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INTER-AMERICAN INVESTMENT CORPORATION

PERU

**IDB GROUP COUNTRY STRATEGY WITH PERU
(2017-2021)**

APRIL 2017

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ABBREVIATIONS

AFIN	Asociación para el Fomento de la Infraestructura Nacional [National Infrastructure Development Association]
BCRP	Central Reserve Bank of Peru
CAF	Development Bank of Latin America
CENAGRO	Censo Nacional Agropecuario [National Agricultural Census]
CGaR	Office of the Comptroller General of Peru
CIAT	Inter-American Center of Tax Administrations
ENAHO	Encuesta Nacional de Hogares [National Household Survey]
ENAPRES	Encuesta Nacional de Programas Estratégicos [National Survey of Strategic Programs]
ENDES	Encuesta Demográfica y de Salud Familiar [Demographic and Family Health Survey]
EPI	Environmental Performance Index
FAO	Food and Agriculture Organization
GDP	Gross domestic product
GWH	Gigawatt hour
IDB Group	IDB-IIC-MIF
IFPRI	International Food Policy Research Institute
ILO	International Labour Organization
IMF	International Monetary Fund
INEI	National Institute of Statistics and Information Technology
MEF	Ministry of Economy and Finance
MINAGRI	Ministry of Agriculture and Irrigation
MINAM	Ministry of the Environment
MINEDU	Ministry of Education
MINSa	Ministry of Health
MSMEs	Micro, small, and medium-sized enterprises
NDC	Nationally determined contribution
OECD	Organization for Economic Cooperation and Development
PBL	Policy-based loan
PCM	Presidency of the Council of Ministers
PPP	Public-private partnership
PRODUCE	Ministry of Production
R&D	Research and development
REDD	Reducing Emissions from Deforestation and Forest Degradation
RICYT	Red de Indicadores de Ciencia y Tecnología [Science and Technology Indicators Network]
SAIDI	System Average Interruption Duration Index
SAIFI	System Average Interruption Frequency Index
SIAF	Sistema Integrado de Administración Financiera [Integrated Financial Management System]
SIMS	Sistema de Información de Mercado Laboral y Seguridad Social [Labor Market and Social Security Information System]
SIS	Sistema Integral de Salud [Comprehensive Health Care System]
SMEs	Small and medium-sized enterprises
SNIP	Sistema Nacional de Inversión Pública [National Public Investment System]

SUNASS	Superintendencia Nacional de Servicios de Saneamiento [National Superintendency of Sanitation Services]
SUNAT	Superintendencia Nacional de Aduanas y de Administración Tributaria [National Superintendency of Customs and Tax Administration]
TFP	Total factor productivity
UNDP	United Nations Development Programme
WDI	World Development Indicators
WEF	World Economic Forum
WEO	World Economic Outlook

PERU
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(2017-2021 APRIL 2017)

EXECUTIVE SUMMARY

Economic and social context:	Peru is one of the greatest economic and social success stories in the region. A combination of structural reforms, prudent management of public policy, and favorable external conditions may be credited for this performance. The social arena shows encouraging advances. The global external outlook for the coming years is less propitious, and Peru faces the challenge of generating new sources of growth to continue to make strides on the path of social development.
The IDB Group in Peru:	The IDB Country Strategy with Peru 2012-2016 prioritized the following areas: (i) social inclusion; (ii) rural development and agriculture; (iii) housing and urban development; (iv) climate change and natural disaster risk management; (v) water, sanitation, water resources, and solid waste; (vi) energy; (vii) transportation; (viii) public management; and (ix) competitiveness and innovation. Twenty-seven sovereign-guaranteed loan operations were approved for a total of US\$1.645 billion, as well as 34 non-sovereign guaranteed operations for a total of US\$849.5 million. The MIF approved 30 operations for a total amount of US\$29.8 million.
Priority areas:	Under the 2017-2021 country strategy, the IDB Group intends to work on three areas: (1) productivity, with an emphasis on the labor market, business climate, business development, and infrastructure; (2) institutional strengthening and basic service delivery, with an emphasis on public management, health, and citizen security; and (3) environmental sustainability and climate change, with an emphasis on water resources, environmental management, and agribusiness. The proposed actions are aligned with the Peruvian government plan, which prioritizes (i) boosting and formalizing the economy; (ii) strengthening public management; (iii) improving the delivery of services to the population; and (iv) reinforcing environmental management.
Lending framework:	Approvals for the 2017-2021 period are projected at US\$1.5 billion. Sovereign-guaranteed disbursements are estimated at US\$1.25 billion, in addition to resources for private-sector projects to be contributed by the IIC and the MIF.
Risks:	The main risks in implementing the country strategy are associated with: (i) complex institutional coordination hampering the public investment design and implementation phases, with traditional public procurement and/or public-private partnerships (PPPs); and (ii) the weak management of some of the executing agencies in implementing investment projects.

Strategy validity period: The Country Strategy with Peru for 2017-2021 will be in effect from its approval to 30 July 2021.

I. CONTEXT¹

- 1.1 **Peru is an economic and social success story in the region.** The Peruvian economy has undergone a radical transformation over the last quarter of a century. From the instability and economic decline of the 1980s, the country has now become one of the region's most prosperous and promising economies. Particularly since the start of this century, Peru has experienced unprecedented economic expansion, with an average growth rate of over 5%. To date, despite a widespread economic slowdown, Peru remains one of the most dynamic economies, having grown in 2016 by an estimated 3.9%, as compared to an average growth of negative 0.7% for Latin America and the Caribbean. Between 2000 and 2016, the country's per-capita gross domestic product (GDP) grew at a real average rate of 3.5% to US\$6,021. Peru became an upper middle-income country (based on the World Bank ranking) in 2008 and is currently carrying out the Organization for Economic Cooperation and Development (OECD) program with a view to its potential admission as a member.²
- 1.2 **A series of structural reforms and prudent public policy management have been the key to the country's transformation.** The mid-1990s witnessed the start of a structural reform process that consolidated macroeconomic stability and laid the groundwork for the country's growth over the last 15 years. Milestones in this area include the Fiscal Responsibility and Transparency Law; the adoption of a system of inflation targets; a unified and free-floating exchange rate; a legal framework for promoting private investment; trade and financial liberalization; and the achievement of investment grade status.
- 1.3 **Favorable external conditions also contributed to the country's sound economic performance during the 2000s.** The commodities boom, coupled with stabilization measures, paved the way for increased tax revenue, a gradual reversal of fiscal deficits, and a doubling of public capital expenditures. At the same time, between 2000 and 2015, the public debt fell from 48% to 24% of GDP. This solid performance translated into a downward trend in sovereign differentials and access to financing at lower costs and for longer terms. Peru also benefited from favorable external financing conditions arising from the response to the global financial crisis, which brought interest rates in developed countries to historic lows. Specifically, Peru and other economies in the region were significant recipients of capital flows seeking higher yields.³
- 1.4 **The country's favorable economic performance led to a lower poverty level.** Between 2009 and 2015, the monetary poverty rate was reduced by more than half, from 33.5% to 21.8%.⁴ However, rural poverty is three times greater than urban poverty. Extreme poverty continues to be mostly rural (13.9% of the rural population vs. 1% of the urban population). In 2015, poverty affected 33.4% of the

¹ The CDC (electronic link) provides a more detailed description and includes the sources of data.

² IMF, WEO, and World Bank, World Development indicators.

³ IMF, WEO.

⁴ Monetary poverty is defined as the proportion of the population that spends a lower amount than the poverty line or extreme poverty line amount (INEI). In 2015, the extreme poverty line stood at 169 nuevos soles per capita per month and the poverty line was 315 nuevos soles per capita per month.

indigenous-language population. Inequality in income distribution, as measured by the Gini coefficient, also fell from 0.47 in 2009 to 0.44 in 2015.⁵

- 1.5 **The external scenario for the coming years looks less favorable for growth.** The end of the commodities supercycle and lower growth in China and other trading partners are circumstances affecting the country's fiscal and external position as well as its outlook for growth. Faced with an economic slowdown, the government adopted fiscal stimulus measures to spur domestic demand, generating a deficit of 2.6% of GDP and expanding public debt to 23.6% of GDP in 2016. At the same time, a normalization of United States monetary policy could raise the costs of external financing, introduce financial volatility into the markets, and reverse capital flows, with potential have implications for the exchange rate and inflation and for monetary policy management.
- 1.6 **In this less favorable external context, Peru faces the challenge of creating new sources of growth.** To ensure the sustainability of growth in the medium term and to continue to move forward on the path of social development, the country needs to boost economic productivity. This means having better public management and institutions with a view to providing quality public services. In turn, a rise in productivity requires conservation and sustainable use of natural resources aimed at protecting biodiversity and the environment.

II. IDB GROUP PRESENCE IN THE COUNTRY

- 2.1 **IDB Country Strategy with Peru 2012-2016.**⁶ The IDB Country Strategy with Peru 2012-2016 (document GN-2628) was aimed at helping to close the economic and social gaps between urban and rural areas and supporting an increase in economic productivity. To this end, it prioritized the following areas: (i) social inclusion; (ii) rural development and agriculture; (iii) housing and urban development; (iv) climate change and natural disaster risk management; (v) water, sanitation, water resources, and solid waste; (vi) energy; (vii) transportation; (viii) public management; and (ix) competitiveness and innovation. Inter-American Investment Corporation (IIC) and Multilateral Investment Fund (MIF) participation envisaged the creation of public-private partnerships (PPPs), investments in transportation infrastructure, and development of economic opportunities.

⁵ INEI.

⁶ The amounts of IDB loan operation approvals during the 2012-2016 country strategy cited in this document are based on IDB records. According to the records of the Ministry of Economy and finance (MEF), 26 IDB operations for a total amount of US\$1.09 billion were approved by the country during the same period. The difference in the amounts is due primarily to the fact that: (i) there was a lapse of time between operation approval by the IDB Board and the external borrowing by the Government of Peru; and (ii) the country did not account for the PBL/DDO operations (PE-L1154 and PE-L1169) since they were considered as contingent resources and not as part of the external borrowing program envisaged under the Peruvian government debt laws. During the 2012-2016 country strategy period, the MEF did not account for: US\$600 million from the PBL/DDO operations (PE-L1154 and PE-L1169) and US\$80 million from an investment operation (PE-L1151) approved by the IDB in December 2016. However, the MEF did account for US\$125 million from two investment operations (PE-L1062 and PE-L1067) approved by the IDB in the last quarter of 2011 and US\$300 million from the Contingent Loan for Natural Disaster Emergencies (PE-X1006) approved by the country as part of the country's contingent financing in the event of a natural disaster.

- 2.2 The country strategy envisaged total financing of US\$1.282 billion for the public sector (an average of US\$257 million per year). Between 2012 and 2016, the Bank approved US\$1.645 billion in sovereign-guaranteed loans (an average of US\$329 million per year), a larger amount than expected due to the 2015 approval of two policy-based loans (PBLs) with deferred drawdown option (DDO) for US\$600 million. Between 2012 and 2016, 27 sovereign-guaranteed operations were approved: 16 investment loans for US\$800 million and 11 PBLs for US\$845 million. Seventy-nine percent of the approved resources were concentrated on social inclusion, transportation, and rural development. In addition, 66 technical cooperation operations were approved for a total of US\$32 million, with an emphasis on fighting deforestation and climate change, social investment, and water and sanitation.
- 2.3 Non-sovereign operations with the private sector have made Peru the country with the second largest IIC exposure. In the aforementioned period, 34 such operations were approved for a total of US\$849.5 million, with an emphasis on transportation (48%), housing (14%), financial services (13%), and energy (12%). Worth noting is the IDB Group's support in transportation infrastructure through PPPs. In addition, also during the aforementioned period, the MIF approved 30 operations for a total amount of US\$29.8 million, primarily in value chains, regional economic development, and financial inclusion.
- 2.4 **Active portfolio.**⁷ The outstanding portfolio⁸ of sovereign-guaranteed operations consists of 22 operations for US\$1.275 billion, including 21 investment operations for US\$975 million, of which 27% (US\$342 million) has been disbursed.⁹ The average size of the portfolio's investment operations is US\$46.4 million. The portfolio contains a policy-based loan with deferred drawdown option for a total amount of US\$300 million. The IIC's outstanding portfolio has an exposure of US\$655.6 million, distributed in oil and gas (42%), energy (24%), financial intermediaries (23%), agribusiness (6%), education (5%), and tourism (1%). The outstanding portfolio of technical cooperation operations includes 23 operations for US\$19.5 million in infrastructure (61%); social sector (22%); strengthening of public management (12%); and others (5%). The MIF has 25 projects for US\$23.7 million, concentrated in business development, technical capacities, and financial services.

Principal outcomes of the IDB Country Strategy with Peru 2012-2016

- 2.5 **Social inclusion.** In social protection and early childhood development, the fundamental challenge for Peru was to improve the operation and coordination of social programs. The Ministry of Development and Social Inclusion (MIDIS) was created in 2011 with this challenge in mind. The Bank provided technical support for an evaluation of social programs, leading to greater coverage of the programs

⁷ See Annex IV. Data as of 31 December 2016.

⁸ The outstanding portfolio comprises operations that have gone been approved by the Bank's Board of Executive Directors and have not yet achieved operational closing, i.e., the final operational financial audit report has not been approved in accordance with the Bank's fiduciary manuals.

⁹ The outstanding portfolio is primarily comprised of operations with an execution life of less than 2.5 years and disbursements of less than 50%. These operations account for 69% of the portfolio in terms of approved amount, compared with 29% for the Andean Community, 13% for Ecuador, and 33% for Bolivia. In addition, the outstanding portfolio includes significant projects in terms of amount and complexity of execution, such as the Lima metro. The average age of the entire portfolio is 3.5 years.

JUNTOS and Cuna Más [Cradle Plus] (in the country's 600 poorest districts) and an improvement in their effectiveness and efficiency.¹⁰ An impact assessment of the Programa Nacional Cuna Más [Cuna Más National Program]¹¹ (PNCM) verified positive impacts on cognitive and noncognitive abilities in the children served by the program. Similarly, operational assessments of JUNTOS were supported along with various aspects of the social programs, such as quality management, monitoring, communications, training of officials, preparation of diagnostics, and piloting of strategies for graduation from JUNTOS and for financial inclusion among beneficiaries of MIDIS programs. With a view to expanding the use of maternal and child health services and reducing child morbidity rates among children under three years of age in rural areas in the country's nine poorest regions,¹² the Bank is working on improving the availability of public health services.¹³ The quality of early childhood education in vulnerable regions was strengthened, with 33 early education centers, 265 trained teachers, and 406 centers with renewed teaching materials in the departments of Ayacucho, Huancavelica, and Huánuco, in predominantly indigenous areas.¹⁴ While the World Bank has been supporting the country in terms of education, the IDB helped the sector authorities to move forward on a teacher evaluation agenda, defining the evaluation instruments (OVE, document RE-498).¹⁵ Peru was the Bank's first borrowing member country to use the fee-for-service system of technical assistance for the evaluation design of and invitation to the BECA18 program. Through the private sector windows, the IDB Group supported: (i) the Innova Schools at the national level, expanding coverage from 2,200 students to 18,535;¹⁶ and (ii) Universidad San Ignacio de Loyola.¹⁷

- 2.6 As part of the Programa Nacional contra la Violencia Familiar y Sexual [National Program against Domestic and Sexual Violence] (PNCVFS), the Bank supported the Ministry for Women and Vulnerable Population Groups in fine-tuning and expanding the Centros Emergencia Mujer [Women's Emergency Centers] (CEM), with a view to expanding the services provided to women, adolescents, and family groups under a coordinated, preventive, and intercultural approach. The MIF

¹⁰ The Bank supported the JUNTOS conditional cash transfer program through a communication strategy, a new operating manual, and a baseline for impact assessment. Progress was also made in consolidating the information in the Direcciones Regionales [regional offices] and other education-, health-, and development and social inclusion-related agencies with a view to verifying the fulfillment of responsibilities. In addition, the methodology for budget formulation and operation of the Sistema Integral de Salud [Comprehensive Health Care System] (SIS) was significantly strengthened. The job programs Construyendo Perú [Building Peru] and Jóvenes a la Obra [Youth Getting to Work] were evaluated, and the operating rules of the latter program and Trabajo en Perú [Work in Peru] were improved. Lastly, the program strengthened the Sistema de Focalización de Hogares [Household Targeting System] (SIFOH) and progressively succeeded in ensuring that social programs use the general registry of households to target their actions (PE-L1072, PE-L1078, PE-L1100, and PE-L1105).

