Multiannual Macroeconomic Framework

2001-2003

MINISTRY OF ECONOMY AND FINANCE

ECONOMIC PROGRAM AND DECLARATION OF FISCAL POLICY PRINCIPLES

1. The main objective of the economic program is to attain a substantial and sustained rate of economic growth in the medium and long run, coupled with low inflation and a level of international reserves that ensures the sustainability of the external accounts. A prudent fiscal policy would allow private investment —which is the key to the creation of permanent jobs and the elimination of poverty— to become the engine of growth. The achievement of this goal calls for an economic environment designed to attract private investment.

2. Fiscal policy, according to the Fiscal Responsibility and Transparency Law, will seek to restore fiscal equilibrium in the least possible time and without risking economic recovery, in order to avoid crowding out private investment and exerting pressure on the current account. That will widen the scope for private sector decisions concerning investment and saving, diminish the fiscal burden of future generations and contribute to build investors' confidence, both domestically and abroad. Tax policy —guided by fiscal prudence and the principles of neutrality, simplicity and equity— will aim at building a structure based on three kinds of taxes —VAT (Impuesto General a las Ventas), Income Tax (Impuesto a la Renta) and Excise Taxes (Impuesto Selectivo al Consumo)— as well as a tariff that fosters efficiency and competitiveness. Additionally, efficiency in public expenditure performance will be evaluated through results. In this way, the necessary resources will be released to increase social expenditure, reduce the public debt burden and alleviate the tax burden on the private sector.

3. Economic policy will aim at consolidating economic stability and growth, which will reduce country risk and, consequentially, domestic interest rates. Interest rates will continue to be determined through market mechanisms and will reflect conditions in the money market and the risk associated with financial transactions. The exchange rate will continue to be determined by the market under the floating regime, which allows the real exchange rate to adjust to economic fundamentals. This will diminish the negative impact of unforeseen foreign shocks and contribute to maintain the viability of the balance of payments.

4. Companies will continue to recover thanks to efforts aimed at eliminating their difficulties in restructuring their financial obligations. Such policies will provide the conditions for a sustained recovery of credit. Additionally, the government will continue to promote the strengthening of the financial system by enforcing a modern prudential regulatory framework and encouraging market solutions, including mergers, private capitalization and the improvement of risk management and internal control.

5. Policies aimed at ensuring macroeconomic stability will be coupled with others intended to foster investment and production, thus promoting efficiency, productivity, competitiveness and employment. This will enable the country to reap further gains from integration into international markets.

6. Trade policy will continue to pursue greater market openness —in compliance with World Trade Organization (WTO) agreements— with the aim of promoting competitiveness. Additionally, prudent fiscal policies will contribute to building an adequate level of international reserves that will help preserving the economy against unforeseen events in the international market.

FISCAL POLICY

1. The Multiannual Macroeconomic Framework (MMF) for 2001-2003 assumes that no negative external or domestic events will occur, and that there will be a strengthened financial system. Additionally, the forecasts contained in the MMF are consistent with the Central Bank monetary program, which is described in the attached report. In a stable environment like the one foreseen, it is essential that the public sector keeps a cautious behavior in order to preserve fiscal discipline and promote saving. The latter could be applied to alleviating the effects of negative unforeseen effects, such as external crises or climatic disturbances to which Peru is exposed. Thus, the use of accumulated fiscal resources could attenuate the effect of any such external or domestic contingency on demand.
2. According to the Fiscal Responsibility and Transparency Law, fiscal policy will seek to equilibrate Public Sector revenues and expenditures in 2003. The Public Sector deficit is forecasted at 1,3 and 0,8 percent of GDP in 2001 and 2002, respectively.
3. General Government revenues are forecasted at around 14 percent of GDP in 2001-2003, which involves the reduction of certain taxes, as the recovery of domestic demand and the improvement of tax administration result in a better fiscal position. Through these policies the tax system will promote investment and saving, which are essential to attain the growth path foreseen in the MMF. Thus, during this period the tax system will be adjusted according to the principles of neutrality, simplicity and equity.
4. By introducing the adjustments mentioned above, it is expected that both tax and non-tax revenues will remain at approximately the same level estimated for 2000. This is also the case of the current revenues of the other organizations of the General Government, which are estimated at 0,9 percent of GDP.
5. Capital revenues —transfers from public enterprises— will be stable at 0,1 percent of GDP in 2001-2003.
6. Non-financial General Government expenditures will remain constant in real terms in 2001-2003. In compliance with Rule 2 of the Fiscal Responsibility and Transparency Law, they will increase at a rate equal to average inflation. This will be consistent with prioritized and targeted social expenditure, especially in health, education and public security in the least-favored regions. Additionally, public administration will continue to be simplified with the aim of improving the quality and effectiveness of public services.
7. General Government financial expenditures —mainly Central interest payments— are forecasted at a yearly average level of 1,9 percent of GDP.

8. Financing of the Public Sector deficit in 2001-2003 will come mainly from external sources and the use of fiscal resources.
9. The privatization and concession program will continue with the aim of promoting the additional investment needed to ensure sustained growth in the next few years. Concessions will be awarded for roads, airports and ports. In addition, these resources will give further strength to the international reserve position and will partially finance social expenditure.

MACROECONOMIC SCENARIO

1. The MMF forecasts GDP annual average growth at 6 percent in 2001-2003, which will absorb the increase in the economically active population (estimated at an annual 3 percent) and raise per capita GDP. The forecasted growth will rely on a 9,4 percent and 9,2 percent average increase in private investment and real exports of goods and services, respectively. Investment would increase its ratio relative to GDP from 22,5 percent in 2000 to 24,7 percent in 2003, respectively, which is consistent with a 6 percent average rate of growth of GDP in the medium run. Domestic demand growth at a lower rate than GDP (an average annual rate of 5 percent), would improve the external accounts. The 4,5 percent annual increase in private consumption would result in a 2,7 percent annual increase in per capita consumption. In the primary and non-primary sectors, a homogenous growth pattern will result in substantial job creation.
2. The Central Bank Monetary Program forecasts inflation at a rate between 2,5 and 3,5 percent in 2001 and between 1,5 and 2,5 percent in 2002 and 2003. The Monetary Program also foresees a 0,6 percent average rate of growth for the real exchange rate, as well as a conservative evolution for the terms of trade.
3. According to Central Bank forecasts, the current account deficit would be 4,1 percent of GDP on average. Imports associated with the expected increase in foreign investment would result in a higher deficit in 2001, but it would decrease in the following years. The trade deficit will follow the same pattern as the current account deficit: exports and imports will grow at an average rate of 12,3 percent and 10,7 percent in 2001-2003, respectively.
4. The MMF foresees a reserve accumulation of US$ 700 million in 2001-2003 (US$ 300 million in 2001 and US$ 200 in 2002 and 2003), which is consistent with the forecasted current account deficit. This will strengthen the external position and reduce the country's vulnerability to unforeseen external shocks.
5. Financing of the current account deficit is guaranteed. The greater part of it will come from long-term private capitals and revenues from privatizations. Thus, it will be possible to reduce foreign disbursement requirements during this period.
6. The policies proposed, together with the prudent monetary policy to be implemented by the Central Bank in 2001-2003, will allow private sector expansion to lead the foreseen growth rate (a 6 percent annual average rate). In this context, a prudent fiscal policy —which would increase the primary surplus from 0,8 percent in 2001 to 1,8 percent in 2003 as a minimum— is intended to

prevent the foreseen increase in private consumption and investment from exerting pressure on the aggregate demand and the balance of payments.

