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PERU

**IDB GROUP COUNTRY STRATEGY WITH PERU
2022-2026**

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ABBREVIATIONS

AFSP	Administración Financiera del Sector Público [Public Sector Financial Administration]
BCRP	Central Reserve Bank of Peru
CDC	Country Development Challenges
CGR	Contraloría General de la República [Office of the Comptroller General of Peru]
CRF	Corporate Results Framework
ELSA	Espacios laborales sin acoso [harassment-free workplaces]
ENA	Encuesta Nacional Agrícola [National Agricultural Survey]
ENP	Estrategia Nacional de Prevención [National Prevention Strategy]
GDP	Gross domestic product
ICPR	Independent Country Program Review
IMF	International Monetary Fund
INEI	Instituto Nacional de Estadística e Informática [National Institute of Statistics and Information Technology]
IPSAS	International Public Sector Accounting Standards
LAC	Latin America and the Caribbean
LGBTQI+	Lesbian, gay, bisexual, transgender, queer, intersex, and other
MEF	Ministry of the Economy and Finance
MIMP	Ministry of Women and Vulnerable Population Groups
MINAM	Ministry of the Environment
MINCETUR	Ministry of Foreign Trade and Tourism
MININTER	Ministry of the Interior
MINSA	Ministry of Health
MSMEs	Micro, small, and medium-sized enterprises
NCB	National competitive bidding
OECD/MAPS	Organization for Economic Cooperation and Development/ Methodology for Assessing Procurement Systems
OVE	Office of Evaluation and Oversight
PBL	Policy-based loan
PCM	Presidency of the Council of Ministers
PNCP	Plan Nacional de Competitividad y Productividad [National Competitiveness and Productivity Plan]
PNIC	Plan Nacional de Infraestructura para la Competitividad [National Infrastructure Plan for Competitiveness]
PPP	Public-private partnerships
SEACE	Sistema Electrónico de Contrataciones del Estado [Electronic Government Procurement System]
SIS	Seguro Integral de Salud [Comprehensive Health Insurance]
SMEs	Small and medium-sized enterprises
SNP	Sistema Nacional de Pensiones [National Pension System]
SUNAFIL	Superintendencia Nacional de Fiscalización Laboral [National Superintendency of Labor Inspection]

EXECUTIVE SUMMARY

Country context	<p>Peru has been an economic and social success story over the past two decades, thanks to the implementation of structural reforms and a favorable external context. However, in the last number of years, growth did not translate into productivity gains. More recently, the COVID-19 crisis created overlapping shocks which harmed the economy and eroded the social gains of the past decade. Although the economy recovered in 2021, social indicators have not reached their prepandemic values. Overcoming these challenges in a context of renewed COVID-19 outbreaks and global uncertainty requires undertaking policies and programs that respond to the impact of the crisis and address long-term issues, with a view to deepening the country's social, productive, and institutional advances.</p>
IDB Group presence in Peru	<p>The IDB Group country strategy with Peru for 2017-2021 prioritized three strategic areas: (i) productivity; (ii) institutional strengthening and delivery of basic services; and (iii) environmental sustainability and climate change. In that period, the Bank approved 26 sovereign-guaranteed loan operations for US\$2,986.7 million, 44.8% of which in the form of investment loans and the remaining 55.2% in the form of policy-based loans. Disbursements in the period totaled US\$2,060.9 million. In addition, the Bank approved 84 technical cooperation operations for a total of US\$39.4 million and 3 investment grants for a total of US\$21.7 million. IDB Invest approved 21 operations for US\$1.471 billion. IDB Lab approved 8 technical cooperation operations for US\$8.7 million.</p>
Priority areas	<p>The objective of the country strategy for 2022-2026 is to support Peru in achieving sustained growth, so as to foster social progress, in a context of environmental sustainability and under a decentralized approach that prioritizes rural areas. The country strategy will provide for the same strategic areas as the previous strategy, but with different approaches, notably including capacity transfer at the regional level, support for work in the Amazon region, and migrant support policies. Issues of gender and diversity, climate change and sustainability, institutional capacity and rule of law, and digitalization will be addressed in crosscutting fashion.</p>
Projected lending scenario	<p>The level of sovereign-guaranteed approvals and disbursements for the 2022-2026 period is estimated at US\$3.000 billion and US\$2.800 billion respectively, in addition to IDB Invest and IDB Lab resources. Under these assumptions, the debt to the Bank would represent 7% of the public external debt at the end of the period.</p>
Preliminary implementation considerations	<p>The active portfolio is an integral part of the new country strategy. The Bank will address the Peruvian government's requirement to work with, and transfer capacities to, the subnational regions and will work closely with the executing agencies. The current context in Peru will demand flexibility, innovative tools, and technical assistance resources to provide relevant solutions to the country's challenges in a highly volatile context. Synergies between the IDB, IDB Invest, and IDB Lab will continue to be harnessed, and the Bank will coordinate with other donors.</p>
Risks	<p>The main risks are associated with: (i) the complexity of interagency coordination at the subnational level in view of the highly volatile political environment, which has made it difficult to implement public policies; (ii) shifting priorities as a result of a turnover in authorities; and (iii) execution challenges. While the country projects robust economic performance over the coming years, this growth will depend both on the country's ability to adequately address the lingering challenges of the pandemic and on the evolving international context, where a persistence of Russia's war on Ukraine could worsen inflationary pressures.</p>