¹¹ The Programa Nacional de Apoyo Directo a los más Pobres (National Program in Support of the Poorest Population) [JUNTOS] and the Programa Nacional Cuna Más (Cuna Más [Cradle Plus] National Program) [CUNA MÁS].

¹² PE-L1005: Second Phase of the Program to Support Health Sector Reform—PARSALUD II.

¹³ PE-L1169: Management Modernization for Universal Health Coverage Program I.

¹⁴ PE-L1062: Program to Improve Early Education in Ayacucho, Huancavelica, and Huánuco.

¹⁵ PE-T1303: Support for Teaching Career Reform.

¹⁶ PE-L1120: Colegios Peruanos: Access to Quality Private Education for Emerging Social Classes in Peru.

¹⁷ PE-L1141: Universidad San Ignacio de Loyola Expansion Project (SCF).

organized workshops and training sessions aimed at calling attention to and raising awareness of gender-based violence in the rural areas of Huancavelica and Ayacucho. These were supplemented by a microcredit access program for more than 1,000 women and 145 female community leaders. The MIF trained more than 1,100 women microentrepreneurs in the Lima metropolitan area and in Arequipa in the areas of marketing, leadership, and financial management. Support for Laboratoria has empowered more than 400 low-income or vulnerable young women by providing them access to education and work in the digital sector, enabling them to increase their income and find gainful and sustainable employment.

- 2.7 **Rural development, agriculture, climate change, and natural disaster risk management.** Agricultural productivity was improved through the Agricultural Health and Agrifood Safety Development Program,¹⁸ eradicating infestations in more than 719,000 hectares of farmland.¹⁹ In addition, the country strategy succeeded in promoting alliance-building, business management, and the adoption of agricultural technologies among more than 16,600 farmers. Creating the Sistema de Información para la Gestión del Riesgo de Desastres [Disaster Risk Management Information System] (SIGRID) and building prevention and response capacity led to an improvement in the index of governance and public policy in disaster risk management from 31.1% in 2008 to 51.8% in 2014.²⁰
- 2.8 The capacity for climate change mitigation and adaptation, and the role of the Ministry of Environment as the governing body, were strengthened through the Program to Support the Climate Change Agenda, which helped to foster: (i) enactment of a new forest and wildlife legislation for Peru; (ii) approval of the Forest Investment Program (FIP); (iii) financing of an adaptation project in the fishing sector using Adaptation Fund resources; and (iv) approval of specific climate adaptation strategies by three regional governments.
- 2.9 In addition, the Bank supported a dialogue between Norway and Peru aimed at creating a fund of up to US\$300 million to counteract deforestation.²¹ Through the private sector windows, the Bank facilitated access to financing for 10,000 farmers from rural agricultural cooperatives (ABACO)²² and the creation of 14,500 jobs in the agroindustry sector (DANPER).²³
- 2.10 **Water, sanitation, water resources, and solid waste.** The Bank supported the Government of Peru in consolidating the country's institutional and legal framework and promoting integrated management of water resources through a participatory sustainability- and equity-based approach. This support, through programmatic

¹⁸ PE-L1023: Agricultural Health and Agrifood Safety Development Program.

¹⁹ Thirty-five quarantine control stations were built and more than 436,000 hectares are surveyed for plant health.

²⁰ PE-L1138: Programmatic policy-based loan, Program to Reduce the Vulnerability of the State to Disasters III.

²¹ In the area of climate change, international resources from the Forest Carbon Partnership Facility (FCPF) and the Global Environment Fund (GEF) were mobilized for the Forest Investment Program (FIP) to drive the agenda for reducing greenhouse gas emissions with a view to counteracting deforestation (Government of Norway).

²² PE-L1158: ABACO: Access to Financing for Small Producers Organized in Value Chains in Peru; PE-L1179: Cooperative Model for Rural Financial Innovation.

²³ PE-L1143: Danper Trujillo S.A.C.

policy-based loans (PBP) and various technical cooperation operations, was supplemented by the implementation of integrated management systems in three priority watersheds in the coastal region. The Water Resource Management Modernization Program²⁴ provided 1,461 water rights licenses for agricultural and non-agricultural use and installed 50 hydrometeorological stations and 6 water quality monitoring stations, resulting in the approval of the management plans by the National Water Authority (ANA) and the signing of local conflict resolution agreements.

- 2.11 Access to water and sanitation services in rural areas—in the departments of Puno, Cusco, Apurímac, Huancavelica, and Ayacucho,²⁵ where the beneficiary population is predominantly indigenous—was expanded and improved with support from the Government of Spain’s Water and Sanitation Fund, increasing drinking water coverage from 31.7% to 33.6% and sanitation coverage from 13.0% to 14.8%.
- 2.12 MIF support to the nongovernmental organization Agualimpia made it possible to promote financial products designed to improve access to water and sewer services for low-income residents of periurban communities. As a result, 10,186 households in periurban areas (Lima, Arequipa, and Callao) have obtained access to microcredit to upgrade sanitation services in their homes; 6,827 households have adopted proper sanitation practices; and three microfinance institutions have joined the program and offer suitable products for sanitation improvements in periurban areas.
- 2.13 **Energy.** Construction and operation of the Chaglla hydroelectric power plant, with 406 megawatts of installed capacity, financed through the private sector window, has helped to create jobs (2,500 direct jobs and 10,000 indirect jobs) and reduce emissions by approximately 467,000 tons of carbon dioxide. The Program for Sustainable and Efficient Management of Energy Resources in Peru (PROSEMER²⁶), supported by the Government of Canada, is contributing to public and regulatory governance as well as to energy sector planning.
- 2.14 The MIF supported the nongovernmental organization Acciona Microenergía Perú in creating an electricity concession through the first social entrepreneurship system that provides electric energy to isolated communities, benefiting more than 1,700 families in rural communities of the Cajamarca region.
- 2.15 **Transportation.** IDB Group interventions in the transportation sector were intended to improve the country’s connectivity and competitiveness. The Bank has supported the country’s work on major highways and departmental and rural roads. Through the National Highway System Serviceability Improvement Program,²⁷ the Bank has financed rehabilitation of 355 km, improvement of 106 km, and maintenance of 1,644 km of the country’s national highway system, improving the level of service and raising the average daily index (ADI).

²⁴ PE-L1070: Water Resource Management Modernization Program.

²⁵ GRT/WS-12127: Water and Sanitation Improvement Program.

²⁶ PE-X1007: Program for Sustainable and Efficient Management of Energy Resources in Peru (PROSEMER).

²⁷ PE-L1006: National Highway System Serviceability Improvement Program.

- 2.16 With regard to departmental²⁸ and rural²⁹ transportation: (i) 1,341 km of unpaved surface roads and 3,277 km of rural roads were rehabilitated; (ii) financing was provided for periodic maintenance of 3,661 km of departmental roads and 7,811 km of rural roads; (iii) 17,475 km underwent routine maintenance and 2,450 km were improved; and (iv) 25 regional governments were supported through preinvestment studies for more than 9,500 km. These interventions at the departmental and rural levels have led to a 20% reduction in travel time, a 5% increase in traffic volume, and a 2% average reduction in passenger and freight rates over 5,139 km of roads.
- 2.17 Lastly, synergy between the public and private sectors was a determining factor for the development and approval of Line 2 of the Lima Metro, which is projected to transport 660,000 passengers daily by 2020. This project is expected to reduce travel times, vehicle operating costs, and greenhouse gas emissions while increasing the number of passengers using the system, among other outcomes. The project has US\$750 million in financing: a sovereign-guaranteed loan of US\$300 million³⁰ and a non-sovereign guaranteed loan of US\$450 million.³¹
- 2.18 **Strengthening of public management.** In this area, the Bank has helped to enhance transparency and accountability, build public investment capacity in regional governments, and modernize State financial and budgetary management.
- 2.19 The Bank has supported the Office of the Comptroller General of Peru (CGR)³² in improving decentralized work, thus making it possible to increase public spending control at the subnational level, with an emphasis on prevention and management improvement. The number of control actions exceeded the baseline by 106% and the project target by 38%. Additional actions included developing audit tools (e-quipu) and management tools (management information system); creating a data center; improving the physical infrastructure of the CGR and upgrading the equipment in the regional offices of Piura, Arequipa, Tacna, and Cuzco; the security and accessibility of regional information has been enhanced through digitalization of documents; and a standardized methodology for financial audits was implemented.
- 2.20 In the area of fiscal and municipal management, the Bank supported the strengthening of public finance management by modernizing the Sistema Integrado de Administración Financiera [Integrated Financial Management System] (SIAF II).³³ Through the Improvement of Territorial Public Investment Management project, the 12 regional governments have consolidated their capacities for public investment planning and execution.³⁴
- 2.21 **Competitiveness and innovation.** The IDB Group has helped to improve Peru's competitiveness and innovation through the strengthening of 20 research and

²⁸ PE0236: Departmental Roads Program.

²⁹ PE-L1011: Decentralized Rural Transportation Program.

³⁰ PE-L1147: Construction of Line 2 and the Avenida Faucett-Gambetta Section of the Lima and Callao Metro Basic Network (sovereign-guaranteed).

³¹ PE-L1160: Lima Metro Line 2 and Line 4 (non-sovereign guaranteed).

³² PE-L1132: Improving the National Control System for Effective Public Management and Integrity.

³³ PE-L1087: Modernization of the Public Finance Administration System to Improve Public Resource Programming, Execution, and Reporting.

³⁴ PE-L1101: Improvement of Territorial Public Investment Management.

innovation laboratories with a view to their technical accreditation, 245 contracts for advanced research projects, and 62 assimilation of technology projects.³⁵

- 2.22 The reforms promoted by the Bank fostered improvements in: (i) the business environment,³⁶ and (ii) institutions and instruments for competitiveness.³⁷ The activities carried out led to a simplification of administrative procedures for starting a business,³⁸ registering property,³⁹ and obtaining construction permits,⁴⁰ as well as reducing logistics costs for international trade⁴¹ and improving the system for recording security interests to make access to credit easier for small-scale entrepreneurs.⁴² At the institutional level, the Consejo Nacional de Competitividad [National Competitiveness Council] (CNC) and the institutional framework of the national quality control system were strengthened (by creating the Instituto Nacional de la Calidad [National Quality Institute] (INACAL) or financing laboratories to ensure quality, metrology, and other standards), advances were made on reforming the model of the Centros de Innovación Tecnológicos [technological innovation centers] (CITES), and the Instituto Tecnológico de la Producción [Production Technology Institute] (ITP) was created to coordinate the CITES network.
- 2.23 The IIC supported sustainable tourism through the innovative project Mountain Lodge Peru, which is benefiting campesino communities located near a new cultural route to Machu Picchu. In the financial sector, technical assistance to the Caja de Arequipa to improve its corporate governance has allowed this savings association to launch negotiations aimed at bringing foreign institutions into its shareholding structure. IIC interventions have helped to expand access to credit for the small and medium-sized enterprise (SME) segment to cover (i) 1,000 SMEs operating as suppliers for medium-sized and large corporate clients of Banco Santander Peru through its Confirming program; (ii) 1,200 micro, small, and medium-sized enterprises (MSMEs) through Financiera Confianza for production loans; and (iii) 27,000 MSMEs in the south central region of Peru through Compartamos Financiera.
- 2.24 **Lessons learned.** The main lessons learned in implementing this strategy include: (i) focus interventions on sectors/issues in which the IDB Group has greater value

³⁵ PE-L1068: Innovation Project for Competitiveness.

³⁶ By reducing the administrative costs of registering a new business and operating a business, customs formalities, and recording security interests.

³⁷ Including improvement in quality standards, public expenditure on research and development, statistical systems for economic surveys.

³⁸ The number of procedures was reduced from 9 to 6, and the number of days to obtain an operating license was reduced from 41 days to 26 days. In addition, adoption of the provisions of the framework law on operating licenses was promoted in 207 municipios.

³⁹ The number of days for registering the purchase of a real estate property was reduced from 14 days to 6.5 days.

⁴⁰ The number of procedures was reduced from 21 to 14, the number of days for obtaining a construction permit was reduced from 215 days to 174 days, and the adoption of simplified procedures was promoted in 47 municipios.

⁴¹ The time associated with an export transaction was reduced from 21 to 17 days, the time associated with an import transaction was reduced from 24 to 17 days, and exports through the UAC-OAS program increased by 4.9% as a percentage of total exports.

⁴² Net registration of security interests increased by 30%, and public investment in research and development (R&D) increased by 0.03% as a percentage of GDP.

added so as to maximize their impact and minimize the transaction costs of preparing and executing the interventions (for example, during the preceding country strategy period, the Bank's interventions were fragmented into 24 investment operations in amounts of approximately US\$30 million on average);⁴³ (ii) move forward on the high-level government dialogue (MEF-PCM) with a view to strengthening the strategic planning capacity, execution of operations, and quality of public investment; (iii) in the context of the Bank's declining financial competitiveness in Peru, develop a strategy to position and enhance its visibility as technical leader in sectors in which the Bank has comparative advantages; and (iv) explore supporting subnational governments, which at present show weaknesses in executing investment projects, discouraging the prioritization of multilateral financing for these governments. From the standpoint of non-sovereign guaranteed operations, the lessons learned are: (i) in working with financial intermediaries, the IIC should select solid institutions with relevant experience in the target sectors in order to ensure fulfillment of the planned objectives; and (ii) the opportunities to support innovative projects should include technical assistance, so as to maximize the IIC's value added and achieve the desired impact.

III. PRIORITY AREAS⁴⁴

- 3.1 **The IDB Group Country Strategy with Peru 2017-2021.** Based on the lessons learned in the preceding strategy period, OVE's recommendations, the country's development challenges identified in the Country Development Challenges (CDC) document, and the dialogue with the government, the objective of the country strategy 2017-2021 is to support Peru in achieving sustained growth so as to foster social advances in a context of environmental sustainability.⁴⁵ To this end, the IDB Group proposes prioritizing three areas: (1) productivity, with an emphasis on the labor market, business climate, business development, and infrastructure; (2) institutional strengthening and basic service delivery, with an emphasis on public management, health, and citizen security; and (3) environmental sustainability and climate change, with an emphasis on water resources, environmental management, and agribusiness. The intervention sectors will be served by the existing portfolio, knowledge products, technical cooperation operations, and new loan and guarantee operations. The complementary use of these instruments will make it possible to address the priority areas on a consistent and coordinated basis between the IDB, the IIC, and the MIF, taking advantage of synergies among the interventions.
- 3.2 The actions envisaged in this strategy are aligned with the Peruvian government plan.⁴⁶ To boost and formalize the economy, the Government of Peru has planned initiatives such as: (i) unblocking large projects; (ii) adopting measures to formalize and reduce the tax burden; (iii) simplifying tax administration; (iv) creating unemployment insurance; (v) delineating job promotion programs; and (vi) restructuring the Consejo Nacional de Competitividad y Formalización [National

⁴³ This average does not include the Lima Metro operation for US\$300 million.

⁴⁴ All references are found in the CDC (Annex I), along with a detailed analysis of the development challenges addressed in this document.

⁴⁵ In this context, the IDB Group will continue to support regional integration processes.

⁴⁶ The government's plan and the proposed public policies are aligned with the United Nations Sustainable Development Goals. For more details, see the electronic links.

Competitiveness and Formalization Council]. To improve public management, the government proposes: (i) reforming the State investment system; (ii) improving services to the public and businesses (by simplifying procedures); (iii) strengthening the integrity and transparency framework; and (iv) automating processes through information technologies (electronic government). Improving the quality of health services requires: (i) strengthening primary care; (ii) implementing and managing primary care-based integrated service networks; and (iii) developing pay scales that encourage meritocracy and productivity. In the citizen security area, the government aims to: (i) improve the working conditions of the National Police and the crime detection system; and (ii) define national citizen security policies in coordination with the various levels of government. To expand water and sanitation coverage, the government plan seeks to increase financing for the sector and consolidate management of the service providers. To strengthen environmental management, the government plans to prioritize natural resource protection and environmental quality improvement.