7. Peru is an emerging economy and, as such, is exposed to terms-of-trade shocks and natural phenomena that could affect the productive structure. Additionally, abrupt disturbances in the international financial markets could occur given the ongoing globalization of the world economy. Thus, it is essential to implement a prudent fiscal policy —such as the one proposed in the MMF— in order to generate in the medium run enough savings to allow the country to absorb unforeseen shocks without significantly affecting the population’s consumption level.

MINISTRY OF ECONOMY AND FINANCE

APPENDIX

Table 1
GENERAL GOVERNMENT REVENUES
(Millions of Nuevos Soles)

	1998	1999	2000	2001	2002	2003
CURRENT REVENUES	**27 462**	**26 571**	**29 385**	**32 168**	**33 981**	**36 546**
CENTRAL GOVERNMENT	**25 733**	**24 693**	**27 443**	**30 038**	**31 842**	**34 164**
TAX REVENUES	22 114	22 055	24 615	26 725	28 654	30 988
Income Tax	5 861	5 072	5 600	6 606	7 067	7 893
Import tax	2 465	2 397	2 695	2 878	2 965	3 151
Value Added Tax (IGV and IPM)	10 781	10 823	12 217	14 070	15 567	16 937
Excise Taxes (ISC)	3 394	3 412	3 900	4 376	4 596	4 971
Other	1 340	2 228	2 451	1 334	1 424	1 476
Certificates	-1 727	-1 877	-2 248	-2 539	-2 965	-3 440
NON-TAX REVENUES	3 619	2 638	2 828	3 313	3 188	3 176
OTHER ENTITIES	**1 729**	**1 878**	**1 942**	**2 130**	**2 139**	**2 382**
CAPITAL REVENUES	**540**	**518**	**460**	**330**	**247**	**265**
TOTAL GENERAL GOVERNMENT REVENUES	**28 002**	**27 089**	**29 845**	**32 498**	**34 228**	**36 811**

MINISTRY OF ECONOMY AND FINANCE

Table 2
GENERAL GOVERNMENT REVENUES
(Percentage of GDP)

	1998	1999	2000	2001	2002	2003
CURRENT REVENUES	**14,9**	**13,7**	**13,9**	**14,0**	**13,8**	**13,8**
CENTRAL GOVERNMENT	**14,0**	**12,8**	**13,0**	**13,1**	**12,9**	**12,9**
TAX REVENUES	12,0	11,4	11,7	11,7	11,6	11,7
Income Tax	3,2	2,6	2,7	2,9	2,9	3,0
Import tax	1,3	1,2	1,3	1,3	1,2	1,2
Value Added Tax (IGV and IPM)	5,9	5,6	5,8	6,1	6,3	6,4
Excise Taxes (ISC)	1,8	1,8	1,8	1,9	1,9	1,9
Other	0,7	1,2	1,2	0,6	0,6	0,6
Certificates	-0,9	-1,0	-1,1	-1,1	-1,2	-1,3
NON-TAX REVENUES	2,0	1,4	1,3	1,4	1,3	1,2
OTHER ENTITIES	**0,9**	**1,0**	**0,9**	**0,9**	**0,9**	**0,9**
CAPITAL REVENUES	**0,3**	**0,3**	**0,2**	**0,1**	**0,1**	**0,1**
TOTAL GENERAL GOVERNMENT REVENUES	**15,2**	**14,0**	**14,1**	**14,1**	**13,9**	**13,9**

Table 3
GENERAL GOVERNMENT EXPENDITURES
(Millions of Nuevos Soles)

	1998	1999	2000	2001	2002	2003
NON-FINANCIAL EXPENDITURES	**26 472**	**28 711**	**29 829**	**31 112**	**31 824**	**32 263**
Of which:						
Projects in execution	5 716	6 684	6 962	6 668	6 767	6 754
New investments	1 961	781	928	1 150	1 191	1 588
INTEREST	**3 126**	**3 598**	**4 219**	**4 492**	**4 679**	**4 786**
TOTAL EXPENDITURES	**29 598**	**32 309**	**34 048**	**35 604**	**36 503**	**37 049**

MINISTRY OF ECONOMY AND FINANCE

Table 4
GENERAL GOVERNMENT EXPENDITURES
(In Percentage of GDP)

	1998	1999	2000	2001	2002	2003
NON-FINANCIAL EXPENDITURES	**14,4**	**14,9**	**14,1**	**13,5**	**12,9**	**12,2**
Of which:						
Projects in execution	3,1	3,5	3,3	2,9	2,7	2,6
New investments	1,1	0,4	0,4	0,5	0,5	0,6
INTEREST	**1,7**	**1,9**	**2,0**	**2,0**	**1,9**	**1,8**
TOTAL EXPENDITURES	**16,1**	**16,7**	**16,1**	**15,5**	**14,8**	**14,0**

Table 5
OVERALL PUBLIC SECTOR DEFICIT/SURPLUS
(Millions of Nuevos Soles)

	1998	1999	2000	2001	2002	2003
GENERAL GOVERNMENT	**-1 596**	**-5 220**	**-4 203**	**-3 106**	**-2 275**	**-238**
REST	**293**	**130**	**212**	**230**	**247**	**265**
TOTAL	**-1 303**	**-5 090**	**-3 991**	**-2 876**	**-2 028**	**27**
FINANCING	**1 303**	**5 090**	**3 991**	**2 876**	**2 028**	**-27**
EXTERNAL	621	-97	2 110	230	247	-794
DOMESTIC [1/]	682	5 187	1 881	2 646	1 781	767

[1/] Includes the use of revenues from privatization.

Table 6
OVERALL PUBLIC SECTOR DEFICIT/SURPLUS
(Millions of Nuevos Soles)

	1998	1999	2000	2001	2002	2003
GENERAL GOVERNMENT	**-0,9**	**-2,7**	**-2,0**	**-1,4**	**-0,9**	**-0,1**
REST	**0,2**	**0,1**	**0,1**	**0,1**	**0,1**	**0,1**
TOTAL	**-0,7**	**-2,6**	**-1,9**	**-1,3**	**-0,8**	**0,0**
FINANCING	**0,7**	**2,6**	**1,9**	**1,3**	**0,8**	**0,0**
EXTERNAL	0,3	-0,1	1,0	0,1	0,1	-0,3
DOMESTIC [1/]	0,4	2,7	0,9	1,2	0,7	0,3

[1/] Includes the use of revenues from privatization.

