In this relation, we welcome the fact that the
Bank is working with IMF, IDB and the authorities to review the fiscal program to find extra space for investment. Through such exercise, we encourage the Bank to make utmost efforts to find a way forward to reconcile prudent fiscal policy and the need for public investment. Otherwise, there could be possibilities that government budgets may not be secured for ongoing and new Bank investment operations and, as a result, the country portfolio may experience further project delays and an even lower disbursement ratio. We also urge the authorities to continue improving its revenue collections and to secure domestic funding for necessary investments.

Furthermore, the high proportion of budget support makes the fiduciary aspects all the more important. We welcome the fact that public financial management reforms “continue to be in force and sustainable (para. 220 in Program Document for PSRL IV)” ; however, we note with concern that the CAS Progress Report points out that “implementation of [CPAR’s] action plan has been mixed (para. 82).” We also believe that further efforts are necessary to tackle corruption not only at the level of the central government but also at the levels of regions and municipalities. We urge the authorities to actively continue reforms on these fronts and the Bank to closely monitor the progress. Staff may also wish to update the Public Expenditure Review and the Country Financial Accountability Assessment at an appropriate juncture.

2. Use of Country Systems

Secondly, we note that the CAS Progress Report mentions that Peru is a “prime candidate” for the initiative of using country systems (para. 87). We would like to emphasize that what will be undertaken in Peru must follow the conclusions of future Board discussions on the use of country systems, and this should be made clear in the wording of the CAS Progress Report when it is disclosed.

3. DECSAL

Finally, we would like to ask one question about the DECSAL. We congratulate the authorities for making significant progress under DECSAL I. At the same time, we note that several triggers were not fully accomplished. For example, the tax reform package failed to eliminate sector exemptions; and the concession of two ports has been delayed. These elements do not seem to appear in the proposed triggers for DECSAL III. Also, the Accreditation Law does not specify the use of SIAF (Integrated Financial Administration System) for verification and does not require public disclosure of accreditation. Although the proposed triggers for DECSAL III include “considering” SIAF’s verification and the public disclosure, they seem to stop short of saying “introducing”. We would appreciate it if staff could elaborate on how the unmet triggers will be followed up in the current and future DECSAL operations.

With these comments and a question, we are happy to support the CAS Progress Report and the proposed loans. We wish staff and the authorities every success in implementation.