A. Productivity⁴⁷

- 3.3 Productivity lags behind that of the United States⁴⁸ and is at similar levels (40% of United States productivity levels) to those of the early 1970s.⁴⁹ The gap is also significant in terms of productivity per worker, which is estimated at 23% of the U.S. figure and is below the regional average of 25% (Conference Board, 2016).
- 3.4 The low productivity of the Peruvian economy is a result of the allocation of resources among companies and the production performance of these companies. The literature shows how market failures and public policies can determine the selection of companies in the market and the allocation of resources among them.⁵⁰ The characteristics of the labor market and the workforce, the availability of infrastructure, and the business climate are the most significant factors at the aggregate level that determine an efficient allocation of resources in the economy.⁵¹ In addition, propensity to innovate and access to capital markets determine the productivity of production units and are closely related to demographics and company size.⁵²
- 3.5 In Peru, productive resources are not efficiently allocated to maximize economic productivity. Interaction between the employment and tax systems and the social

⁴⁷ The actions planned in this area are aligned with United Nations Sustainable Development Goals 7 (affordable and clean energy); 8 (decent work); 9 (industry, innovation, and infrastructure); and 10 (reduced inequalities).

⁴⁸ World Bank, (2015), Peru - Building on success: boosting productivity for faster growth.

⁴⁹ Penn Tables.

⁵⁰ Restuccia and Rogerson (2008), Hsieh and Klenow (2009), Syverson (2011), and Bartelsman et al. (2013).

⁵¹ Syverson, C. (2011), What Determines Productivity? *Journal of Economic Literature* 49(2), 326–365.

⁵² According to Prescott (1998) and Parente and Prescott (1999), the differences in productivity between countries are due to a failure to adopt new technologies and inefficient use of current technologies. For Cole et al. (2005), Latin America has not grown as much as other economies because of low productivity due to barriers to competition. Hsieh and Klenow (2009) attribute the differences in productivity to a poor allocation of resources. Lastly, the investment climate (defined as regulations, corruption, crime, quality and availability of energy and transportation infrastructure, communications, and access to financing) can significantly affect productivity, employment, and growth (Djankov et al., 2002, Rodrik and Subramanian, 2004; Aterido et al., 2011; Escribano and Guasch, 2012).

insurance architecture creates discontinuities in the earnings function of businesses and perverse incentives in the behavior of businesses and workers.⁵³ The result is a fragmentation of economic activity into many small and unproductive businesses, along with a high level of self-employment and informality.

- 3.6 **Labor market.** Peru has one of the highest rates of informal employment in the region: 78% (2015) as compared to the regional average of 55%.^{54,55} Based on its income level, Peru should have 30% to 40% of its workers in formal jobs, rather than the current 22% (SIMS, 2015). Informality is coupled with high employment turnover. Thirty-five percent of workers in Peru have been at their jobs for less than one year, the highest percentage for any country in the region other than Colombia (Alaimo et al., 2015). These labor market characteristics have consequences for social insurance and only 22% of workers contribute to pensions, compared to the regional average of 45% (Alaimo et al., 2015; Palomino, 2015).
- 3.7 Informality and job turnover are due to the excessive costs of formalization (Alaimo et al., 2015). Peru has one of the highest formalization costs in the region, together with Guatemala, Bolivia, Paraguay, Nicaragua, and Honduras. Non-wage costs account for 55% of total labor costs, 12 percentage points higher than the regional average. Non-wage costs notably include separation-related costs, which are equivalent to 13% of annual wages and are the highest in the region (Alaimo et al., 2015).
- 3.8 The skills gap fuels informality.⁵⁶ Seventy percent of formal Peruvian businesses find it difficult to fill vacancies. This figure is higher than the world average of 36% and the figure for companies in other countries in the region.⁵⁷ Two of every three businesses experience problems in hiring skilled labor.⁵⁸
- 3.9 These results are due to gaps in basic education and a job training system that fails to address educational shortcomings. The results of the 2015 Program for International Student Evaluation (PISA) test⁵⁹ show an improvement in the quality of education, Peru being the Latin American and Caribbean country that has made the greatest strides with respect to the 2012 measurements. However, the gaps with respect to the OECD countries are considerable.⁶⁰ The job training system is not helping to improve this situation⁶¹ and fails to coordinate vocational education, higher

⁵³ Levy, S. (2016), http://www.grade.org.pe/wp-content/uploads/Levy_inaugural.pdf.

⁵⁴ Informality affects different socioeconomic groups differently. It is greater among young workers (88%), women (76.6%, compared to 70% among men), and less-educated workers (95.8%). Informality among indigenous peoples and Afrodescendants is close to the national average (SIMS). There are geographic differences: metropolitan Lima has a 58.7% informality rate, compared to 80.5% in the rest of the country; the informality rate is 95.4% in rural areas and 66.5% in urban areas. The coastal region has a lower informality rate (65.1%) than both the highlands (83.4%) and the jungle (84.6%) regions (INEI, 2015).

⁵⁵ Informality is intimately related to low productivity of businesses and workers. In the region, countries with higher productivity levels tend to have lower informality for the same formality cost (Alaimo et al., 2015).

⁵⁶ Chacaltana et al. (2015).

⁵⁷ Manpower Group (2015) Talent Shortage Survey.

⁵⁸ Apoyo (2013). Four measures to address the scarcity of skilled labor. Policy Proposal.

⁵⁹ Of the 69 countries evaluated, Peru placed 61st in mathematics, 62nd in reading, and 63rd in science.

⁶⁰ It has been estimated that, at the pace of progress shown between 2012 and 2015, Peru would reach the OECD average in 21 years.

⁶¹ Chacaltana et al. (2015).

education, and job training. This is due to: (i) weak governance, leading the system's actors (i.e., education and labor ministries) to independently regulate the components assigned to each, creating duplication;⁶² (ii) limited quality assurance mechanisms and limited productive sector involvement;⁶³ (iii) limited and inadequate labor and vocational information; and (iv) insufficient public financing (Peru invests 0.1% of GDP as compared to an average of 0.2% for the region and 0.6% for OECD countries).⁶⁴

- 3.10 To foster productivity, formality, and social insurance while addressing gender and ethnicity gaps, the Bank will support the country in defining and implementing its informality reduction strategy, examining, among other measures, the opportunity to reduce non-wage labor costs and strengthen the job training system and its relationship with the education system. In addition, the Bank will support the Comisión de Protección Social [Social Protection Commission], created by the Government of Peru to examine reform opportunities in the areas of pensions, health sector financing, and unemployment insurance.
- 3.11 **Business development.** The Peruvian business landscape is dominated by MSMEs, which account for 99% of all businesses and employ 60% of the economically active population. In the rest of Latin America, MSMEs employ 30% to 40% of the population (ILO, 2015). Roughly 56% of Peruvian MSMEs are informal. Forty percent of individuals who start a business⁶⁵ are women, generally microentrepreneurs.⁶⁶ The productivity of microenterprises is 3% of that of large enterprises, and the productivity of small enterprises is 49% of that of large enterprises (SUNAT, 2014). While the literature shows a positive relationship between economic growth and number of businesses,⁶⁷ not all businesses make similar contributions. In Latin America, SMEs account for 30% of GDP, while in OECD countries they account for 60% of GDP (OECD, 2015a). Peruvian SMEs are predominantly young: 60% of them have been in the market for 5 years. The rate of creation of new enterprises (2 for every 1,000 working-age individuals) is lower than the rate in OECD countries (4.5 for every 1,000 working-age individuals) (IDB, 2014a), and growth expectations for new enterprises are limited, with minor differences across sectors. According to data from SUNAT, the majority of businesses created in Peru since 2009 are microenterprises (96.8%). Furthermore, both micro and small enterprises record hardly any discernable sales growth in their first five years in operation, with 44% of microenterprises and 20% of small enterprises going out of business during this period.

⁶² Escárate (2012).

⁶³ Chacaltana et al. (2015).

⁶⁴ Alaimo et al. (2015).

⁶⁵ PRODUCE (2015). On an annual average, entrepreneurs account for 21% of the employed economically active population (EAP). This is equivalent to an average of 3 million individuals per year.

⁶⁶ PRODUCE (2015). In general, women become entrepreneurs at an earlier age than men. Thirty-five percent of men attend university, as compared to 63% of women. Women have a limited presence in the agricultural sector (26% vs. 66% in the case of men).

⁶⁷ Kantis et al. (2002).

- 3.12 The growth of micro, small, and medium-sized enterprises is restricted by access to credit⁶⁸ and a limited propensity to innovate.^{69,70} Financial depth indicators show a credit/GDP ratio of 40%, below the regional average of 41%.⁷¹ Credit to SMEs as a percentage of total credit is 4.5%, compared to 12.4% for the region.⁷² In addition to the size of the business, credit is highly concentrated by economic sector and geographic area: 70% is provided to commerce and services, and 73% to Lima businesses. Restrictions on access are greater for women. For example, only 4% of women agricultural producers have access to credit as compared to 8% of men, this being one of the lowest percentages in the region (INEI, 2015 and FAO⁷³). The factors accounting for this low rate of access to financing include: (i) the productive structure of the enterprise; (ii) the institutional and regulatory environment; (iii) the degree of certainty and information asymmetries; and (iv) transaction and scale costs.⁷⁴
- 3.13 Incipient innovative efforts constrain the productivity of production units.⁷⁵ The lack of innovation is a result of: (i) low levels of investment in research and development (total investment in R&D is equivalent to 0.16% of GDP as compared to a regional average of 0.32%, and the private sector's contribution is a mere 6% of this investment total as compared to a Latin American average of 21%);⁷⁶ (ii) a lack of skilled human capital (the proportion of researchers per 1,000 members of the workforce (0.4%) is one third of the average in the region (1.11%) and a fraction of

⁶⁸ The literature acknowledges the importance of financial considerations for investment decisions and the impact of frictions in obtaining access to external financing sources on the capacity of businesses to take advantage of productive investments opportunities. The positive impact of credit on innovation, research and development, market access, and access to higher value added business segments has been extensively documented and is significant for small enterprises (Aghion et al., 2010; Beck et al., 2006a; Beck et al., 2006b; Manova and Yu, 2012; Gatti and Love, 2008; Chen and Guariglia, 2013; Butler and Cornaggia, 2011; Ferrando and Ruggieri, 2015; Aghion, 2007; Bloom et al., 2010; Pagés, 2010). The literature identifies positive impacts on: (i) economic growth (Beck et al., 2008; Rajan and Zingales, 1998), it being one of the most important variables for economic convergence (Aghion et al., 2005) (ii) allocation of the capital factor to projects with higher returns (Galindo et al., 2007); and (iii) total factor productivity, mitigating the impact of volatility and macroeconomic shocks (Cavallo et al., 2013; Aghion et al., 2005).

⁶⁹ There is a general theoretical consensus on the positive relationship between research and development (R&D), innovation, and productivity at the business level (Griffith et al., 2003; Mairesse and Mohnen, 2010). Recent studies for Latin America (IDB, 2015a; Grazi et al., 2016) point to a positive relationship between inputs and innovation outcomes and between innovation outcomes and productivity. Returns on innovation depend on the type of innovation and are greater for products than for processes. In addition, returns on innovation are greater for more productive enterprises.

⁷⁰ Beck et al., 2008; Cavallo et al., 2010; Ibarraran et al., 2010; Mateev et al., 2013.

⁷¹ Word Development Indicators.

⁷² OECD (2012) Latin American Economic Outlook 2013.

⁷³ <http://www.fao.org/3/a-as107s.pdf>. In Brazil and Chile, 13% of women have access to credit.

⁷⁴ IDB (2014) Support to SMEs and Financial Access/Supervision Sector Framework Document. A productive structure such as Peru's, with its strong presence of micro and small enterprises and its bias toward informality, involves uncertainty and higher transaction costs, leading to a suboptimal provision of credit. The information asymmetries are more pronounced for smaller businesses due to their difficulty in generating adequate and accurate information—i.e., audited financial statements—needed by financial institutions to assess credit risk (de la Torre et al., 2009).

⁷⁵ Pagés (2010): La era de la productividad: Transformando economías desde sus cimientos [The productivity era: Transforming economies from the ground up].

⁷⁶ RICYT and OECD, 2011. OECD Reviews of Innovation Policy: Peru.

the average in OECD countries (7.18%);⁷⁷ and (iii) the complexity of the national innovation system.⁷⁸

- 3.14 To improve access to credit for MSMEs, the IDB Group will support: (i) deepening the capital markets, particularly the debt market,⁷⁹ through mechanisms aimed at encouraging SMEs to participate as issuers, expanding the universe of institutional investors to include those with a greater risk appetite, and implementing risk mitigation mechanisms for certain fixed income issues; (ii) greater access to credit through financial intermediaries, particularly in still underserved rural areas and in urban areas that need broader microcredit coverage; and (iii) access to financing for value chains and support for foreign trade through the Trade Finance Facilitation Program (TFFP). To strengthen the innovative effort of enterprises, the IDB Group will prioritize greater and better delivery of public goods, specifically through institutional strengthening of the innovation system, innovation financing, technology transfer and entrepreneurship, and advanced human capital. These interventions will seek to support women entrepreneurs.
- 3.15 **Business climate.** The business climate affects both the allocation of resources and business productivity, generating incentives for businesses to invest, grow, and create jobs.⁸⁰ The private sector has played a central role in closing investment gaps in Peru.⁸¹ In 2015, private investment was three times greater than public investment as a percentage of GDP (19.9% for private investment and 5.8% for public investment, Central Reserve Bank of Peru (BCRP), 2016), this being a larger proportion than in most of the countries in the region and in OECD countries.⁸² PPPs have favored the channeling of private investment. Between 2006 and 2014, annual investment through PPPs went from US\$900 million to US\$14 billion, and was channeled into projects totaling US\$30 billion.⁸³ However, between 2011 and 2016,

⁷⁷ RICYT, 2015.

⁷⁸ According to the Encuesta Nacional de Innovación en la Industria Manufacturera [National Survey on Innovation in the Manufacturing Industry] (ENIM 2012), close to half of enterprises in Peru work with internal sources of information and only 30% of large companies and 18% of small enterprises have any links to universities or technology institutes. Of these collaboration efforts, only 3.6% in the case of large companies and 2.6% in the case of small enterprises are associated with technological innovation and development projects. This limits the relevance of the applied research produced by the technology institutes and universities to the production needs of the enterprises. Coordination among companies is also limited. According to the ENIM, while 57% of enterprises report links with other companies, just 7% are for the purpose of R&D projects.

⁷⁹ Despite its growing importance in private sector financing, the debt market has been concentrated on bond issues by large companies with the best credit ratings, reflecting the conservative profile of institutional investors in Peru (particularly pension funds (AFPs)).

⁸⁰ The business climate has a significant effect on the productivity (Escribano and Guasch, 2012) and growth of businesses (Aterido et al., 2011).

⁸¹ In the 1990s, the Peruvian government introduced a series of regulations to drive and encourage private investment in public service infrastructure through concession-based projects. The first Framework Law on Public-Private Partnerships was enacted in 2008 as a means of expanding investment and closing the existing gaps at the national level.

⁸² WEO, IMF.

⁸³ Thirty percent of investments committed in the form of PPPs are in the electricity sector, with an estimated aggregate investment amount of US\$8 billion, and are aimed at expanding the country's electric power generation capacity by 3,600 megawatts and expanding transmission lines by 6,281 km. As a result of private-sector participation, 27% of the entire national highway system—6,851 km of roads—is under concession through 16 contracts.