Table 7
PROJECTION OF THE PUBLIC DEBT SERVICE
(Millions of US$)

	Disbursed Loans		Debt to be disbursed or settled		Total	
	Domestic	External	Domestic	External	Domestic	External
2000	227	1 752	0	34	227	1 786
2001	264	1 806	0	127	264	1 932
2002	296	1 847	0	203	296	2 050
2003	264	1 966	0	268	264	2 234
2004	282	1 968	0	313	282	2 281
2005	224	1 950	0	415	224	2 365
2006	206	1 911	0	482	206	2 393
2007	197	1 903	0	563	197	2 466
2008	161	1 838	0	620	161	2 458
2009	164	1 784	0	602	164	2 386
2010	79	1 630	0	554	79	2 184

Note:	**External Debt**	**Domestic Debt**
	(Balances in millions of US$)	
2001	20 142	1 345
2002	20 361	1 171
2003	20 227	1 023

Table 8
MAIN MACROECONOMICS INDICATORS

	1998	1999	2000	2001	2002	2003
Gross Domestic Product						
Annual percent change	0,3	3,8	5,0	5,5	6,0	6,0
Billions of Nuevos Soles	183,8	193,3	211,0	229,9	247,1	264,6
Exchange Rate						
Annual average	2,93	3,38	3,55	3,68	3,72	3,72
End of period	3,14	3,49	3,65	3,71	3,72	3,72
Consumer Price Index						
Average (annual percent change)	7,3	3,5	4,0	3,5	2,2	1,7
End of period (annual percent change)	6,0	3,7	4,0	3,0	2,0	1,5
External Sector (Millions of US$)						
Exports	5 735	6 114	7 035	7 678	8 900	9 958
Imports	8 200	6 714	7 416	8 404	9 240	10 049

Table 9
GLOBAL SUPPLY AND DEMAND
(Percent changes)

	1998	1999	2000	2001	2002	2003	Average 2001-2003
I. GLOBAL DEMAND (1+2)	**0,3**	**-0,6**	**5,4**	**6,4**	**6,3**	**5,9**	**6,2**
1. Domestic demand	-0,6	-3,0	5,2	6,2	4,6	4,7	5,2
a. Private consumption	-0,4	0,9	4,0	4,4	4,5	4,5	4,5
b. Public consumption	1,8	3,2	1,4	0,0	1,0	0,4	0,5
c. Gross domestic investment	-1,5	-12,3	9,1	11,8	5,8	6,3	7,9
- Private	-2,3	-15,7	12,8	13,6	7,1	7,7	9,4
- Public	3,4	7,2	-7,7	2,3	-2,1	-3,3	-1,0
2. Exports	3,3	7,5	5,7	7,0	11,5	9,1	9,2
II. GLOBAL SUPPLY (3+4)	**0,3**	**-0,6**	**5,4**	**6,4**	**6,3**	**5,9**	**6,2**
3. Gross Domestic Product	0,3	3,8	5,0	5,5	6,0	6,0	5,8
4. Imports	0,1	-17,1	6,9	10,9	7,7	5,4	8,0

Table 10
GROSS DOMESTIC PRODUCT
(Percent changes)

		1998	1999	2000	2001	2002	2003	Average 2001-2003
I.	**AGRICULTURE AND LIVESTOCK**	**3,6**	**12,1**	**3,5**	**4,5**	**4,5**	**4,5**	**4,5**
II.	**FISHING**	**-35,6**	**66,3**	**18,5**	**4,8**	**3,5**	**3,5**	**3,9**
III.	**MINING AND FUEL**	**4,8**	**10,0**	**5,9**	**6,1**	**11,5**	**7,1**	**8,2**
IV.	**MANUFACTURING**	**-2,8**	**7,6**	**7,1**	**5,5**	**5,1**	**5,9**	**5,5**
	1. Based on raw materials	-10,6	22,2	9,8	5,5	4,1	5,0	4,9
	2. Non-primary industries	0,4	2,3	6,0	5,5	5,5	6,2	5,8
V.	**CONSTRUCTION**	**1,3**	**-12,3**	**6,4**	**8,2**	**8,0**	**7,5**	**7,9**
VI.	**COMMERCE**	**-2,2**	**-0,5**	**4,3**	**5,5**	**5,7**	**6,2**	**5,8**
VII.	**OTHER SERVICES**	**1,5**	**1,5**	**3,5**	**4,8**	**4,9**	**5,7**	**5,1**
VIII.	**GDP**	**0,3**	**3,8**	**5,0**	**5,5**	**6,0**	**6,0**	**5,8**
	GDP primary sectors	-0,6	13,7	5,7	5,2	6,6	5,7	5,8
	GDP non-primary sectors	0,9	-3,7	4,5	5,7	5,5	6,2	5,8

MINISTRY OF ECONOMY AND FINANCE

MULTIANNUAL MACROECONOMIC FRAMEWORK 2001-2003

The following report evaluates the Multiannual Macroeconomic Framework (MMF) draft submitted by the Ministry of Economy and Finance to the Central Reserve Bank of Peru.

1. MACROECONOMIC OBJECTIVES

a. The fiscal and monetary policies and the structural reforms are geared to attain a high and sustainable rate of growth in real terms, coupled with low inflation and an adequate level of net international reserves. A responsible economic management aimed at achieving these goals, as well as a set of targeted poverty reduction strategies, will lead to an improvement of the population's living standards.

b. GDP average growth in 2000-2003 would be close to 6 percent, which is consistent with the economic recovery that has taken place since the last quarter of 1999. Economic activity was attenuated by the El Niño events, the deterioration of the terms of trade of Peruvian exports in 1998 and 1999, and the foreign credit squeeze that occurred in the last quarter of 1998. In addition to the stimulus from macroeconomic stability, growth requires structural reforms aimed at improving resource allocation, encouraging investment and creating jobs.

c. The reduction of inflation to an annual rate between 2,5-3,5 percent in 2001 and 1,5-2,5 percent in 2002-2003, creates favorable conditions for price stability, thus fostering investment and financial intermediation.

d. External soundness —reflected in a substantial level of net international reserves— provides a barrier against unexpected events in the international market. For that reason, it is convenient to ensure that net international reserves increase by US$ 230 million on average in 2001-2003.

e. Finally, it must be noted that this scenario assumes a normal environment with no adverse events, a strengthened financial system and a steady reduction of country-risk indicators consistent with the economic policy and the reform strategies to be implemented.

