Statement by Matthias Meyer  
Date of Meeting: June 19, 2001

**Peru: Country Assistance Strategy Progress Report, Programmatic Social Reform Loan, and Second Rural Roads Project**

We welcome the discussion of this CAS Progress Report together with the proposed Programmatic Social Reform Loan and the Second Rural Roads Project. We thank staff for a very clear CAS progress report with a candid assessment of the recent developments in Peru. We congratulate the transition government for the various initiatives it has started in the right direction (stabilization of economy, structural reforms, fight against corruption, etc.).

Due to the transitional arrangements and the political insecurities, I agree with staff’s proposal for an interim CAS for the next 9 to 12 months, before a full CAS will be elaborated with a new government firmly in place. Considering that poverty is still widespread (about 50% of population are considered poor), I agree with the focus on poverty reduction of the proposed interim CAS. I also support the main directions as mentioned in para 27: stable political and economic transition to a new government; restoring of economic growth; reversing the recent deterioration in poverty indicators; and supporting institutional development through structural reforms and capacity building. In this context, I can also support the two proposed loans, i.e. the first Programmatic Social Reform Loan, and the Second Rural Roads Project.

This statement focuses mainly on the CAS Progress Report and provides a few observations on the Programmatic Social Reform Loan (PSRL) as well as on the Second Rural Roads Project (RRP).

**CAS Progress Report:**

On the background of important political transition to a democratic Government, a deteriorating economic context and a worsening poverty situation (mainly indigenous people), this progress report provides an accurate picture of recent developments in Peru and a candid assessments of the challenges ahead. In the poverty context, the issue of unemployment deserves special attention and we would like to hear from staff what specific strategies the Bank will use to address this issue. We also miss the mentioning of gender issues and how they are going to be addressed.
Realizing that Peru goes through a difficult economic situation, we welcome the Government's intention to protect social expenditures. The PSRL aims at assisting the Government in this endeavor and we urge the incoming Government to sustain public expenditures in social sectors. Considering the weak institutions, especially at local government level (municipalities), and combined with the fact that structural reforms were almost halted since 1997, it is important to regain momentum in the reform process and to specifically **improve public expenditure management**. To render it more transparent and accountable, a comprehensive PEM system should be introduced and based on medium term expenditure plans it should also comprise annual PERs. Taking into account the backlog in structural reforms and the institutional weaknesses, the projected increase in growth from 2.5% in 2001 to 5% in 2002 (Table 2 on page 8) seems to me over-ambitious, particularly during an year of political transition.

For the **sustainability** of social programs at the local level (service delivery in education, health, etc.), it is important to strengthen local government institutions. In this relationship, we urge the new government to initiate a **decentralization** program which would lead to devolution to municipalities. To successfully strengthen the local institutions and their capacities, a consistent decentralization to local governments would be a prerequisite. Only in this manner, could social services to the people and poor be improved and sustained. I welcome in this respect the PSRL and its intended support in this direction. In this connection, I would also like to see that PIUs (like the PCR in the rural roads program, see below) are no longer used by the Bank. As we long know, such PIUs are not sustainable and generally prevent the Bank’s operations from adequately strengthening local institutions.

We are encouraged by the joint work with WBI in the fight against corruption. We urge the incoming government to maintain the drive presently initiated in fighting corruption and to prepare a comprehensive strategy. In this respect, I assume that the fourth trigger on transparency for the low case scenario under the interim CAS (para 35 on page 14) includes the issue of corruption. Could staff clarify. We understand that in the present situation of political change and uncertainties reforms of the legal sector are not very opportune, but would like to see such reforms discussed as early as possible to strengthen and sustain the focus on improving governance in general.

In light of poverty reduction, I would like to see a **stronger focus on poverty also in IFC’s strategy**. I appreciate the intention to associate GEF funding with Bank lending in order to exploit synergies between development and environment and am looking forward to a deeper analyses of such opportunities in the context of a full CAS.

We congratulate Bank’s field staff for a well functioning coordination among the multilateral institutions, but wonder why nothing is mentioned in this report on a broader coordination among all donors, including bilaterals. The report correctly states that such coordination is important also to secure adequate and continuous funding for Peru’s development program. I would like to know from staff in this respect, how far discussions have gone in Peru about making use of SWAps and harmonization of procedures.
As the CAS report correctly states, the main risks are of political nature and will have to be assessed based on first experiences with the incoming government to subsequently be addressed in a full CAS.

**Programmatic Social Reform Loan:**

As stated above, we welcome this loan which should assist the Peruvian authorities to stabilize the economic situation and to safeguard critical social expenditures. The aim for decentralization is also very welcome - as mentioned above - but it will not come automatic and it will not be easy. It needs a consistent strategy and an adequate monitoring of associated risks by the Bank. In this connection, I would also be interested to hear more from staff about the planned up-front triggers for the foreseen second programmatic loan.

**Second Rural Roads Project:**

I appreciate that this second rural roads project builds on the lessons learnt from the first one. We also understand that there is a good ex-ante assessment of the socioeconomic situation in the project areas (established under the first project), against which the project impact can be measured. We wonder, however, why besides the access to health posts, the access to schools and the improved access to markets (important for boosting agricultural production) are not also included among the key indicators for such impact assessments (Chapter 2 on page 2 of PAD, and Annex 1).

Why is it still the intention to implement this project under a PIU (PCR, Chapter 4 on page 14 of the PAD) which will hamper the strengthening of local institutions under a decentralization exercise (cf. also comments above). Could staff elaborate.