- private investment has exhibited declining rates of growth, averaging 5% (about half the growth rate in the first decade of the century (9.5%) and then turning negative since 2014 (BCRP, 2016).
- 3.16 This decline is the result of a deterioration in the ease of doing business index and governance indicators. In 2016, Peru was ranked 50th among the 189 countries assessed by the World Bank's Doing Business Report, five positions lower than in the previous year. Peru has fallen behind in terms of ease of starting a business (-3.13 percentage points), registering property (-0.01 percentage points), and getting electricity (-3.13 percentage points). The most significant gaps with respect to high-income OECD countries are in: (i) ease of starting a business (97th place), where the costs and time required in Peru are three times higher than the OECD average; and (ii) getting electricity (64th place), where the costs and reliability of service, although better than in the rest of the region, fail to match those in more advanced countries.⁸⁴ In the area of policy implementation, worth noting are the challenges of implementing the new PPP law,⁸⁵ which has been in effect since late 2015, in terms of strategic planning and prioritization of public investment and risk management and allocation (McKinsey, 2013, Infrastructure UK, 2011).
- 3.17 To foster private-sector participation, the Bank will continue to support: (i) improving the business climate through lower business creation costs and administrative simplification; and (ii) consolidating the capacities of public institutions to implement the new regulatory framework for PPPs and boost public investment. This will facilitate PPP planning and structuring and consequently make it easier to generate bankable projects that are attractive for private-sector participation. In this area, the IDB Group will provide advice on implementing best practices that ensure the bankability of PPP projects.
- 3.18 **Infrastructure.** The availability and quality of infrastructure contribute to business productivity (Escribano and Guasch, 2012), create complementarities with private capital, and promote economic growth (Cockburn et al., 2013).⁸⁶ The literature recognizes a positive relationship between investment in transportation infrastructure, productivity, and economic growth (Calderón and Servén, 2010). In Peru, productivity is circumscribed by the provision of quality infrastructure, particularly road and energy infrastructure, and the digital divide.
- 3.19 *Transportation.* The length of the country's road network doubled between 2000 and 2012, from 78,000 km to 140,000 km. The departmental network (17% of the total) and the rural network (65% of the total) expanded by 70%-85%. In 2012, 13% of all roads had been paved, with large differences by jurisdiction (59% of the national

⁸⁴ World Bank (2015), World Bank's Doing Business Report.

⁸⁵ The PPP regulatory framework was modified through Legislative Decree 1224 of September 2015, and then again through Legislative Decree 1251 of 30 November 2016 under the present government administration, with a view to streamlining processes, improving the quality of projects, and strengthening PROINVERSION through a restructuring and decentralization process. The implementing regulations for the new provisions are expected to be in place in the first quarter of 2017.

⁸⁶ The infrastructure stock and its quality have a positive impact on growth and on reducing inequality and poverty (Bonifaz and Urrunaga, 2013; Chong and Calderón, 2001; Escobal, Saavedra, and Torero, 1999). Cockburn et al. (2013) consider the direct effect of infrastructure on productivity. Other studies on the effect of infrastructure on growth include Barro (1991), Rivas (2003), Fisher and Turnovsky (1998), Yakita (2004), Agenor and Moreno-Dodson (2006), Ohdoi (2007), and Park and Philippopoulos (2002).

network, 10% of the departmental network, and 2% of the rural network).⁸⁷ These levels are lower than the regional average of 27%.⁸⁸ Eighty-three percent of the Red Vial Nacional [National Road Network] (RVN) is in good condition, compared to 15% of the departmental road network and 7% of the rural network.⁸⁹ Transportation flows have grown faster than has coverage, creating capacity and quality problems. Road density indicators, which measure the number of kilometers (km) per 100 km² of territory, identify Peru as a low-density country, with 12% density as compared to the regional average of 17%.⁹⁰ According to the World Economic Forum, Peru is ranked 111th in a sample of 140 countries in terms of road quality, with a quality level that is half that of Chile's. The evolution of this indicator reveals a decline in quality between 2012 (score of 3.6 out of 7) and 2015 (3.2 out of 7).⁹¹

- 3.20 At the same time, urban public transportation is inefficient. This problem is particularly significant in the city of Lima, where most travel takes place. Thus, while 65% of trips (of a daily total of approximately 17 million) are completed using public transportation (buses, minibuses, vans), only 5% are completed using public mass transport (metropolitan transportation and Line 1 of the metro). In addition, the traditional bus system predominantly relies on vans,⁹² which are small units that cover excessively long routes, make frequent stops, and in many cases have a useful life of 10 years. This system results in higher CO₂ emissions and greater congestion problems than integrated multimodal systems where the use of mass transport is more prevalent.
- 3.21 The sector's main challenges have to do with the difficulties of closing the investment gap and curing institutional shortcomings. While economic growth has made it possible to multiply the Ministry of Transportation's budget (from 1 billion nuevos soles to 5.4 billion nuevos soles between 2006 and 2013), the investment gap remains wide and is projected to be US\$11 billion through 2025 (AFIN, Mintransporte). In this context of increased expenditure, the Ministry of Transportation continues to show weaknesses in all aspects of road management, from strategic planning to monitoring of works, affecting the quality of road infrastructure. These limitations are particularly significant for subnational governments,⁹³ since a large portion of the investment is executed or coexecuted at this government level.⁹⁴ These challenges are associated with the Sistema Nacional de Inversión Pública [National Public Investment System] (SNIP), which exhibits cumbersome processes, weaknesses in quality assessment, and long project

⁸⁷ Ministry of Transportation and Communication—General Office of Planning and Budget, Provías Nacional.

⁸⁸ IDB, Regional Logistics Observatory.

⁸⁹ Provías Nacional and Departamental.

⁹⁰ IDB, Regional Logistics Observatory.

⁹¹ These gaps negatively affect logistical performance in Peru. According to the World Bank's 2014 Logistical Performance Index (LPI), Peru is ranked 71st (out of 160 countries).

⁹² Lima has a total of 4.37 public transport vehicles per 1,000 inhabitants. This rate is nine times higher than the rate for Bogotá (Colombia).

⁹³ Regional governments are responsible for the departmental road network. Local governments, specifically provincial municipios, are responsible for the rural road network. However, the vast majority of local governments lack technical capacity and resources. See diagnostic assessments of PE-L1135: Subnational Transportation Support Program (PATS).

⁹⁴ Ministry of Transportation and Communication—Multiannual Strategic Sector Plan—Transportation and Communication Sector 2012-2016.

approval times. The SNIP is in the midst of a reform process.⁹⁵ In the case of urban transportation, there is a lack of specific public transportation policies. This lack has encouraged individual private transportation as well as a low level of investment by the central government in municipal urban transportation systems.

- 3.22 *Energy.* The quality of the electricity supply is becoming a bottleneck for business growth and productivity⁹⁶ and is affecting the business climate.⁹⁷ In the last 15 years, electricity coverage went from 64% to 91% of the population. The indicators of energy infrastructure quality are at similar levels to the average for Latin America, but below countries such as Chile, Mexico, and Uruguay. Between 2015 and 2016, Peru fell 13 places in the getting electricity indicators of the Doing Business Report, dropping from 51st to 64th places out of 189 countries.
- 3.23 The low quality of electricity service is due to lags in distribution infrastructure investment and an inadequate management model at the public electric utilities.⁹⁸ In the last 10 years, the low quality of electricity service has correlated with an infrastructure lag over the same period, indicating a challenge in terms of financing infrastructure requirements (Vera Tudela et al., 2013). A World Bank study (2008)⁹⁹ comparing the performance of public and private companies concludes that there is a pronounced difference between the two in labor productivity, distribution losses, rates, and service quality. This is related to shortcomings in the quality of electricity service due to the disparity among distribution companies in terms of quality of supply.¹⁰⁰ These challenges are coupled with corporate governance weaknesses in the public energy companies controlled by the Fondo Nacional de Financiamiento de la Actividad Empresarial del Estado [National Fund for Financing of State Enterprise Activities] (FONAFE).¹⁰¹

⁹⁵ Legislative Decree 1252, published on 1 December 2016, repealed the National Public Investment System (SNIP) Act and created the Sistema Nacional de Programación Multianual y Gestión de Inversiones [National Multiannual Investment Planning and Investment Management System] (invierte.pe). The MEF is currently preparing the implementing regulations for invierte.pe. With the newly created system, the MEF delegates all formulation responsibilities to the sector agencies and only takes on the governing role for multiannual investment planning. The objective of this change is to improve the relevance of public investment projects in order to reduce the infrastructure gap and shorten its preparation times.

⁹⁶ Devine (1983) finds a strong connection between economic growth and electricity use. At the company level, Allcott et al. (2014), Alby et al. (2013), and Kitchens & Fishback (2013) find that unreliable energy sources significantly lower the productivity of businesses across different sectors, essentially reducing their production potential and incentives to invest in more efficient capital. These effects are more pronounced in small, lower-revenue businesses that typically lack the resources to protect themselves against shortcomings in energy supply.

⁹⁷ The country's energy matrix shows a high share of primary fossil resources (80% including oil and gas) and sustainability challenges arising from the proven natural gas reserves.

⁹⁸ The limited long-term financing possibilities affect the investment plans of public companies, restricting them to short-term options (OECD, 2015b).

⁹⁹ World Bank (2008), Benchmarking Analysis of the Electricity Distribution Sector in the Latin American and Caribbean Region.

¹⁰⁰ Public companies have the lowest electric service reliability and continuity levels, as measured by the System Average Interruption Duration Index (SAIDI) and System Average Interruption Frequency Index (SAIFI).

¹⁰¹ <http://www.fonafe.gob.pe>.

- 3.24 *Digital divide*.¹⁰² Unlike developed countries, where mass internet use is primarily dependent on individual preferences or generational limitations, internet penetration in Peru (as in the rest of the region) is determined by the availability of infrastructure and other socioeconomic and geographic characteristics. In 2013, 26% of Peruvian households had fixed internet access (compared to a regional average of 30%), with a 26-point gap between urban (26%) and rural (0%) households. The ratio of households with internet access in the country's wealthiest quintile to households with internet access in the poorest quintile was 50, the highest in the region together with Paraguay.¹⁰³
- 3.25 One of the factors restricting internet use is the limited development of broadband. In 2015, Peru had a broadband development index of 4.28 (out of a possible 8), similar to the regional average of 4.24 but lower than the OECD average of 6.09. In particular, the country lags behind in infrastructure development, with an index score of 3.3 compared to a regional figure of 3.65 and the OECD score of 5.7.¹⁰⁴
- 3.26 The IDB Group will support improvements in management and sector planning for quality road and energy infrastructure supply and efforts to close the digital divide. In road infrastructure, the IDB Group will give particular consideration to support for urban mass transit systems as well as for expanding and improving the subnational road network. Proposed interventions in this sector will include participating in the financing of PPPs or private initiatives, facilitating the mobilization of private resources with a view to closing the infrastructure gap, together with IIC advisory services aimed at helping to manage the social and environmental risks of these projects. In the energy area, improving the quality of energy supply would require reviewing the legal and regulatory frameworks as well as adjusting the management model of public distribution companies to enable them to have an investment program consistent with the need for delivery of quality services. The IDB Group could perform a facilitating role aimed at implementing best practices in this area. IDB Group interventions seek to maximize the share of renewable energy¹⁰⁵ (including hydroelectric energy) and gas-based generation as a means of fostering a diversification of the energy matrix; support an expansion of the natural gas transportation and distribution network and an expansion of the electric transmission network to achieve greater and more efficient system coverage; and support integration with neighboring countries. The IDB Group will support the development of policies and the necessary infrastructure for adoption and use of information technologies. In particular, the IDB Group will assist Peru and the other members in developing the Digital Agenda of the Pacific Alliance, determining priority activities for its implementation and facilitating a dialogue between the public and private sectors.

¹⁰² All definitions of digital divide agree on the essence of the concept, which is the difference in access by the various sectors of the population to the information available through new information and communication technologies and the potential advantages resulting from such access.

¹⁰³ CAF 2015, *El Ecosistema y la Economía Digital en América Latina* [The Digital Ecosystem and Economy in Latin America].

¹⁰⁴ Iglesias et al., 2015, IDB—Annual Report on the Broadband Development Index in Latin America and the Caribbean.

¹⁰⁵ As of 2015, nonconventional renewable energy (small-scale hydroelectric, wind, solar, and biomass energy) accounted for just 2% of the country's electricity generation.

3.27 **Alignment.** The proposed actions in this strategic area contribute to the following objectives of the Update to the IDB Institutional Strategy 2010-2020: provide inclusive infrastructure and infrastructure services; provide adequate knowledge and innovation ecosystems; foster inclusion in financial markets; and insert firms into value chains. These initiatives contribute to the strategic priorities of the 2017-2019 IIC Business Plan: infrastructure development (particularly in transportation and energy), improvement of SME access to financing, directly and through value chains; support to the crosscutting areas of gender and diversity; and environmental sustainability.

3.28 **Portfolio contribution.** Forty-nine percent of the outstanding sovereign-guaranteed portfolio (equivalent to US\$625 million) contributes to productivity objectives. Specifically, the following operations are in execution: (i) four urban and rural transportation operations for US\$500 million aimed at enhancing the country's connectivity; and (ii) four trade facilitation, technological innovation promotion, and labor market operations for US\$125 million.¹⁰⁶ Eighty-one percent of the outstanding non-sovereign guaranteed portfolio (equivalent to US\$530 million) contributes to productivity objectives. Operations in this portion of the portfolio notably include: (i) financing for the Peru LNG energy project, with an exposure of US\$272 million; (ii) the Chaglla Hydroelectric Power Plant project, with a balance of US\$148 million; and (iii) nine operations supporting MSME development for US\$78 million.¹⁰⁷

B. Institutional strengthening and delivery of basic services¹⁰⁸

3.29 Institutions determine the volume, quality, timeliness, and accessibility of the public services provided to the population. In addition, institutions can eliminate obstacles to business productivity and growth and provide certainty in transactions and dispute resolution. Moreover, institutional performance affects business incentives.¹⁰⁹ The framework of public institutions, which determines effectiveness in policy design and implementation, poses challenges that relegate institutional performance indices in Peru to levels that are inconsistent with the country's income level. These challenges, which are common to several sectors and have to do with decentralized management and lack of institutional coordination, hinder basic service delivery.¹¹⁰

3.30 **Public management.** According to the World Economic Forum, the institutions pillar (as well as the innovation pillar) in the Global Competitiveness Index lags furthest behind, relegating Peru to 116th place (out of 140 countries), with a score of 3.3 out of a possible 7. This score has declined from 3.53 to 3.28 between 2011 and 2015.¹¹¹ Management weaknesses directly affect both the general public and businesses,

¹⁰⁶ PE-L1058, PE-L1151, PE-L1068, PE-L1135, PE-L1147, PE-L1152, PE-L1159, and PE-L1162.

¹⁰⁷ PE-L1016, PE-L1029, PE-L1102, PE-L1113, PE-L1136, PE1109A-03, PE3864A-02, PE3880A-02, PE3891A-01, PE3925A-01, PE3940A-01, PE3946A-01, PE3949A-01, PE3976A-01, and PE3984A-01.

¹⁰⁸ The actions planned in this area are aligned with United National Sustainable Development Goals 3 (good health and well-being); 5 (gender equality); 10 (reduced inequalities); and 16 (governance).

¹⁰⁹ IDB (2015b), Update to the Institutional Strategy 2010-2020.

¹¹⁰ See Vera Tudela, (2013) for electrification, Valdivia Vargas, (2013), Ministry of Education (2013) for education, Inter-American Development Bank (2015), PE-L1169: Management Modernization for Universal Health Coverage Program I and World Bank (2011a) and World Bank (2012) for health.