2. GDP GROWTH IN REAL TERMS

a. The MMF anticipates that GDP will grow at an average annual rate of 6 percent, which falls within the range forecasted by the Central Bank. It should be mentioned that growth in 2001 is expected to be lower than in 2002-2003 (5,5 percent vis à vis 6,0 percent).

Table 1
GROSS DOMESTIC PRODUCT
(Percent changes)

	2000	2001	2002	2003	Average 2001-2003
I. GLOBAL DEMAND (1 + 2)	**5,4**	**6,4**	**6,3**	**5,9**	**6,2**
1. Domestic demand	5,2	6,2	4,6	4,7	5,2
a. Private consumption	4,0	4,4	4,5	4,5	4,5
b. Public consumption	1,4	0,0	1,0	0,4	0,5
c. Gross domestic investment	9,1	11,8	5,8	6,3	7,9
- Private	12,8	13,6	7,1	7,7	9,4
- Public	-7,7	2,3	-2,1	-3,3	-1,0
2. Exports	5,7	7,0	11,5	9,1	9,2
II. GLOBAL SUPPLY (3 + 4)	**5,4**	**6,4**	**6,3**	**5,9**	**6,2**
3. Gross domestic product	5,0	5,5	6,0	6,0	5,8
4. Imports	6,9	10,9	7,7	5,4	8,0

An average rate of growth of around 6 percent between 2001 and 2003 is necessary to absorb the increase in the economically active population, which is estimated at an annual rate of 3,0 percent. To achieve these goals in production and employment, policy actions aimed at stimulating capital accumulation and factor productivity —which is essential to increase incomes and improve living standards— are required. The increase in production should preferably be directed to exports. These actions will secure conditions for private investment and exports of goods and services to provide the dynamism needed for growth. It should be stressed that, over the ten years to 2000, GDP, private investment and exports of goods and services grew at average annual rates of 4,6, 5,7 and 7,6 percent, respectively. GDP growth in real terms in 2001-2003 would rely on annual average rates of growth of private investment and exports of goods and services of 9,4 and 9,2 percent, respectively. Investment would increase its ratio relative to GDP from 22,5 percent in 2000 to 24,7 percent in 2003, which is consistent with the desired 6 percent rate of growth of GDP in the medium term. Domestic demand growth would be 5 percent per year. To the extent that this rate of growth is lower than that of GDP, it will imply a strengthening of the external stance. The increase in private consumption is expected to be around 4,5 percent per year, which implies that per capita consumption would grow at an average annual rate of 2,7 percent.

b. Macroeconomic stability is a central determinant of investment, but structural reforms foster capital accumulation in sectors where limitations to private projects and low factor productivity growth prevail. These policies are crucial to reach the desired 6 percent average growth rate of GDP in 2001-2003. The most important structural reforms proposed are the following:

- **Continue the privatization process** with the aim of attracting foreign investment and improving efficiency for the benefit of consumers.

- **Grant concessions for airport, maritime port and road services** to promote investment in these sectors, foster competitiveness and allow the public sector to focus efforts on social priorities.

- **Continue to reduce the average tariff rate and tariff dispersion** in order to encourage competitiveness through increased market openness.

- **Continue the Reform of the State**. On the one hand, this involves reducing the share in collections of taxes on certain inputs or production factors, which distort resource allocation and reduce efficiency. This reform must be gradual and consistent with a prudent fiscal policy. As a result, the tax system would rely mainly on taxes on value added (Impuesto General a las Ventas) or income (Impuestos a la Renta), as well as on excise taxes on final consumption of fuel, alcohol and tobacco. On the other hand, the Reform of the State would involve improving the quality of public expenditure.

- **Continue reforms in sectors such as agriculture**, in order to promote private investment and job creation.

- **Develop capital markets** to encourage long-term financing, especially through the allocation of institutional investors' savings (pension funds, mutual funds and insurance companies).

c. Central Bank forecasts of GDP growth are based on the foreseen dynamism of several economic sectors, assuming the policies mentioned above are implemented and the economic and financial conditions in both the international and domestic markets are favorable.

Table 2
GROSS DOMESTIC PRODUCT
(Percent changes)

		2000	2001	2002	2003	Average 2001-2003
I.	**AGRICULTURE**	**3,5**	**4,5**	**4,5**	**4,5**	**4,5**
II.	**FISHING**	**18,5**	**4,8**	**3,5**	**3,5**	**3,9**
III.	**MINING AND FUELS**	**5,9**	**6,1**	**11,5**	**7,1**	**8,2**
IV.	**MANUFACTURING**	**7,1**	**5,5**	**5,1**	**5,9**	**5,5**
	1. Processing of primary goods	9,8	5,5	4,1	5,0	4,9
	2. Rest of industries	6,0	5,5	5,5	6,2	5,8
V.	**CONSTRUCTION**	**6,4**	**8,2**	**8,0**	**7,5**	**7,9**
VI.	**COMMERCE**	**4,3**	**5,5**	**5,7**	**6,2**	**5,8**
VII.	**OTHER SERVICES**	**3,5**	**4,8**	**4,9**	**5,7**	**5,1**
VIII.	**GDP**	**5,0**	**5,5**	**6,0**	**6,0**	**5,8**
	GDP primary sectors	*5,7*	*5,2*	*6,6*	*5,7*	*5,8*
	GDP primary sectors	*4,5*	*5,7*	*5,5*	*6,2*	*5,8*

- The agriculture and livestock sectors are expected to grow at 4,5 percent on average, reflecting the modernization that would take place in this period.

- Fishing would grow around 3,9 percent per year. A process of modernization and diversification is expected, especially in the production of high-quality fishmeal and canned and frozen goods.

- The mining and fuel sector is expected to grow at an average annual rate of 8 percent in 2001-2003. This rate of growth is explained by projects such as Antamina (copper-zinc-silver), Tintaya (gold-copper) and, at the end of the period, Camisea (natural gas and liquid fuels), as well as several projects such as Tantahuatay, La Quinua, La Zanja, Antapite, Cerro Lindo and Zona del Explorador, among others.

- Manufacturing production will grow by 5,5 percent per year in 2001-2003. Primary sector growth (5 percent) would rely on increased fishing and sugar production thanks to normal climatic conditions and —in the case of the latter— to the modernization of companies. Non-primary industries' growth (6 percent per year) would be explained by domestic market expansion, which will be possible thanks to higher incomes, the assimilation of new population groups, the demand derived from the rest of productive activities and the growth of exports.

- A greater dynamism in the construction sector (8 percent per year in 2001-2003). This would result from the recovery of private investment associated with the mining, fuel, manufacturing, tourism and trade sectors, as well as with concession for roads, airports and ports.