¹¹¹ In 2016, Peru climbed 10 places in the institutions pillar with respect to 2015. This progress is associated with an improvement in property rights protection, judicial independence, and transparency in government policies. However, Peru declined in the burden of government regulation pillar.

which report very low trust in institutions due to: (i) the slow pace of processing formalities; (ii) the lack of responsiveness by civil servants; (iii) the insufficiency of available information; and (iv) excessive requirements (LAPOP, 2014). In 2015, Peru was in the 44th percentile in government effectiveness and in quality of policy formulation and implementation, while Latin American and Caribbean countries were on average in the 53rd percentile, with OECD countries in the 88th percentile (World Bank). In corruption control, Peru was in the 33rd percentile, while Latin American and Caribbean countries were on average in the 52nd percentile, and OECD countries in the 85th percentile. As a result, the levels of trust in the legislative branch, the police, and the judiciary, among other public institutions, are lower than the regional average.¹¹² The rate of victimization due to corruption is 26.4%, exceeding the regional average of 20%.¹¹³

- 3.31 These indicators are framed in a context of growing decentralization. From 2005 to 2012, the budget managed by subnational governments expanded by 143%.¹¹⁴ In addition, the budget managed by local governments was 183% higher in 2012 than in 2007.¹¹⁵ However, these transfers did not always go hand in hand with the reforms (subnational capacity-building, instruments for policy and investment coordination, human resources, etc.) needed to formulate efficient and quality expenditures governed by the principles of subsidiarity, selectivity, proportionality, and precaution as indicated by international lessons learned.¹¹⁶ As a result, the different sectors, regional governments, and local governments have performed unevenly,¹¹⁷ with a significant fragmentation of investment projects (i.e., proliferation of small projects) and lack of coordination among the various levels of government when designing and executing public works.¹¹⁸
- 3.32 These weaknesses in institutional coordination are evident across the entire public sector.¹¹⁹ Other factors limiting the efficiency and effectiveness of the public sector

¹¹² LAPOP (2014). Sixty-two percent of citizens surveyed do not trust the police, and 66% have no trust in the judicial system. These are the highest levels of mistrust in the entire region.

¹¹³ LAPOP (2014). Twenty-six point four percent of those surveyed in Peru reported having been asked to pay a bribe in the previous 12 months. This percentage is lower than in Bolivia, Paraguay, Mexico, and Venezuela.

¹¹⁴ Office of the Comptroller General of Peru, Estudio del proceso de descentralización en el Perú [Study of the decentralization process in Peru], 2014.

¹¹⁵ In recent years, local governments have been responsible for 40% of total investment expenditures, while regional governments have been responsible for 21% and the central government for 39% (average for 2011-2015).

¹¹⁶ These principles are laid out in the Law Governing Decentralization.

¹¹⁷ Ibid.

¹¹⁸ OECD, 2015. Multidimensional Review of Peru. Volume 1. In addition, in 2016, according to data from the Office of the Comptroller General of Peru, 560 public works (74% at the local government level) in an amount equivalent to 4.293 billion new soles were at a standstill due to inadequate formulation issues. Another revealing piece of information in this regard is the high incidence of PPP contract renegotiations occurring shortly after the contracts are awarded. In the 2009-2015 period, 49 addenda were signed with respect to 22 transportation concession agreements, and 9 of these addenda were entered into within the first 3 years following the initial signature date (Apoyo).

¹¹⁹ Institutional Profiles Database (2012), Office of the Treasury, Government of France. Peru had an index of 1 out of a possible 4. In 2012, according to a global survey on interagency coordination, Peru's score was half the regional average for Latin America and the Caribbean and less than one third the average for OECD countries. The same survey, which covered 143 countries, ranked Peru in 127th place in quality of the public policy formulation process.

- include: (i) shortcomings in the design and execution of public investment;¹²⁰ (ii) weaknesses in the legal and institutional framework in preventing and controlling corruption;¹²¹ and (iii) an excessive regulatory burden,¹²² associated with limited use of information technologies to facilitate government procedures for the public.¹²³
- 3.33 In this context, the IDB Group will support the government in: (i) strengthening institutional coordination for the delivery of public goods and services; (ii) consolidating strategic planning of public investment, including its linkage to PPP projects; (iii) simplifying procedures and improving regulatory quality and encouraging the use of information technologies (electronic government); and (iv) strengthening the legal and institutional framework for integrity and transparency in the public sector.
- 3.34 The aforementioned institutional challenges, coupled with a low level of public spending,¹²⁴ limit the ability to deliver quality public services in key sectors such as health, citizen security, and water and sanitation.
- 3.35 **Health.** Infant mortality varies according to geographic area—Lima metropolitan area: 12 per 1,000 live births; the rest of the coastal region: 14 per 1,000 live births; the highlands region: 25 per 1,000 live births; and the jungle region: 25 per 1,000 live births—or according to the mother’s educational level—no education: 34 per 1,000 live births; primary education: 24 per 1,000 live births; secondary education: 15 per 1,000 live births; and higher education: 17 per 1,000 live births. Together with Bolivia and Ecuador, Peru has the region’s highest chronic malnutrition rates after Guatemala, and the likelihood that a child will be malnourished is approximately five times higher for children of poorly educated mothers than for children of highly educated mothers (Berlinski et al., 2015). In 2014, according to the ENDES, 37% of children under five nationwide suffered from anemia. Chronic malnutrition affected 43%, and anemia 43.5%, of children under five in indigenous households.¹²⁵

¹²⁰ Public investment is characterized by an extensive fragmentation of projects (large number of small projects) and lack of coordination among the various government levels (among municipios and between local governments and the regional government) when designing and carrying out public works (OECD, 2015. Multidimensional Review of Peru. Volume 1). This limited capacity is reflected in the data from the Office of the Comptroller General of Peru. In 2016, 560 public works (74% at the local government level) in an amount equivalent to 4.293 billion new soles were at a standstill due to inadequate formulation issues. Another revealing piece of information in this regard is the high incidence of PPP contract renegotiations occurring shortly after the contracts are awarded. In the 2009-2015 period, 49 addenda were signed with respect to 22 transportation concession agreements, and 9 of these addenda were entered into within the first 3 years following the initial signature date (Apoyo).

¹²¹ PCM and GHZ (2012) Good practices for promoting the Code of Ethics in Public Service.

¹²² The number of regulations is partly the reason that Peru is ranked 133rd out of a total of 140 countries in the regulatory burden indicator of the World Economic Forum’s 2015-2016 Global Competitiveness Index. Peru’s score is 2.7, pointing to a significant regulatory burden. The use of information technologies for the delivery of public services is restricted by the extent of broadband development.

¹²³ See paragraph 3.24-3.25. Complex procedures and the use of obsolete technologies to process information are additional reasons for an environment that favors a lack of transparency (OECD, 2016).

¹²⁴ Social public spending accounts for 9.5% of GDP, compared to a regional average of 14% of GDP (CEDLAS).

¹²⁵ Flores-Bendezu et al. (2015), *Desnutrición crónica y anemia en niños menores de 5 años de hogares indígenas del Perú—Análisis de la Encuesta Demográfica y de Salud Familiar 2013* [Chronic malnutrition and anemia among children under the age of five in indigenous households in Peru—Analysis of the 2013 Demographic and Family Health Survey].

Between 1990 and 2013, the burden of chronic diseases measured in years of life adjusted for disability went from 34% to 64%, the burden of communicable and maternal-infant diseases went from 46% to 22%, and the burden of violence and accidents went from 20% to 13% (Global Burden of Disease, 2013). The principal epidemiological challenge faced by the country, with health service consequences, is the search for care related to cancer, hypertension and cardiovascular disease, diabetes, depression, anxiety, chronic kidney diseases, and chronic respiratory diseases. The rapid growth of chronic diseases has not been matched by an expansion of health services, which are primarily aimed at delivering maternal-infant services (Global Burden of Disease, 2013). The Ombudsman's Office (2015) reports that more than half of the indigenous people lack health facilities. Between 2004 and 2015, public insurance coverage went from 15% to 46% thanks to an expansion of the Seguro Integral de Salud [Comprehensive Health Care Insurance] (SIS), which is facing sustainability problems.¹²⁶

- 3.36 In addition to the sector's institutional weaknesses,¹²⁷ the poor quality of health care, associated with the low level of spending and limited investment management capacity accounts for these results.¹²⁸ Service quality is low. In the public sector, indicators of delays in receiving care (two hours) and in scheduling an appointment (three weeks) are high (Susalud, 2015). Despite having increased, public spending is insufficient to close the gaps and improve service quality. Per-capita health expenditure—purchasing power parity (PPP) US\$626 in 2013—is lower than in Colombia (US\$842), Mexico (US\$1,061), Brazil (US\$1,453), Chile (US\$1,678), and the average for Latin America and the Caribbean (US\$1,132) and for OECD countries (US\$4,579) (World Bank, 2015). Investment management in the public sector faces three main weaknesses: (i) discretionary investment decisions; (ii) duplication resulting from a lack of joint planning among the various system segments; and (iii) limited institutional capacity for timely execution of the investment cycle.¹²⁹
- 3.37 In this area, the IDB Group will support the country in: (i) better organizing investment in and delivery of health services, prioritizing institutional strengthening in the sector and more efficient services in the primary health care network; and (ii) identifying opportunities for synergies between the IDB and the IIC in the context of health-related PPPs, expanding the availability of financing for cofinanced public initiatives, by following the experience of MINSA and EsSalud in granting concessions for hospital projects through PPPs. There is potential for attracting

¹²⁶ The SIS is not an insurance fund in the classic sense but rather a budgetary channel for financing the public health care system. The MEF does not treat it as an insurer, since the amount of budgetary transfers to the SIS is not calculated on an actuarial basis; i.e., it does not take into account either the size and characteristics of the insured population or the probability and cost of the insured events. An annual budget is determined on an ad hoc basis, and the transfer amount per insured individual has varied considerably.

¹²⁷ Vallejos-Ragas and Vilcahuaman-Bernaola (2013), Modelos de atención de salud en el Perú. Contextos e influencias [Health care models in Peru. Contexts and influences]. The fragmentation of the health system is considered one of the main causes of inefficiency and inequity in the delivery of health services.

¹²⁸ World Bank (2012), Public Expenditure Review.

¹²⁹ The Ministry of Health (MINSA) has identified an investment gap of close to US\$5 billion aimed at building new (especially primary care) facilities and repairing, expanding, or modernizing existing (especially hospital) facilities - Cetrángolo et al. (2013), El sistema de salud del Perú: situación actual y estrategias para orientar la extensión de la cobertura contributiva [The health care system in Peru: Current state and strategies for extending tax coverage].

- private investment to the sector, as evidenced by the interest shown by the private sector in the form of several private initiatives submitted to Proinversión. Because this is a high social impact sector, there is an opportunity to mobilize resources from the impact investor community through syndicated loans or cofinancing, where the PPP modality does not yet have a track record to match that of other, more traditional sectors (i.e., transportation, energy).
- 3.38 **Citizen security.** Peru has the highest victimization rate in all of Latin America: 30.6% as compared to a regional average of 20% in 2014.¹³⁰ Between 2002 and 2014, violence against women rose from 193.9 cases to 284.9 cases per 1,000 women (Demographic and Family Health Survey, ENDES).¹³¹ Only 31% of Peruvians trust the police, and close to 70% are very or somewhat dissatisfied with police performance (Latinobarómetro, 2015).
- 3.39 Shortcomings in coordination among the institutions involved in the citizen security system and their limited management capacity adversely affect the quality of service. This is due to: (i) inadequate institutional structure in the Ministry of Interior and lack of effective mechanisms for effective administrative, operational, and budgetary management;¹³² (ii) difficulties in gathering information and evidence and limited capacity for criminological analysis by the National Police;¹³³ (iii) inappropriate human resource policy and management by the National Police;¹³⁴ (iv) absence of planning and strategic and operational management by the National Police and limited coordination between the National Police and the Municipal Security Guards with a view to joint actions in the territory;¹³⁵ (v) limited physical, technological, and operational infrastructure resources;¹³⁶ and (vi) fragile internal monitoring and control system to ensure effective delivery of security services to the public.¹³⁷
- 3.40 This is coupled with high rates of criminal recidivism and low productive integration of youth. The criminal recidivism rates in both the adult prison system (69%)¹³⁸ and in adolescent offenders (8%) are high and are due to: (i) inadequate functioning of

¹³⁰ Percentage of population 15 years or older who have been victims of robbery, theft, assault, fraud, blackmail, extortion, threats, or other type of crime in the last 12 months. Source: LAPOP's Barómetro de las Américas, 2014.

¹³¹ Demographic and Health Survey(ENDES).

¹³² Based on the results of the Ministry of the Interior's self-assessment on the 11 standards it should meet to ensure quality service for the population, the MININTER obtained a general score of 51 points out of 120 (43%). Specifically, it obtained a low score on service standards including the following: customer care (20%), measurement and public satisfaction (22%), procedural processes (33%), internal organization (40%), and access to information (56%). (Plan for MININTER Institutional Management Modernization, 2014-2016).

¹³³ Peru: Census of Police Precincts, INEI, 2014.

¹³⁴ Inseguridad en Perú ¿Qué hacer? [Insecurity in Peru: What to do?], Costa and Romero, 2011.

¹³⁵ Inseguridad en Perú ¿Qué hacer? [Insecurity in Peru: What to do?], Costa and Romero, 2011.

¹³⁶ Peru: Census of Police Precincts, INEI, 2014.

¹³⁷ Mininter-PNP Work Agenda on Modernization, Modernization and Institutional Development Office, Ministry of the Interior, September 2016.

¹³⁸ The recidivism rate is 64% in Barbados, 59% in Uruguay, and 17% in Chile (Organization of American States 2014: Reduciendo la reincidencia delictiva: Metodología estandarizada para el monitoreo y la evaluación de proyectos y programas de reintegración social orientados a la disminución de la reincidencia delictiva [Reducing criminal recidivism: Standardized methodology for monitoring and evaluating social rehabilitation projects and programs aimed at reducing criminal recidivism]).

- prisons and adolescent rehabilitation centers; and (ii) a lack of rehabilitation and social reintegration infrastructure and programs for offenders.¹³⁹ In addition, an average of 25.4% of young people aged 15 to 24 do not work or attend school.¹⁴⁰
- 3.41 In this area, the IDB Group proposes (i) strengthening sector management, particularly on the part of the Ministry of Interior and the National Police; and (ii) supporting the design and implementation of public policies aimed at preventing, addressing, and controlling crime.
- 3.42 **Alignment.** The initiatives in this strategic area contribute to the following objectives of the Update to the Institutional Strategy 2010-2020: strengthen the capacity of the state; eradicate extreme poverty; and provide inclusive infrastructure and infrastructure services; and the crosscutting issue of strengthening institutional capacity. These initiatives also contribute to the strategic priority of the 2017-2019 IIC Business Plan of supporting the development of social infrastructure.
- 3.43 **Portfolio contribution.** Thirty-two percent of the active sovereign-guaranteed portfolio (equivalent to US\$411 million) contributes to institutional strengthening and basic services delivery objectives. Six operations are in execution for a total amount of US\$111 million, aimed at strengthening public management in the strategic areas of transparency; public investment; tax administration; judicial system administration; and financial administration and State payroll.¹⁴¹ Added to this is a programmatic policy-based loan (PBL/DDO) for the health and social protection sector for US\$300 million.
- C. Environmental sustainability and climate change¹⁴²**
- 3.44 Peru is one of the most biodiverse countries in the world (in 2014, it was ranked 11th out of 187 countries by the World Bank). The country has 73 million hectares of natural forest, equivalent to 57.3% of its national territory, and 94% of this total is in the Amazon region (Minambiente, 2015). For Peru, as for the other countries in the region, coordinating sustainable development goals with the commitments arising from the COP21 (nationally determined contributions (NDCs)) is a priority challenge. Developing NDCs will be an undertaking cutting across the priority sectors through mitigation and adaptation measures associated with comprehensive management

¹³⁹ INEI, 2016 and Ministry of Justice and Human Rights, 2015.

¹⁴⁰ INEI, Map of Provincial and District Poverty 2013.

¹⁴¹ PE-L1031, PE-L1154, PE-L1169, PE-L1187, PE-L1101, PE-L1106, PE-L1130, and PE-L1132.

¹⁴² The actions planned in this area are aligned with United Nations Sustainable Development Goals 6 (clean water and sanitation); 13 (climate actions); and 15 (ecosystems).

of water resources,¹⁴³ renewable energy, and sustainable transportation, as well as sustainable agriculture and avoided deforestation.¹⁴⁴

- 3.45 **Water resources.** Water availability in Peru, in terms of both quantity and quality, is being seriously affected by climate variability and climate change. In addition, population growth is exerting pressure on demand in numerous areas of the country. Water coverage is not universal. Fourteen percent of households have no access to drinking water and 32% of households lack sanitation facilities. These figures compare unfavorably to the average for the region (5% for water and 17% for sanitation). Twenty-one point nine percent of Peruvian households with an indigenous head of household and 14.7% of Peruvian households with an Afrodescendant head of household lack access to drinking water (ENAHO, 2015). Water and sanitation coverage in urban areas is respectively 95% and 87.7%, while coverage in rural areas is respectively 68.4% and 22.1%.¹⁴⁵ A mere 40% of those in the poorest quintile have access to improved sanitation solutions. Service quality is a challenge. According to the National Superintendency of Sanitation Services (SUNASS), in 2014, between 10% and 50% of the wastewater produced in the country's sewer services was treated by a public utility.¹⁴⁶ On average, the urban population with access to drinking water receives this service 19 hours a day (only four public utilities provide service 24 hours a day) and only 66% of this population has micrometering (below the estimated average of 80% for Latin America and the Caribbean). In addition, 36% of the water produced is unbilled. This percentage is lower than the estimated average for the region (40% to 50% at the vast majority of utilities) but higher than the figure at efficient utilities in developed countries (10% to 20%).¹⁴⁷
- 3.46 The main reason for the geographic gaps in water and sanitation is the difference in investments to date: 71% of investments in the sector have been in urban areas, and only 29% have been in rural areas.¹⁴⁸ In addition, inefficient business management by municipal public utilities is reflected in operational issues and low

¹⁴³ Of water for consumption, 86.6% is used for agricultural purposes, while 11.4% is used by the population, 1.4% for mining purposes, and 0.6% for industry (National Water Authority (ANA)). Eighty percent of the water consumed by the agricultural sector comes from the Pacific watershed. Mining poses challenges for water management in the watersheds, not because of the volume of demand, which is relatively low, but rather because of the risk of pollution from the dumping of water resulting from the processing of minerals. These challenges are associated with the proliferation of artisanal and informal mining and with the environmental liabilities of old mines (National Water Authority (ANA)). This underscores the need to develop a comprehensive approach in the management of water resources so as to take the impact of climate change into account.

¹⁴⁴ IDB 2014. Water and Sanitation Sector Framework Document; IDB 2015, Climate Change Sector Framework Document; IDB 2016, Agriculture and Natural Resources Management Sector Framework Document.

¹⁴⁵ INEI, ENAPRES, 2015.

¹⁴⁶ The percentage depends on the size of the public utility. The large ones treated 53% of the wastewater, the medium-sized ones treated 23%, and the small ones treated 9%.

¹⁴⁷ Data from the National Superintendency of Sanitation Services and the Asociación de Entes Reguladores de Agua Potable y Saneamiento de las Américas [Association of Water and Sanitation Regulatory Agencies in the Americas] (ADERASA).

¹⁴⁸ Ministry of Housing. 2014 National Investment Plan.

service quality arising from issues including poor institutional coordination and limited capacity on the part of local and regional governments.¹⁴⁹

- 3.47 In this area, the IDB Group will support the country in: (i) closing the investment gap to expand water and sanitation coverage in urban, periurban, and rural areas; (ii) strengthening and modernizing the operators, examining the option of introducing management models with private-sector participation where the IIC could play a financing role; and (iii) reinforcing the institutional capacity of and coordination among the sector authorities responsible for managing the water resources.
- 3.48 **Environmental management.** There is limited capacity to manage natural resources and the environment. The World Economic Forum's environmental sustainability indicators rank Peru in 58th place (out of 113 countries) in terms of rigorousness of environmental regulations and in 76th place in terms of ability to enforce environmental regulations, with a score of 4 of a possible 7, below Chile (4.42) and Uruguay (4.23). There is evidence that expansion of the agricultural frontier in the jungle region threatens the Amazonian forest. This is related to a lack of clarity regarding land rights.¹⁵⁰ Peru does not have a deforestation monitoring system, but data compiled by external sources indicate that average deforestation for 1975-2000 was 108,392 hectares/year.¹⁵¹ More than half the hectares of deforested land are the result of forest fires associated with agricultural work, involving farming practices that exert strong pressure on primary and secondary forests and damage the ecosystem (POF, 2011).
- 3.49 The reasons for this performance are related to noncompliance with environmental regulations due to weak institutional coordination, lack of environmental information, and ineffective oversight (Ombudsman's Office, 2015).¹⁵² At the institutional level, there is a duplication of agency responsibilities and mandates as well as excessive decentralization coupled with a lack of capacity to perform environmental management work on the part of regional and local governments.¹⁵³ The limited availability of information on the state of the environment, the limited use of existing information and inventories of polluting activities are an obstacle to proper regulation, monitoring, and oversight (World Bank, 2015a). Lastly, incomplete enactment of implementing regulations for existing laws and an inadequate system of penalties diminish the effectiveness of environmental oversight (Ombudsman's Office, 2015).
- 3.50 Solid waste management is an element that affects environmental management. According to the National Statistics Institute, 694 municipios collect garbage on a daily basis, 341 municipios do so on a weekly basis, 382 municipios collect garbage twice a week, and 325 municipios collect it every other day. In the department of

¹⁴⁹ ANA and OECD (2012).

¹⁵⁰ Zegarra and Gayoso (2015).

¹⁵¹ The deforestation rate varies by decade: 150,000 hectares/year in 1990-2000 (PROCLIM); 108,572 hectares/year in 2000-2010 (DGOT); and 132,690 hectares/year in 2010-2012 (CIAT).

¹⁵² In recent years, Peru has been making efforts to build institutional capacity to protect the environment. Public spending was increased, new government agencies were created, and new laws and decrees were approved establishing quality standards and regulating environmental licenses (World Bank, 2011b).

¹⁵³ IDB, (2014i).

- Lima, 85 municipios provide daily garbage collection.¹⁵⁴ Final disposal service is still limited: in 2014, a total of 7.5 million tons of municipal waste was generated, less than 50% of which was disposed of in sanitary landfills.¹⁵⁵ The main challenges in terms of solid waste¹⁵⁶ are: (i) weak municipal institutions; (ii) an inadequate infrastructure; and (iii) lack of sector planning, since only 62% of provincial municipios have lawfully approved comprehensive solid waste management plans and 17% promote the formalization of recyclers.¹⁵⁷
- 3.51 In this area, the IDB Group will work with the country toward: (a) clearer land title rights; and (b) effective management of natural resources and the environment through a comprehensive environmental management system that includes: (i) environmental quality standards, rights of use or development of natural resources; (ii) an environmental information system; and (iii) a streamlined and modern environmental licensing system that allows decentralized action under national public policy regulations. In the solid waste area, the IDB Group will support: (i) recovery of degraded areas; and (ii) strengthening of municipal management in terms of final disposal of solid waste. In addition to supporting policy reform aimed at enabling compliance with commitments to reduce carbon emissions under the NDC, the Bank will prioritize monitoring and verification issues by developing the Sustainability and Climate Change Fund with the Norwegian government. Peru will participate in technical cooperation activities under the Canadian Extractive Sector Facility (CANEF), financed by the Government of Canada with a view to improving the regulatory framework and governance of resources. The IIC and the MIF will assess opportunities for reducing vulnerability to climate change through the following initiatives: (i) housing, by leveraging prior IIC support in preparing the Sustainable Building Code and eligibility criteria for sustainable housing; (ii) transportation, by reducing the country's high dependence on diesel and petroleum derivatives, incorporating biofuels and expanding the use of natural gas for vehicles; (iii) agriculture, by fostering the adoption of sustainable practices by agricultural producers, particularly those with export potential, and promoting investment in technologies such as efficient irrigation and renewable energy; and (iv) energy efficiency in the industrial, commercial, service, and residential sectors.
- 3.52 **Agribusiness.** Peru continues to have a significant gap in agricultural productivity with the region and the OECD.¹⁵⁸ Moreover, there are disparities in this gap both geographically and in terms of products. Producers in the coastal region are up to 5% more productive than those in the highlands and jungle regions.¹⁵⁹ While the yield of products such as grapes, tangerines, asparagus, and mangoes (coastal crops) grew at annual rates of 2.2% to 5.2% between 2000 and 2013, the potato (a highlands crop) yield grew at an annual rate of 1.7% in the same period (Apoyo

¹⁵⁴ INEI (2014), Environmental Statistics Yearbook.

¹⁵⁵ MINAM, 2016. National Integrated Solid Waste Management Plan. Forty-six point seven eight percent of the waste is being improperly disposed of in the environment, in dumps, bodies of water, and uncontrolled burns. This could become a serious health and environmental problem.

¹⁵⁶ MINAM, 2016. National Integrated Solid Waste Management Plan.

¹⁵⁷ OEFA, Fiscalización Ambiental en Residuos Sólidos de Gestión Municipal Provincial [Environmental Oversight of Provincial Municipal Solid Waste Management], 2013-2014.

¹⁵⁸ Galarza et al. (2015).

¹⁵⁹ Galarza et al. (2015).

- Consultoría, 2015). In the coastal and jungle regions, there are higher levels of alliance-building.¹⁶⁰ Allied producers are more market-oriented, engage in better agricultural practices, enjoy greater access to credit, have infrastructure and machinery of higher value, and exhibit better well-being indicators than non-allied producers.¹⁶¹
- 3.53 Constraints on increases in agricultural productivity are associated with the availability of assets.¹⁶² According to the 2012 National Agricultural Census (CENAGRO), only 25.6% of the country's farmers have registered title to their land. The remainder do not have clear land ownership rights. This constraint is even more pronounced in the highlands region, where 64.3% of farmers lack such rights, as compared to 11.2% in the coastal region and 24.5% in the jungle region (CENAGRO, 2012). The lack of clear land ownership rights limits access to credit (Torero and Field, 2005) to such an extent that, according to the 2012 CENAGRO, only 10% of producers obtained loans. In addition, there is a correlation between this deficiency and deforestation in the jungle region (MINAM, 2015). Twenty percent of agricultural establishments in Peru are headed by women, who have an average of 1.8 hectares of farmland as compared to 3.3 hectares in the case of men. The agricultural sector continues to represent a small share of the financial sector, accounting for 5.2% of all lending in 2015 (Superintendency of Banks). In addition to land tenure, the farming cycle, the risks associated with climate change, and the absence of specialized instruments (microinsurance) hamper an expansion of credit to the sector (IDB, 2016). In 2015, according to the National Water Authority (ANA), only 20% of farmers in the highlands region had water rights, while in the coastal region the proportion was 80%.
- 3.54 To contribute to the agricultural sector's productivity and mitigate the environmental impacts, the IIC and the MIF plan to support the sector by means of: (i) direct operations, particularly aimed at enterprises with competitive products, to finance investment capital and supplementary working capital;¹⁶³ (ii) financing and guarantees through financial intermediaries such as commercial banks, microfinance institutions, development banks, and anchor firms in value chains; and (iii) knowledge products and technical assistance for commercial banks and microfinance institutions with a view to improving their technology for assessing agricultural credit risk, and advisory support to sub-borrowers—particularly small farmers—to improve their productivity, agricultural technology, and management and business skills.
- 3.55 **Alignment.** The initiatives in this strategic area contribute to the objective of the Update to the IDB Institutional Strategy 2010-2020 of addressing the economic and social impacts of climate change adaptation and mitigation. These initiatives also contribute to the following strategic priorities of the 2017-2019 IIC Business Plan: development of water infrastructure; improvement of access to financing and

¹⁶⁰ See Fort and Vargas, in Escobal et al. (2015). Producers who belong to production associations account for approximately 10% of the total, while the proportion of producers of this type in the highlands region is only 3%.

¹⁶¹ See Fort and Vargas, in Escobal et al. (2015).

¹⁶² The agricultural sector continues to have a limited share of the financial sector, accounting for 5.2% of all lending in 2015 (Superintendency of Banks).

¹⁶³ These could include energy efficiency projects.

corporate sector capacities, with special emphasis on the agribusiness sector, including all actors in the agricultural value chain; and support for environmental sustainability.

- 3.56 **Portfolio contribution.** Sixteen percent of the outstanding sovereign-guaranteed portfolio (US\$210 million) contributes to the objectives of environmental sustainability and climate change. Two investment loans (US\$115 million) to improve access to water and sanitation services and three operations (US\$95 million) to promote sustainable agriculture are currently in execution.¹⁶⁴ Six percent of the outstanding portfolio of non-sovereign guaranteed operations (equivalent to US\$39 million) contributes to the objectives of environmental sustainability and climate change. These operations notably include financing for Damper Trujillo to allow the firm to expand its asparagus and avocado production and invest in machinery and equipment, with an exposure of US\$37 million.¹⁶⁵

IV. PROJECTED LENDING FRAMEWORK

- 4.1 The projected demand scenario for sovereign-guaranteed financing envisages annual approvals for an average of US\$300 million or a total of US\$1.5 billion for the 2017-2021 period. These approvals, together with the expected disbursements, would enable the Bank to maintain a 10% share of the country's total external debt. To achieve this level of approvals, the Bank will stress its technical support in the strategic areas. During the strategy implementation period, the IDB Group will continue to explore options such as a treasury or other instrument that can provide local currency in an efficient, cost-effective manner. The Peruvian government is expected to continue to have access to financial markets on favorable terms. It is worth noting that the differential between the Bank's sovereign-guaranteed financing conditions and the financial markets has been narrowing in recent years. In the new strategy period, larger operations with more efficient disbursements will be given preference.

V. STRATEGY IMPLEMENTATION

- 5.1 **Coordination within the IDB Group.** Coordination among the IDB, the IIC, and the MIF will follow the following parameters: (i) joint implementation of this country strategy; (ii) planning of joint missions to interact with authorities, particularly in areas requiring policy reforms and/or with evident synergies allowing for complementary work; (iii) organization of joint activities aimed at disseminating the IIC's work to expand and diversify its portfolio of potential clients; (iv) maximization of operational synergies; and (v) joint knowledge products that are relevant for an operational dialogue with clients.
- 5.2 **Donor coordination.** The Bank envisages a close collaboration with: (i) KfW and the Government of Spain in the area of water and sanitation; (ii) JICA in the area of solid waste management; (iii) Canadian International Development Agency (CIDA) in the area of energy, implementation of the Canadian Extractive Sector Facility (CANEF), and institutional strengthening (transparency and anticorruption efforts);

¹⁶⁴ PE-L1060, PE-L1092, PE-L1026, PE-L1122, and PE-L1125.

¹⁶⁵ PE-L1143, PE3886A-01, PE3955A-01.

(iv) the World Bank in executing the investment plan of the Forest Investment Program and the judicial case file digitization program; and (v) multilateral banks (World Bank, CAF, and the European Investment Bank) and bilateral cooperation agencies (KfW and AFD) for Line 2 of the Lima Metro. Also worth noting is the coordination with the Government of Norway in developing the National Forest Conservation and Climate Change Strategy.

5.3 Country systems. At present, the Bank makes full use of the budget, treasury, accounting and reporting, and external control subsystems. In 2013, the Bank's Board of Executive Directors (document GN-2358-11) approved the use of the framework agreement and reverse auction electronic catalogue subsystems of Peru's Sistema de Adquisiciones Públicas [public procurement system] (SAP). The SEACE advertising subsystem will continue to be used for contracts of all types. A diagnostic assessment of the SAP, completed in 2016 using the OECD/DAC methodology, shows significant progress with respect to the previous (2008) assessment.¹⁶⁶ In several indicators, Peru meets international best practices. Nonetheless, there continues to be room for improvement in the institutional framework and management capacity of the SAP operators, in promoting greater competition, and in strengthening the policy framework for combating fraud and corruption in public procurement. The Bank will continue to provide support for improving SEACE (the transactional procurement portal), developing the capacities of the SAP operators, standardizing and improving bidding processes and documents, and streamlining and modernizing government procurement policies and simplifying procurement regulations, and technical assistance for expanding the scope and use of electronic catalogues for framework agreements and reverse auctions.

5.4 While the public financial management system has been strengthened, additional efforts are needed in: (i) implementing a results-based budget and technologically upgrading the computer tool for integrated financial management (SIAF); (ii) the process of implementing internal control regulations based on international practices; and (iii) strengthening external control to support the Office of the Comptroller General of Peru (CGR) as governing body of the national control system. In this context, the Bank will continue to support strengthening the public financial management, transparency, and accountability country systems. The following table summarizes the use of country systems in Peru:

Use of country systems	2016 baseline	2021 projected use	Planned actions
Budget	100%	100%	Strengthening by upgrading the information technology tool through a future operation that will supplement operation 2445/OC-PE.
Treasury	100%	100%	Training for MEF users in the use of the financial management system, financed through a future operation that will supplement operation 2445/OC-PE. Plans call for a diagnostic assessment of the treasury single account based on the Bank's methodology.