3. TRADE BALANCE

a. The MMF and Central Bank forecasts of the average annual growth of exports and imports in 2001 a-2003 are 12,3 percent and 10,7 percent, respectively.

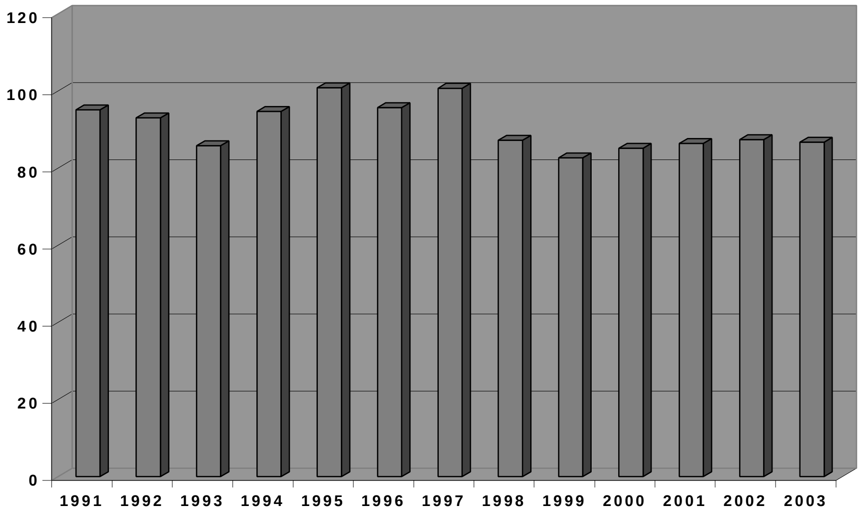
Table 3
TRADE BALANCE
(MillIons of U.S. dollars)

	2000	2001	2002	2003	Percent change 01/00	02/01	03/02	Average
1. EXPORTS	**7 035**	**7 678**	**8 900**	**9 958**	**9,1**	**15,9**	**11,9**	**12,3**
Tradicional goods	4 886	5 324	6 346	7 170	9,0	19,2	13,0	13,7
Mining	3 430	3 781	4 709	5 402	10,2	24,5	14,7	16,5
Oil	314	307	304	360	- 2,2	- 0,9	18,4	5,1
Agricultural	333	332	345	356	- 0,2	4,0	3,0	2,3
Fishing	808	903	986	1 052	11,7	9,2	6,6	9,2
Non-tradicional goods	2 055	2 228	2 423	2 649	8,4	8,8	9,3	8,8
Other	94	127	132	139	34,3	4,1	5,3	14,6
2. IMPORTS	**7 416**	**8 404**	**9 240**	**10 049**	**13,3**	**10,0**	**8,7**	**10,7**
Consumption goods	1 503	1 683	1 874	2 042	12,0	11,4	8,9	10,8
Intermediate goods	3 378	3 543	3 992	4 357	4,9	12,7	9,1	8,9
Capital goods	2 405	3 069	3 258	3 528	27,6	6,2	8,3	14,0
Other	130	109	116	122	- 15,9	6,3	5,4	-1,4
3. TRADE BALANCE (1-2)	**- 381**	**- 725**	**- 340**	**- 91**	**90,4**	**- 53,1**	**- 73,2**	**-12,0**

b. Given the growth of imports resulting from private investment dynamism, a trade deficit of US$ 725 million is expected. However, this deficit would tend to decrease in 2002 and 2003 to US$ 340 and US$ 91 million, respectively, as the projects mentioned above start the production phase.

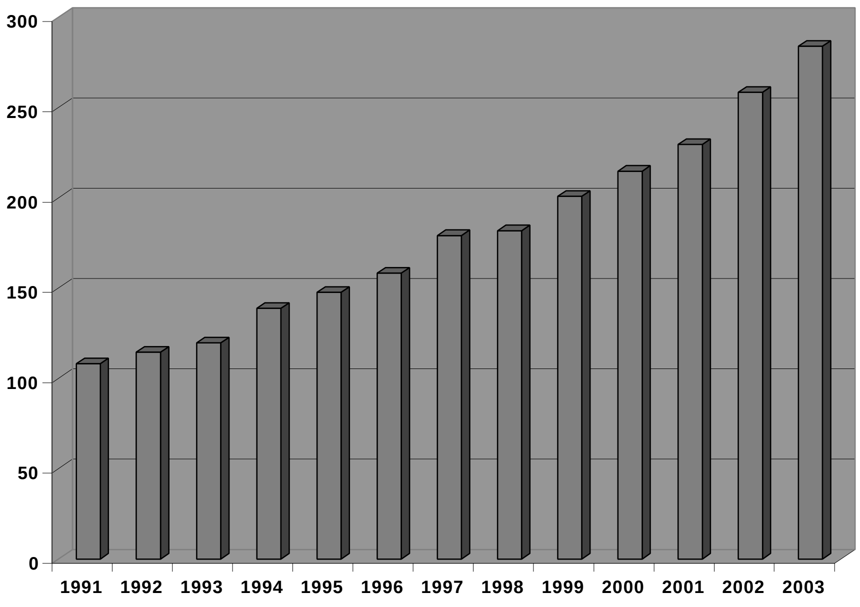
c. These estimates assume a 0,6 percent annual increase in the real exchange rate, as well as a conservative forecast for the evolution of the terms of trade. These are assumed to increase by 0,6 percent on average, resulting from the expected 2,3 percent increase in export prices, partially offset by a 1,7 percent increase in import prices. These trends in commodity prices are consistent with IMF forecasts of GDP growth, according to which the world economy would continue to grow, but at lower rates than in 2000, because of the expected slowdown of the American economy.

Graph 1
TERMS OF TRADE
(1990=100)



d. The export volume is expected to increase at a 10 percent annual average rate, with iron and copper exports growing at 65 and 23 percent per year, respectively.

Graph 2
VOLUME OF EXPORTS
(1990=100)



e. As a result, the value of exports would grow at a rate of 12,3 percent per year, with traditional and non-traditional exports growing at 13,7 percent and 8,8 percent, respectively. The most dynamic traditional exports would be iron (due to the expansion of Shougang) and copper and zinc (as Antamina enters the production phase). Among non-traditional exports, agriculture and fishing would show the highest rates of growth.

Table 4
TRADITIONAL EXPORTS
(Millions of U.S. dollars)

	2000	2001	2002	2003	Percent change 01/00	02/01	03/02	Average
FISHING	**808**	**903**	**986**	**1052**	**11,7**	**9,2**	**6,6**	**9,2**
Fishmeal	721	805	879	937	11,6	9,2	6,6	9,1
Volume (thousands of t.)	1873	1930	1970	2019	3,0	2,1	2,5	2,5
Price (US$/t.)	385	417	446	464	8,3	7,0	4,0	6,4
Fish oil	87	98	108	115	12,5	9,7	6,4	9,5
Volume (thousands of t.)	350	360	363	372	2,9	0,8	2,6	2,1
Price (US$/t.)	250	273	297	308	9,4	8,8	3,7	7,3
AGRICULTURAL	**333**	**332**	**345**	**356**	**- 0,2**	**4,0**	**3,0**	**2,3**
Cotton	2	2	2	3	8,3	8,1	9,4	8,6
Volume (thousands of q.)	27	29	30	31	4,8	4,2	4,4	4,5
Price (US$/q.)	77	80	83	87	3,3	3,8	4,8	4,0
Coffee	296	309	321	331	4,2	4,2	3,0	3,8
Volume (thousands of t.)	149	151	154	157	1,7	2,0	1,9	1,9
Price (US$/q.)	92	94	96	97	2,5	2,1	1,0	1,9
Rest of agricultural goods 1/	34	22	22	22	.35,3	0,0	0,0	11,7
MINING	**3430**	**3781**	**4709**	**5402**	**10,2**	**24,5**	**14,7**	**16,5**
Copper 2/	910	1002	1360	1828	10,1	35,8	34,3	26,7
Volume (thousands of t.)	528	574	747	975	8,8	30,1	30,5	23,1
Price (¢US$/lb.)	78	79	83	85	1,2	4,4	2,9	2,8
Tin	168	200	202	209	19,1	1,3	3,4	7,9
Volume (thousands of t.)	32	36	36	37	13,6	0,0	1,4	5,0
Price (¢US$/lb.)	240	252	255	260	4,9	1,3	2,0	2,7
Iron	100	116	422	444	15,2	265,0	5,2	95,1
Volume (thousands of l.tn.)	5	5	15	15	8,4	185,7	2,0	65,4
Price (US$/l.tn.)	21	22	28	29	6,3	27,7	3,1	12,4
Gold	1271	1368	1468	1595	7,7	7,3	8,7	7,9
Volume (thousands of tr.oz.)	4400	4560	4674	4884	3,6	2,5	4,5	3,5
Price (US$/tr.oz.)	289	300	314	327	3,9	4,7	4,0	4,2
Refined silver	175	188	203	228	7,3	8,1	12,3	9,2
Volume (thousands of tr.oz.)	33	35	38	42	6,4	7,1	11,3	8,3
Price (US$/tr.oz.)	5	5	5	5	0,9	0,9	0,9	0,9
Lead 2/	200	237	248	259	18,9	4,2	4,7	9,3
Volume (thousands of t.)	233	253	260	271	8,8	2,9	4,0	5,2
Price (¢US$/lb)	39	43	43	43	9,3	1,3	0,7	3,8
Zinc	571	630	763	792	10,4	21,0	3,9	11,8
Volume (thousands of t.)	733	790	953	940	7,8	20,6	- 1,3	9,0
Price (¢US$/lb)	35	36	36	38	2,5	0,3	5,3	2,7
Rest of mining products	36	40	43	47	11,1	8,0	8,0	9,0
OIL	**314**	**307**	**304**	**360**	**- 2,2**	**- 0,9**	**18,4**	**5,1**
Volume (millons of barrels)	16	18	19	23	16,3	3,5	18,9	12,9
Price (US$/barrel)	20	17	16	16	- 15,9	- 4,2	- 0,4	- 6,8
TRADITIONAL EXPORTS	**4886**	**5324**	**6346**	**7170**	**9,0**	**19,2**	**13,0**	**13,7**

1/ Includes coca leaves, molasses, wool, fur and sugar.
2/ Includes silver content.

f. Imports would grow by 10,7 percent per year. The most dynamic could be capital-good imports (13 percent per year) due to private investment growth. These forecasts rely on the continuation of trade reforms.

4. BALANCE OF PAYMENTS

a. The stability of the Peruvian economy requires an adequate level of international liquidity. In this context, the forecasted balance of payments foresees an accumulation of Central Bank net international reserves of US$ 300 million for 2001 and US$ 200 million in 2002-2003. Total amortization of short- and long-term debt, both public and private, would stay at 75 percent of net international reserves, which reinforces the country's foreign position and reduces its vulnerability to eventual foreign shocks.

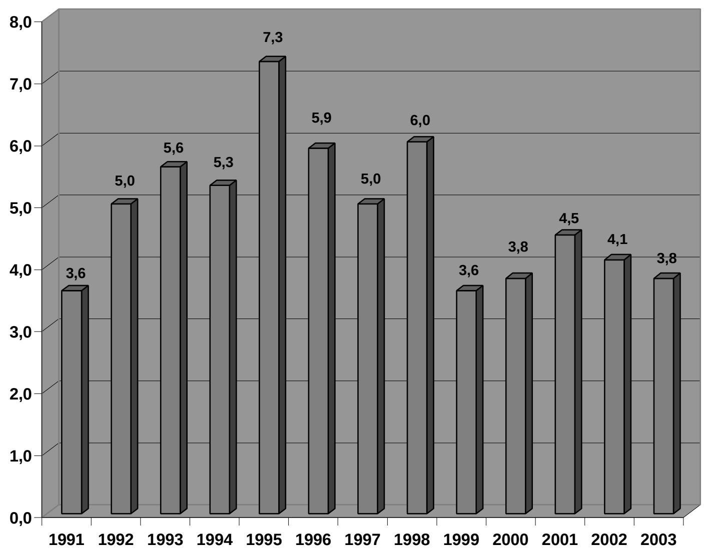
Table 5
BALANCE OF PAYMENTS
(MillIons of U.S. dollars)

	2000	2001	2002	2003	Percentage of GDP 2000	2001	2002	2003
A. CURRENT ACCOUNT BALANCE	**-2 279**	**-2 842**	**-2 754**	**-2 691**	**- 3,8**	**- 4,5**	**- 4,1**	**- 3,8**
B. FINANCIAL ACCOUNT	**2 579**	**3 142**	**2 954**	**2 891**	**4,3**	**5,0**	**4,4**	**4,1**
i. Private	1 535	1 969	2 242	2 869	2,6	3,2	3,4	4,0
ii. Privatization 1/	404	1 000	1 000	850	0,7	1,6	1,5	1,2
iii. Public 2/	494	6	- 294	- 833	0,8	0,0	- 0,4	- 1,2
iv. Short term 3/	146	168	6	5	0,2	0,3	0,0	0,0
C. CENTRAL BANK NIR FLOW	**300**	**300**	**200**	**200**	**0,5**	**0,5**	**0,3**	**0,3**

1/ Includes only payments by non-residents.
2/ Incluye Fondo de Estabilidad Fiscal (FEF) investments (Law 27245).
3/ Includes exceptional financing and errors and omissions.

b. Reserve accumulation is consistent with an average current account deficit of US$ 2 762 million in 2001-2003, which is equivalent to 4,1 percent of GDP. It should be noted that the deficit is higher in 2001 (4,5 percent of GDP), due to the concentration of foreign investment projects and, consequentially, of the imported component. In 2003 the current account deficit would reach 3,8 percent of GDP.