¹⁶⁶ Based on the results of the 2016 SAP diagnostic assessment, a new advanced validation of the SAP will be performed during the 2017-2021 period with a view to using the SAP in Bank-financed projects in Peru.

Use of country systems	2016 baseline	2021 projected use	Planned actions
Accounting and reporting	100%	100%	Diagnostic assessments will be performed to identify areas requiring intervention (loan 2445/OC-PE does not encompass interventions in the SIAF I project management module). The government is expected to include management of externally financed projects as part of the operation that will supplement the SIAF II operation to avoid reducing the level of use achieved to date.
Internal audits	0%	0%	Support for formulation of a regulatory framework and development of methodology guides for internal control, as well as for promotion and training in the aforementioned framework, through operation 2969/OC-PE. A diagnostic assessment of the subsystem is expected to be available around 2020.
External audits	100%	100%	Strengthening of CGR capacities through loan 2969/OC-PE.
Information system	100%	100%	The SEACE advertising subsystem will continue to be used for contracts of all types.
Shopping	47%	100%	Source: IDBDOCS-40672110-Boletin_Uso_parcial_de_sistema_nacional_PRM_en_Peru_a_sept_2016.PPT
Individual consultants	0%	100 %	A new advanced validation of Peru's SAP will be performed based on the 2016 MAPS results.
Partial NCB	0%	100%	A new advanced validation of Peru's SAP will be performed based on the 2016 MAPS results.
Advanced NCB	0%	100%	A new advanced validation of Peru's SAP will be performed based on the 2016 MAPS results.

VI. RISKS

- 6.1 **Institutional coordination.** The complexity of interagency coordination has made it difficult to identify priority projects on an orderly basis as well as to design and implement public investment. This has led to sector initiatives not always in line with the priority areas of the Bank and the government in the context of the country strategy. To mitigate this risk and ensure that the Bank carries out its operations within the framework of the country strategy, the Bank will maintain a continuous dialogue with the authorities in the Presidency of the Council of Ministers (PCM) and the Ministry of Economy and Finance (MEF). At the same time, the Bank will work with the MEF to strengthen the strategic planning capacity for the country's public investment either through traditional public procurement or through PPPs. The Bank will monitor this risk through periodic government coordination and portfolio review meetings.
- 6.2 **Execution risk.** The weakness of some executing agencies in terms of their capacity to manage investment projects is one of the main execution risks for the Bank's portfolio in Peru. To mitigate this risk and improve the pace of execution and disbursement, during the new operation design stage, the Bank will place greater emphasis on assessing the institutional capacity of the entities responsible for execution, particularly those that have not previously worked with the Bank. This will make it possible to determine the institutional strengthening needs and provide training to strengthen execution and monitoring capacity with a view to achieving the outcomes agreed upon by the Government of Peru and the Bank. Recognizing the challenges involved in executing the portfolio and the financing framework envisaged in this strategy, the Bank plans to: (i) focus Bank interventions on larger-scale operations with more efficient disbursements, mitigating potential execution risks in units that have no experience working with the Bank and providing institutional strengthening to the executing agencies that so require, building project planning and management capacity; and (ii) generate institutional capacity for project structuring and management under a strategic planning approach. By mitigating the risks affecting execution, the use of Bank products that allow greater execution efficiency will make for better management of portfolio resources. The Bank will monitor this risk through periodic portfolio review meetings.

ANNEX I: RESULTS MATRIX

Government priorities (strategies)	The Bank's strategic areas	The Bank's strategic objective	Expected outcomes	Indicator	Baseline	Source
ECONOMIC RECOVERY	Economic productivity	Support formalization of the economy	Increase the percentage of workers who contribute to social security	Percentage of workers who contribute to the social security system	2014: 20%	SIMS, IDB (1)
		Support business development	Increase total (public and private) investment in R&D	Total investment in R&D (% of GDP)	2014: 0.16%	RICYT
		Strengthen the business climate	Improve the business climate	Ease of doing business index (distance from the border, percentage points)	2017: 70.25	World Bank: Doing Business
PROMOTING SCIENCE, TECHNOLOGY, AND INNOVATION		Improve the available infrastructure	Improve the quality of the road transportation infrastructure	Paved network (% of the total)	2012: 13%	Ministry of Transportation
			Improve the quality of the electricity supply	Quality of electricity supply index	2015: 4.7/7	WEF
			Increase the use of public mass transit	Percentage of daily trips made using public mass transit	2011: 5%	Ministry of Transportation
MODERNIZATION OF THE STATE TO SERVE THE PUBLIC	Institutional strengthening and delivery of basic services	Improve public management	Boost public management capacity	Public sector performance index	2015/2016: 2.8/7	WEF
			Strengthen the legal and institutional integrity framework	Ethics and corruption index—public institutions pillar—global competitiveness index	2015/2016: 2.7/7	WEF
			Increase the use of information technology in government formalities	Percentage of individuals who reported using internet to complete formalities	2015: 8.5%	Latinobarómetro
ZERO TOLERANCE FOR CORRUPTION		Improve access to and quality of health care services	Reduce anemia due to iron deficiency in children under age five	Percentage of children (< 5) with anemia due to iron deficiency	2014: 37%	ENDES
			Reduce mortality due to chronic diseases	Probability of dying at 30 to 70 years of age due to any of the four major chronic diseases	2014: 11%	WHO

Government priorities (strategies)	The Bank's strategic areas	The Bank's strategic objective	Expected outcomes	Indicator	Baseline	Source	
			Reduce wait times for generic medical checkups	Wait in days to receive a medical checkup [2]	2015: 19.4	SUSALUD	
		Improve citizen security	Reduce the crime rate in the population	Percentage of the population that has been the victim of a crime [3]	2014: 30.6%	LAPOP	
ENVIRONMENTAL PROTECTION	Foster environmental sustainability and climate change mitigation and adaptation	Improve access to and quality of water and sanitation service	Increase drinking water coverage in urban and rural areas	Drinking water coverage in urban areas	2015: 94%	INEI, ENAPRES	
				Drinking water coverage in rural areas	2015: 68.4%	INEI, ENAPRES	
				Increase basic sanitation coverage in urban and rural areas	Basic sanitation coverage in urban areas	2015: 87.7%	INEI, ENAPRES
DRINKING WATER FOR EVERYONE				Basic sanitation coverage in rural areas	2015: 22.1%	INEI, ENAPRES	
				Increase wastewater treatment	Rate of wastewater treatment by service providers	Midsized service providers: 23% Small service providers: 9%	SUNASS
PROSPEROUS AGRICULTURAL SECTOR		Strengthen environmental management	Boost environmental performance	Environmental performance index	2014: 45.05/100	Yale Center for Environmental Law	
	Increase the percentage of solid waste disposed of in sanitary landfills		Percentage of solid waste disposed of in sanitary landfills	2014: 50%	MINAM		
	Expand access to credit for agricultural producers		Percentage of agricultural producers who obtain loans	2012: 10%	INEI		

1. Labor Market / Social Security Information System.
2. In MINSA's health care facilities and regional governments.
3. Robbery, theft, assault, fraud, blackmail, extortion, threats, or any other type of crime.

Results matrix for work on country systems

Strategic objectives	Expected outcomes	Indicator	Baseline 2016	Indicative targets	Periodicity
Strengthening of country fiduciary systems	Reduction in the fiduciary risks of entities that execute Bank projects	Index of implementation of the internal control system in the central government as determined by the Office of the Comptroller General of Peru	36%	50%	At the end of the strategy period
	Improvement in public expenditure monitoring and evaluation levels	Percentage of the national budget prepared based on results	62%	80%	At the end of the strategy period
	Improvement in the profiles of skills, management capacity, and management of new information technologies by procurement operators	Percentage of accredited operators	83%	100%	At the end of the strategy period
	Modernization of the public procurement system	MAPS global indicator value (1)	2.09	2.40	At the end of the strategy period
Increase in the operational efficiency of the Bank portfolio	Update of the SIAF project module used for all Bank-financed loan operations in Peru	Percentage of IDB operations that use applications to strengthen the SIAF I project management module	5%	25%	At the end of the strategy period
Use of the country fiduciary systems	Shopping	Percentage of IDB operations that use framework agreements and reverse auctions	47%	100%	At the end of the strategy period
	Partial national competitive bidding (NCB)	Percentage of IDB operations that use partial NCB	0%	100%	At the end of the strategy period
	Advanced national competitive bidding (NCB)	Percentage of IDB operations that use advanced NCB	0%	100%	At the end of the strategy period
	Individual consultants	Percentage of IDB operations that use individual consultants	0%	100%	At the end of the strategy period

1 Explanatory note: In the event that the new MAPS-OECD country system assessment methodology modifies the scoring scale for results, an equivalent scale will be adopted and, if necessary, the target will consider that at least 80% of the MAPS indicators have been fully met (80% of the assessment without red flags).

ANNEX III: ECONOMIC AND SOCIAL INDICATORS

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Social indicators										
Population (millions)	28.2	28.7	29.1	29.6	29.8	30.1	30.5	30.8	31.1	31.5
Life expectancy at birth (years)	73.0	73.2	73.4	73.6	73.8	74.1	74.3	74.5	74.8	
Adult literacy (%)	89.6					93.8		93.7	94.4	
Unemployment (%) 1/	8.5	8.3	8.4	8.0	7.7	7.0	5.9	6.0	6.4	6.8
			<i>(Percentage change or otherwise indicated)</i>							
Production and Prices										
Real GDP	8.5	9.1	1.0	8.5	6.5	6.0	5.8	2.4	3.3	
CPI (Average)	1.8	5.8	3.0	1.5	3.4	3.7	2.8	3.2	3.5	3.6
CPI (EOP)	3.9	6.7	0.3	2.1	4.7	2.7	2.9	3.2	4.4	3.2
External Sector										
Exports	17.9	10.4	2.0	-37.8	135.6	2.2	-9.6	-7.8	-13.4	
Imports	32.0	45.2	-14.8	-34.6	134.1	10.4	3.3	-3.1	-8.9	
Current account balance (% GDP)	1.5	-4.4	-0.5	-2.4	-1.8	-2.7	-4.3	-4.1	-4.9	
International reserves (US\$ bill)	27.7	31.2	33.2	44.2	48.9	64.0	65.7	62.4	61.5	61.7
Monetary Sector										
Monetary liquidity (M2) 2/	23.1	25.6	6.8	21.7	15.1	12.5	15.3	9.5	11.5	
Credit to the private sector 3/	30.0	33.9	5.0	16.7	21.6	13.3	18.3	13.2	13.9	
			<i>Percentage of GDP</i>							
Public Sector										
Revenue 4/	21.8	22.1	19.8	20.8	22.0	22.8	22.6	22.2	20.0	18.5
Primary expenditures 4/	17.1	18.1	20.1	19.9	18.8	19.6	20.9	21.5	21.2	20.0
Primary balance 4/	4.9	4.2	0.0	1.0	3.3	3.4	2.0	0.7	-1.0	-1.6
Balance (deficit -) 4/	3.1	2.5	-1.4	-0.2	2.1	2.3	0.9	-0.3	-2.1	-2.7
Debt										
Total external debt	32.5	28.7	28.9	29.5	28.5	31.4	30.8	31.8	35.5	
Total public debt	29.9	26.9	27.2	24.3	22.1	20.4	19.6	20.0	23.3	
Domestic	11.1	10.1	11.0	11.2	10.7	10.6	10.8	11.3	12.2	
External	18.8	16.8	16.1	13.2	11.4	9.8	8.8	8.7	11.1	
Memo items										
Nominal GDP (US\$ billion)	102	121	121	147	172	193	201	201	189	
	3,61			5,02		6,38				
GDP per capita (US\$)	1	4,209	4,166	1	5,770	6	6,581	6,490	6,027	

Source: Bloomberg, World Bank, International Monetary Fund, and local authorities.

1/ Corresponds to the LIMA metropolitan area.

2/ Liquidity of deposit institutions at the current exchange rate.

3/ Covers the deposit institutions.

4/ Corresponds to the nonfinancial public sector.

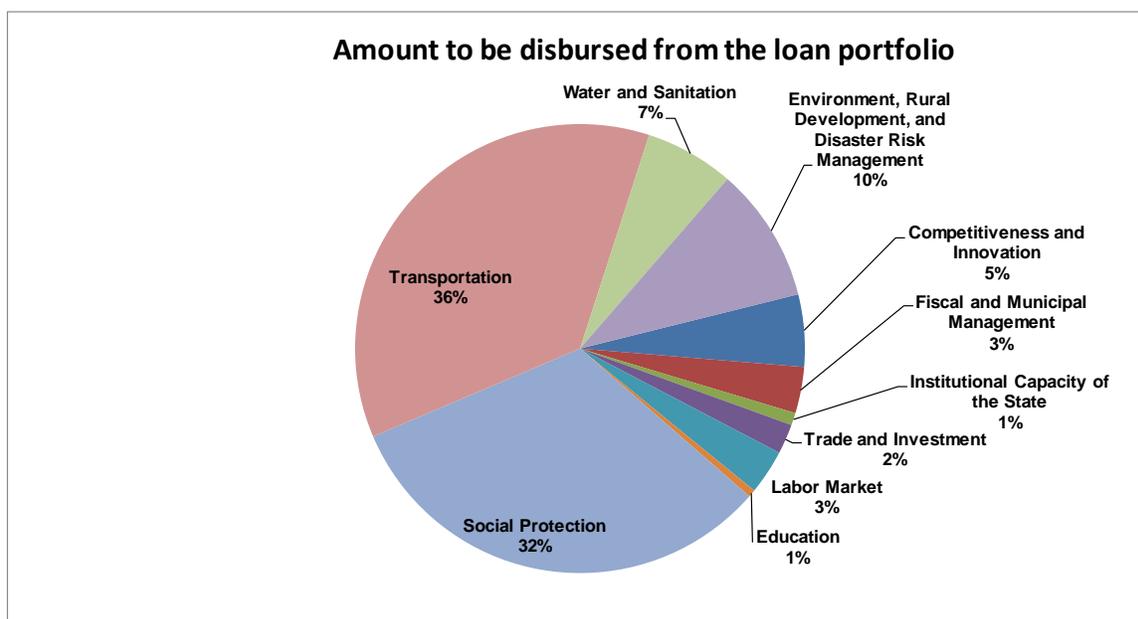
ANNEX IV: IDB GROUP OUTSTANDING LOAN PORTFOLIO

Outstanding portfolio of sovereign-guaranteed loans (as of 31 December 2016)