Graph 3
CURRENT ACCOUNT DEFICIT
(Percentage of GDP)



c. The services balance would virtually stay at 1,2 percent of GDP (US$ 774 million) in this period, basically due to the imported components of services associated with the greater foreign investment. This would be offset by the increase in revenues from tourism. Net factor income would become increasingly negative due to a greater remission of profits and reinvestment associated with returning private capitals and the greater public and private interest payments.

d. The greater part of the deficit will be financed with long-term private capitals —excluding privatization— which would amount to US$ 2,4 billion (3,5 percent of GDP) on average. The most important are the mining investments and Camisea, which involve more than US$ 7 500 million in this period.

e. It should be stressed that this level of international reserves requires privatization revenues from abroad of US$ 2 850 million (a yearly average of US$ 950 million) between 2001 and 2003, which would reduce foreign disbursement requirements.

f. The public sector financial account for 2001-2003 is forecasted at US$ -373 on average for 2001-2003, under the assumption that the Fondo de Estabilización Fiscal and the Fondo Nacional de Ahorro Público (FONAHPU) would deposit a yearly average of US$ 318 million abroad. These are a support against eventual negative exogenous shocks.

g. Yearly public sector disbursements —including those of the Corporación Financiera de Desarrollo (COFIDE)— would amount to US$ 1 089 million. The most important are the investment projects, with a yearly average level of US$ 870 million.

   In 2001-2003 the yearly average payment of interests and amortization of public debt amount to US$ 1 271 and US$ 1 025 million, respectively.

5. MACROECONOMIC GAPS

a. Economic growth in the coming years will rely on a greater private investment, at a level that will be consistent with the continuation of the structural reforms and a climate of confidence and macroeconomic stability. The greater private sector expenditure will not result in pressure on aggregate demand or the balance of payments, only if public finances are managed in a prudent way.

b. As was mentioned before, the external gap would increase in 2001 due to greater imports associated with investment projects. However, it would decrease gradually since 2002, with the beginning of operations of several mining projects. Private investment requirements would increase from 18,7 percent in 2000 to 21,5 percent in 2003, while private saving would increase by 0,8 percentage point over the said period, that is, from 16,7 percent to 17,5 percent of GDP.

Table 6
MACROECONOMIC GAPS
(Percentage of GDP)

	2000	2001	2002	2003
1. External gap (2+3=a-b)	**-3,8**	**-4,6**	**-4,3**	**-4,0**
a. Domestic saving	18,8	19,6	20,1	20,7
b. Total investment	22,6	24,2	24,4	24,7
2. Private sector gap (a-b)	**-2,0**	**-3,3**	**-3,5**	**-4,0**
a. Private saving	16,7	17,1	17,4	17,5
b. Private investment	18,7	20,4	20,9	21,5
3. Public sector gap (a-b)	**-1,8**	**-1,3**	**-0,8**	**0,0**
a. Primary balance	0,3	0,8	1,2	1,8
b. Interests	2,1	2,1	2,0	1,8

c. The public sector should converge to equilibrium by 2003. Under this scenario, the public sector is expected to attain a minimum primary result of 0,8 percent of GDP in 2001, and reach 1,8 percent of GDP in 2003.

6. PUBLIC FINANCES

a. There is a coincidence with the objective of attaining a fiscal equilibrium in 2003 stated in the Multiannual Macroeconomic Framework draft. Taking into consideration this objective and the cost in terms of tax collection of the structural reforms intended to increase the competitiveness of the economy, these measures should be implemented gradually. It is important to continue to improve the tax administration in order to expand the tax base and enforce a better control of evasion.

b. On the other hand, it is advisable to design an efficient financing policy, that is to say, to the smallest cost and greatest term. The amortization requirements as of December 31, 1999, amount to an annual average of US$ 873 million in 2001-2003. These requirements, added to the deficit in 2001 and 2002, would demand funding that may come from foreign disbursements and from privatization revenues that are not destined to the Fiscal Stabilization Fund.

Targets and scope

c. The Fiscal Responsibility and Transparency Law establishes that a fiscal balance or surplus should be attained in the medium term, mainly through two numerical targets:

- The public sector deficit should not exceed 1 percent of GDP. This limit is fixed at 2 and 1,5 percent of GDP for 2000 and 2001, respectively.

- The non-financial expenditure of the General Government should not exceed the inflation rate plus two percentage points.

d. Acoording to the mentioned law, the General Government covers the institutions and organizations of the Central Government, the regional government and other decentralized instances, as well as constitutionally autonomous organizations, excluding the Central Reserve Bank and the Superintendency of Banking and Insurance. Local governments, state-run firms EsSalud organizations for the regulation of public services are excluded.

Revenues

e. In 2001, Central Government current income is expected to reach 13,0 percent of GDP, which is similar to the level anticipated for 2000. This improvement would be a result of the greater dynamism of VAT and Income Tax collectionst, which in turn would reflect the recovery of economic activity induced by structural reforms.

f. The current revenue of the Rest of the General Government would amount to 0,9 percent of GDP. It includes mainly the income of Public Institutions assigned to ministries. General Government capital revenue would amount to 0,1 percent of GDP (S/. 339 million), which correspond basically Central Government revenue from donations and capital transfers from state-run companies. Thus, General Government revenue would amount to 14,1 percent of GDP, which is similar to the level foreseen for 2000, and would decrease to 13,9 and 13,8 percent of GDP in 2002 and 2003, respectively, as a result of the decrease of Central Government collections in terms of GDP mentioned above.

Expenditures

g. General Government nonfinancial expenditure anticipated in the Central Bank and MMF foreseen for 2001 would amount to 13,5 percent of GDP, 0,6 percentage points lower than the 2000 forecast. Given the forecasted revenue, expenditure is assumed to remain constant in real terms and grow at a rate equal to average inflation. This must be consistent with improving in the quality of expenditure and prioritizing social cost in health, education and public security.

h. According to the Central Bank and MMF forecasts, General Government nonfinancial expenditure would diminish progressively to 12,9 and 12,2 percent of GDP in 2002and 2003, respectively (of which 11,9 and 11,3 percent correspond to the Central Government), in compliance with the objective of attaining fiscal balance in the medium term.

i. General Government financial expenditure would amount to 2,0 percent of GDP in 2001, reflecting mainly the payment of Central Government interests, of which US$ 1 153 million correspond to foreign debt. Interest payment would amount to US$ 1 175 million and US$1 185 million in 2002 and 2003, respectively.