Loan number	Project name	Execution unit	Approved amount	Disbursed amount	% disbursed	Available amount	Date of last disbursement
2693/OC-PE	Innovation Project for Competitiveness	INNÓVATE PERÚ	35,000,000	26,478,176	76%	8,521,824	28-Sep-19
3700/OC-PE	Improved Levels of Productive Innovation at the National Level	INNÓVATE PERÚ	40,000,000	0	0%	40,000,000	22-Aug-23
2445/OC-PE	Modernization of the Public Financial Administration System to Improve Public Resource Programming, Execution, and Reporting	UCPS-MEF	20,000,000	16,460,834	82%	3,539,166	31-Dec-17
2703/OC-PE	Improvement of Territorial Public Investment Management	UCPS-MEF	20,000,000	7,528,681	38%	12,471,319	19-Apr-17
2991/OC-PE	Improving the Public Sector Payroll Budget Information Service	MEF	10,000,000	3,310,000	33%	6,690,000	20-Jul-19
3214/OC-PE	Tax and Customs Management Consolidation Projects	SUNAT - MEF	15,000,000	6,628,572	44%	8,371,428	29-Aug-20
2534/OC-PE	Program to Modernize the Justice Administration System in order to Enhance Services Provided to the Peruvian Population – Phase I	MINJUS / Judicial Branch	26,000,000	21,919,212	84%	4,080,788	29-Jun-18
2969/OC-PE	Improving the National Control System for Effective Public Management and Integrity	Office of the Comptroller General of Peru	20,000,000	15,755,284	79%	4,244,716	12-May-19
3546/OC-PE	Improvement of Foreign Trade Facilitation Services through the Single Window (VUCE)	MINCETUR	20,000,000	0	0%	20,000,000	29-Apr-21
3547/OC-PE	Improvement and Expansion of Employment Center Services for Formal Job Placement of Youth	MTPE	30,000,000	0	0%	30,000,000	28-Jun-21
2661/OC-PE	Program to Improve Early Education in Ayacucho, Huancavelica, and Huánuco	UE 118-PMEI	25,000,000	19,966,176	80%	5,033,824	14-Feb-18
3586/OC-PE	Management Modernization for Universal Health Coverage Program I	MEF	300,000,000	0	0%	300,000,000	
3587/OC-PE	Subnational Transportation Support Program (PATS)	Provias Descentralizado	50,000,000	0	0%	50,000,000	4-Apr-21
3373/OC-PE	Construction of Line 2 and the Avenida Faucett-Gambeta Section of the Lima and Callao Metro Basic Network	AATE	300,000,000	97,520,621	33%	202,479,379	30-Oct-19
2769/OC-PE	Lima-Canta-La Viuda-Unish Highway Rehabilitation and Improvement Project	Provias Nacional	70,000,000	63,014,000	90%	6,986,000	17-Dec-17
1836/OC-PE	Border Crossing Project at Desaguadero	MRE	3,993,000	3,993,000	100%	-	15-Dec-16
3881/OC-PE	Project for Improvement of the Huánuco-Conococha Highway, Huánuco-La Unión-Huallanca Segment (Route PE-3N) (North-South Mountain Highway)	MRE	80,000,000	0	0%	80,000,000	
2645/OC-PE	Cajamarquilla, Nievería, and Cerro Camote Project – Expansion of Water and Sewerage Systems in Sectors 129, 130, 131, 132, 133, 134, and 135 – Districts of Lurigancho and San Antonio de Huarochiri	SEDAPAL	100,000,000	43,195,526	43%	56,804,474	14-Feb-19
2759/OC-PE	Project for the Development of Solid Waste Management Systems in Priority Areas	MINAM	15,000,000	12,060,615	80%	2,939,385	14-Feb-17
3088/OC-PE	Project for the Improvement of the National Agricultural Innovation Program's Agricultural Innovation Strategic Services	INIA	40,000,000	2,820,200	7%	37,179,800	16-Apr-19
3370/OC-PE	Rural Land Cadastre, Titling, and Registration Project in Peru	UGPS - MINAGRI	40,000,000	932,932	2%	39,067,068	13-Feb-20
3272/OC-PE	Project to Improve the Agricultural Statistical Information System and the Agricultural Information Service for Rural Development in Peru	UGPS - MINAGRI	15,000,000	455,625	3%	14,544,375	13-Aug-20
Total outstanding loan portfolio		22	1,274,993,000	342,039,455	27%	932,953,545	

Sector distribution of the sovereign-guaranteed portfolio

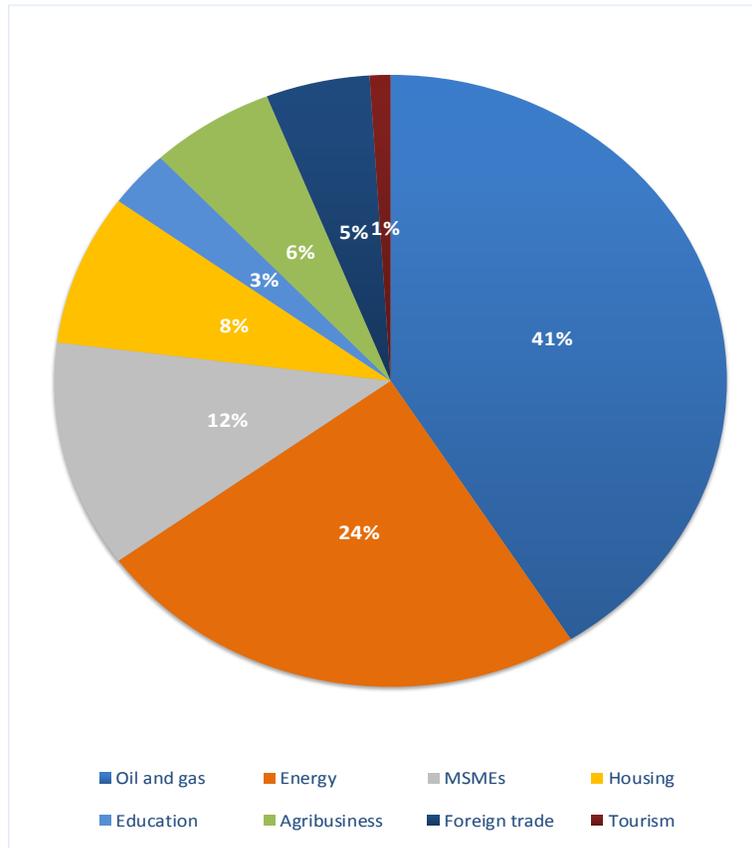
	Sector	Amount to be disbursed	%	Approved amount	%
CTI	Competitiveness and Innovation	48,521,824	5%	75,000,000	6
FMM	Fiscal and Municipal Management	31,071,913	3%	65,000,000	5
ICS	Institutional Capacity of the State	8,325,504	1%	46,000,000	4
TIN	Trade and Investment	20,000,000	2%	20,000,000	2
LMK	Labor Market	30,000,000	3%	30,000,000	2
EDU	Education	5,033,824	1%	25,000,000	2
SPH	Social Protection	300,000,000	32%	300,000,000	24
TSP	Transportation	339,465,379	36%	503,993,000	40
WSA	Water and Sanitation	59,743,859	6%	115,000,000	9
RND	Environment, Rural Development, and Disaster Risk Management	90,791,243	10%	95,000,000	7
	TOTAL	932,953,545		1,274,993,000	



IIC outstanding loan portfolio (US\$ millions)

Legacy	Project/Transaction Name	Total Exposure	Type of product
IDB	Peru LNG	272,174,400.00	NSG A-Loan
IDB	Chaglla Hydroelectric Power Project	147,751,100.00	NSG A-Loan
IIC	SCOTIABANK	40,000,000.00	IIC loan
IDB	Danper Trujillo S.A.C	37,258,000.00	NSG A-Loan
IDB	Banco Continental Subordinated Loan Facility	30,000,000.00	NSG A-Loan
IDB	RTFF - Banco Interamericano Finanzas (BIF) (Peru) Loan	20,000,000.00	TFFP Loan
IDB	Banco Interamericano de Finanzas	20,000,000.00	NSG A-Loan
IDB	Universidad San Ignacio de Loyola - Expansion	18,976,000.00	NSG A-Loan
IIC	SANTANDER	15,000,000.00	IIC loan
IDB	Colegios Peruanos	13,402,100.00	NSG A-Loan
IIC	CANCHAYLLO	6,229,440.00	IIC loan
IIC	BIF	6,000,000.00	IIC loan
IIC	HIDROCAÑETE	5,737,500.00	IIC loan
IIC	BIF	4,500,000.00	IIC loan
IIC	FINANCIERA CONFIANZA	4,000,000.00	IIC loan
IIC	AREQUIPA	4,000,000.00	IIC loan
IIC	BANCO FINANCIERO	2,500,000.00	IIC loan
IIC	MLP	2,500,000.00	IIC loan
IIC	MLP II	2,000,000.00	IIC loan
IDB	Caja Sullana subordinated	2,015,000.00	NSG A-Loan
IIC	EXFRUSUR	1,217,391.32	IIC loan
IIC	ICA PACIFIC	217,391.35	IIC loan
IDB	Banco Continental PCG Facility	80,000.00	NSG Guarantee
IDB	Banco Interamericano de Finanzas (BanBif)- MSME Downscaling	80,000.00	NSG Guarantee
TOTAL		655,638,323	

Risk distribution of the IIC portfolio



**ANNEX V: MANAGEMENT’S RESPONSE TO THE COUNTRY PROGRAM EVALUATION: PERU
2012-2016**

	Management’s response
<p>Recommendation 1</p> <p>Adopt a strategic approach focused on strengthening public management, encouraging the country to make deeper changes. The Bank should maintain and strengthen the work niche where it has positioned itself, and continue to support the improvement of public management, broadly defined. That support should be given by increasing the depth of the reforms and concentrating on a smaller and more select number of areas based on a sound diagnostic assessment of the capabilities of the Peruvian government, identifying the priority areas lagging most, followed by dialogue with the government authorities.</p>	<p>Agree.</p> <p>The country development challenges (CDC) diagnostic report on the Bank’s country strategy and dialogue with the government has found that Peru faces challenges in terms of execution of public expenditure, institutional coordination and responsiveness of the government, transparency and accountability, and efficiency in tax revenue collection. These challenges lower the effectiveness and quality of the delivery of public goods and services, jeopardize citizen confidence in institutions, and affect the country’s business climate and growth potential.</p> <p>Based on this diagnostic assessment and country dialogue, during the 2017-2021 country strategy period the IDB Group will emphasize support to the country in the area of public management, which is a priority of the Peruvian government. This support will focus on institutional capacity-building for basic service delivery with greater efficiency and quality standards through (i) better institutional coordination for the delivery of public goods and services; (ii) consolidation of the institutional architecture of the National Public Investment System (SNIP); (iii) strengthening of the formulation, structuring, and implementation of investment projects through public-private partnerships (PPPs); (iv) simplification of procedures and improvement of regulatory quality; and (v) use of the legal and institutional framework for integrity and transparency.</p> <p>The new strategy will emphasize improved management in key sectors such as health, water and sanitation, and citizen security.</p>
<p>Recommendation 2</p> <p>Building on previous success, increase support for the country in institutional areas of social inclusion and poverty reduction. These areas are still priorities in</p>	<p>Agree.</p> <p>During the 2017-2021 strategy period, the IDB Group will continue to prioritize technical capacity-building at the Ministry of Development and Social Inclusion (MIDIS) through support for</p>

<p>Peru, even though it has made great strides. The Bank possesses capacity to work on these issues, as demonstrated in 2011 when it became the main partner for addressing them. Yet this relationship has weakened in recent years. The Bank should extend an offer to the government to redouble its efforts to address these areas by helping it strengthen MIDIS and improve the social protection system.</p>	<p>implementation of the recommendations derived from the impact assessments of existing conditional cash transfer programs. The Bank will also work with the government to map out the urban poverty reduction strategy. Specifically, the Bank will work to expand the coverage and quality of health and water and sanitation services, as well as support MIDIS in mapping out an urban poverty reduction strategy.</p>
<p>Recommendation 3</p> <p>Strengthen work with the private sector, selecting the projects to finance more carefully, making greater efforts to expand its population of potential clients, and improving the evaluability of its operations. The IIC should finance projects that have financial additionality and are relevant for the country's development. For this, the IIC needs to make itself more widely known in the Peruvian private sector, and thus expand its portfolio of potential clients to include more firms without a large market share. Lastly, the IIC needs to substantially improve the evaluability of its projects, so that it can demonstrate its additionality and effectiveness.</p>	<p>Agree.</p> <p>Inter-American Investment Corporation (IIC) is working to implement the new Development Effectiveness Framework (DEF). The DEF includes the ex ante application of DELTA to analyze projects across several different dimensions including economic development and financial additionality. Use of this tool will make it possible to finance projects that have financial additionality and relevance for the country's development and do not crowd out private investment. DELTA also includes an evaluability analysis, so substantive improvements are expected in the evaluability of operations.</p> <p>The IIC is designing the country presence strategy and strategy for working with SMEs. These strategies, respectively, will make it possible to improve knowledge of the IIC's work in Peru and expand the number of SME beneficiaries.</p>
<p>Recommendation 4</p> <p>Continue supporting PPP projects, but with clear rules on such involvement established before the fact. The IDB Group should set the terms on which it will participate in this type of project financing the public sector, private sector, or both. It should also have transparent guidelines in place that determine the scope and the time frames of its participation, financial and nonfinancial, in each case. That way, such projects can be supported without adding uncertainty to the concession processes, and avoiding conflicts of interest.</p>	<p>Partially agree.</p> <p>The IIC is developing guidelines to establish an intervention model that is more structured and coordinated with the IDB, to optimize synergies between the public and private sectors in the structure and financing of PPPs.</p> <p>However, in Management's view, given the features of the projects and differences among the sectors where opportunities exist for structuring PPPs, establishing a single set of conditions, time frames, and type of participation for predetermined cases is inadvisable.</p>

ANNEX VI: DEM

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX	
<p>In August 2008, the Board of Directors approved the Development Effectiveness Framework (GN-2489) to increase the evaluability of all Bank development products.</p> <p>The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."</p>	
<p>COUNTRY STRATEGY: PERU</p> <p>STRATEGIC ALIGNMENT Refers to the degree to which the design and objectives of the CS are consistent with the country development challenges and with the government's development plans and priorities.</p> <p>EFFECTIVENESS This measures whether the country strategy is likely to achieve its intended objectives, through an examination of three dimensions: (i) the quality of the diagnostics on which Bank action is based in each area of work; (ii) the quality of the results matrix for the strategy; (iii) the use and build up of country systems.</p>	
Effectiveness dimensions	
I. Country Diagnosis - Country Development Challenges (CDC)	Yes/No
- The CDC is comprehensive / holistic / complete	Yes
- The CDC clearly identifies the main development challenges	Yes
- The CDC presents magnitudes of the main development challenges that are based on empirical evidence	Yes
II. Priority Area Diagnostics	%
- That clearly identify and dimension, based on empirical evidence, the priority area's specific constraints and challenges	100%
- That clearly identify and dimension, based on empirical evidence, the main factors or causes contributing to the specific constraints and challenges	80%
- That provide corresponding policy recommendations	80%
III. Results matrix*	%
- The strategic objectives are clearly defined	100%
- The expected outcomes are clearly defined	89%
- The strategic objectives and expected results that are directly related to the main constraints identified in the Diagnosis	100%
- The indicators are outcome indicators and are SMART	86%
- The indicators have baselines	100%
IV. Vertical logic	Yes/No
- The CS has vertical logic	Yes

* The Results Matrix is composed by indicators that are meaningful to, and capture progress towards, the expected results. The expected results stem from the strategic objectives.

CS Diagnostic: As part of the country strategy 2017-2021 a country development challenges diagnostic was presented (electronic link). The CDC diagnostic is comprehensive and based on empirical evidence. The CDC diagnostic identifies three priority areas for the Bank's intervention productivity, quality of public institutions and social mobility. The diagnostic clearly identifies and dimensions, based on empirical evidence, 90% priority area's specific constraints and challenges. The diagnostic clearly identifies and dimensions, based on empirical evidence, the main factors or causes contributing to the specific constraints and challenges for 80% of the priority areas. The diagnostic provides policy recommendations for Bank actions that are based in empirical evidence, for 80% of the priority areas.

Results matrix: The section of the results matrix corresponding to the new strategic area includes nine strategic objectives for Bank action, 19 expected results and 21 indicators to measure progress. 100% of the Strategic Objective(s) are clearly specified. 89% of the expected result(s) are clearly specified. 100% CS Objectives are directly related to the main constraints identified in the Diagnosis. 86% of the indicators used are SMART. 100% of the indicators have baselines.

Country Systems: Diagnostics are available for all financial management sub-systems. We will continue to use 100% of the sub-systems of budget and treasury, partly the sub-system of accounting and the reports, and the sub-system of external control of at least one pilot (5%) of the projects of the portfolio. In terms of acquisitions, there is a diagnosis of the information system available; We are expected to work on strengthening all sub-systems acquisitions. Vertical logic. The CS has vertical logic.

Risks. *The main risks facing the implementation of the country strategy are related to: (i) the strategy to reduce foreign currency indebtedness in favor of an increase in the use of local currency; (ii) the complex institutional coordination that hinders the design and implementation phases of public investment; and (iii) weak management of some of the executing agencies for the implementation of investment projects. The CS identifies specific mitigation and monitoring measures for each risk.*