Economic result and its financing

j. Central Bank and MMF forecasts anticipate a Consolidated Public Sector deficit of 1,3 percentage points of GDP for 2001. In 2002-2003, the Consolidated Public Sector deficit will be progressively reduced until a balance is attained in 2003.

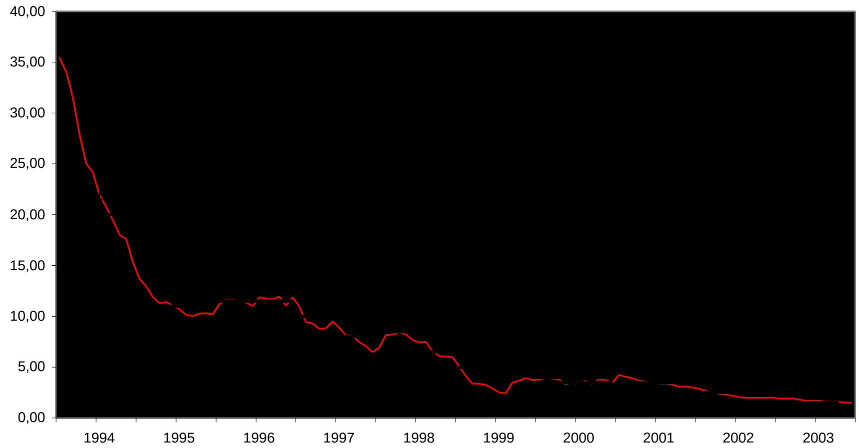
k. The greater part of the deficit would be financed domestically in 2001-2003, reflecting mainly new privatizations. Foreign debt disbursements would amount to a yearly average of US$ 920 million, of which US$ 253 million would correspond to freely available disbursements.

l. Even though there is coincidence in the MMF and Central Bank forecasts concerning total required financing, there are differences in the composition of the financing of the public sector deficit.

7. MONETARY POLICY

a. In compliance with the constitutional mandate of preserving stability, the monetary policy implemented by the Central Reserve Bank of Peru will continue to aim at gradually reducing the rate of inflation to industrial-country levels towards 2003. The rate of inflation is expected to be between 2,5 and 3,5 percent in 2001, and between 1,5 and 2,5 percent in 2002 and 2003.

Graph 4
ANNUAL TARGET INFLATION RANGES AND TWELVE-MONTH INFLATION



In this way the Central Bank contributes to macroeconomic stability, which is a fundamental condition for the achievement of sustained economic growth.

Table 7
TARGET RANGES
2000-2003

	RANGES	TARGETS
2000	3,5 - 4,0	4,0
2001	2,5 - 3,5	3,0
2002	1,5 - 2,5	2,0
2003	1,5 - 2,5	1,5

b. Price stability provides a macroeconomic framework that's suitable to attract productive investment and ensure sustained economic growth, thus contributing to raising the population's living standards. With stable prices, the economic agents have certainty about the future, and the economy works more efficiently.

Historical evidence shows that it is not possible to grow artificially with expansive monetary and fiscal policies since their effects are, at the best, temporary, and they are reverted at a high cost in terms of economic growth. Furthermore, the inflation deteriorates the distribution of income, since it affects lower-income groups more severely.

c. Inflation reduction will be the main mechanism to reinforce the public's preference for the domestic currency and thus continue the remonetization process. The rate of inflation foreseen by the MMF shows a decreasing pattern, similar to the one anticipated by the Central Bank.

d. Liquidity management through control of the monetary base growth will continue to be consistent with the inflation objective. Thus, since the design of the monetary policy implemented by Central Bank will be maintained, the interest rates and the exchange rate will continue to be determined through market mechanisms. Consequentially, Central Bank intervention in the foreign exchange market will take place under high exchange rate volatility. It is important to mention that a floating exchange rate regime —where the real exchange rate adjusts in line with economic fundamentals— attenuates the recessive impact of adverse external shocks maintains balance of payments viability.

e. The average balance of the monetary base will increase at an annual rate between 7,5 and 9,5 percent in 2001-2003, which is consistent with the inflation target ranges. The range established for the average monetary base growth is based on a 13.0 percent forecasted annual growth of the demand for domestic currency. This annual growth rate is greater in each year to the estimated increase in nominal GDP (between 6,8 and 9,0 percent), due to a greater preference of the public for domestic currency in response to decreasing inflation.

f. As far as the components of the money supply are concerned, the greater demand for soles (13 percent annually) would be covered with an increase in the banking multiplier of around 4 percent (associated to a greater financial intermediation in domestic currency) and the 7,5-9,5 percent increase in the monetary base mentioned above. It is important to mention that the expansion of the average monetary base is considered as a range, and not as a point rate, due to the variability that the demand by domestic currency could display.

Table 8
MONETARY POLICY VARIABLES
(Average percent changes)

	Nominal GDP	Liquidity in domestic currency		Average monetary base	Average multiplier Promedio
		Average	Velocity		
2000	9,1	9,0	0,1	9,0	0,0
2001	9,0	13,0	-3,5	8,5	4,1
2002	7,5	13,1	-5,0	8,5	4,3
2003	6,8	13,1	-5,6	8,5	4,3

g. The Central Bank will continue to use its instruments of monetary regulation in a way that is consistent with the increase in the monetary base. These instruments can be classified as: (a) market instruments: foreign exchange market interventions and auctions of Central Bank Deposit Certificates (primary and repo operations); (b) discount window instruments: monetary regulation credits and temporary foreign currency purchases (swaps); and (c) reserve requirements.

h. Given the perspectives of economic growth in the next years, as well as the consolidation of macroeconomic stability, it is expected that the improvements in the financial system will be reflected in a recovery of its solvency indicators. This will lead to greater creditworthiness and lower country risk, which will in turn result in lower interest rates and the recovery of credit to the private sector to levels that are consistent with the foreseen GDP growth rates.

8. FINAL COMMENTS

MMF forecasts aim at ensuring the achievement of a stable rate of real growth of around 6 percent in the next years, which will depend on the macroeconomic stability, notably a healthy fiscal position.

The forecasted growth requires structural reforms that eliminate the obstacles to productive resource allocation, especially through the privatization process, which is one of the most important mechanisms for the promotion of economic efficiency. It is also important to continue the trade reform and modify the current tax structure.

Finally, the application of prudent macroeconomic policies, complemented with targeted poverty-reduction policies, will improve the welfare of the population.

MINISTRY OF ECONOMY AND FINANCE

APPENDIX

MACROECONOMIC ASSUMPTIONS
2000-2003

	2000	2001	2002	2003
GDP growth (in real terms)	5,0	5,5	6,0	6,0
Accumulated inflation	4,0	3,0	2,0	1,5
Average exchange rate	3,55	3,68	3,72	3,72
Exports (millions of US$)	7 035	7 678	8 900	9 958
Imports (millions of US$)	7 416	8 404	9 240	10 049