I. COUNTRY CONTEXT¹

- 1.1 **Peru has been an economic and social success story in the region.** The country made a major transition from the economic instability of the 1980s to a path of sustained growth after the turn of this century. Between 2000 and 2019, the Peruvian economy expanded at an average annual rate of 4.8%, while growth in Latin America and the Caribbean (LAC) averaged 2.6% over the same period. In those years, the country's per-capita gross domestic product (GDP) rose from US\$1,956 to US\$7,028, and Peru became an upper middle-income country (based on the World Bank ranking). This was the result of a series of structural reforms made in the 1990s, coupled with favorable external conditions in the 2000s. The reforms boosted the role of the private sector in the delivery of public goods, strengthened public finance management, granted independent status to the Central Reserve Bank of Peru (BCRP) while instituting management improvements, and facilitated greater trade and financial openness. At the same time, the boom in commodity prices between 2004 and 2013 helped to improve the fiscal accounts, such as by gradually reversing the fiscal deficit and reducing the public debt from 52% of GDP in 1999 to 26.6% of GDP in 2019. The latter development enabled the country to obtain investment grade status in 2009 and brought about a reduction in sovereign risk.²
- 1.2 **Before the pandemic, the Peruvian economy had begun to slow down.** The country's economic growth declined from an average of 6.2% between 2004 and 2013 to an average of 3% between 2014 and 2019.³ This slower pace of growth is partly a consequence of lower aggregate economic productivity, which in turn results from an unfinished agenda in the areas of innovation, digitalization, financial inclusion, and human capital and labor market development, among others. The contribution of productivity to growth went from an average of 1.5 percentage points between 2004 and 2013 (excluding 2009 due to the global financial crisis) to -0.2 percentage points between 2014 and 2019.⁴
- 1.3 **The pandemic is one of Peru's worst crises in recent history.** In 2020, the Peruvian economy contracted by 11%, the sharpest drop in all of LAC and one of the sharpest worldwide. Once the first case was identified, tight restrictions on movement were put into place along with quarantine regulations that ranked among the strictest anywhere. To cushion the economic impact, the government implemented a series of steps. On the fiscal side, it suspended the fiscal rules for 2020 and 2021 and provided for the use of fiscal savings (Fiscal Stabilization Fund: 3% of GDP). This enabled the government to obtain part of the space needed to, among other things, apply tax relief measures (2.6% of GDP), grant subsidies to households and workers (2.3% of GDP), and implement government-guaranteed credit programs (10.8% of GDP).⁵ Monetary policy supported this fiscal effort. The BCRP lowered its policy rate from 2.25% in February 2020 to 0.25% in April 2020,

¹ The Country Development Challenges document (CDC) (web link) provides a more detailed description and includes the sources of the data.

² BCRP statistics, IMF's World Economic Outlook, and World Bank's World Development Indicators.

³ BCRP statistics.

⁴ The Conference Board. Total Economy Database.

⁵ Ministry of Economy and Finance (2021). Multiyear Macroeconomic Framework (MMF) 2022-2025.

bringing it to an historical low; at the same time, the BCRP actively intervened in the financial and foreign exchange markets.⁶

- 1.4 **The COVID-19 crisis has deepened the social gaps in the country.** Between 2004 and 2019, monetary poverty fell from 58.7% to 20.2%. However, in 2020, as a result of the pandemic, monetary poverty rose to 30.1%, a level not seen since 2010. Moreover, there are persistently significant geographic inequalities, as rural poverty, at 45.7%, is almost double the rate of urban poverty (26%).⁷ In addition, informal employment grew from 72.7% in 2019 to 76.8% in 2021 and is higher in rural areas (95.3%) than in urban ones (71.4%). At the same time, there are gender, ethnicity, and vulnerable population gaps in terms of labor market integration. For example, women are more likely to be self-employed (38%; men: 35%), have informal jobs (75%; men: 68%), and bear a greater burden of household care, which limits their development and employment prospects.⁸ These lags in job quality are also seen in the degree of informal employment in indigenous and Afro-Peruvian communities (89% and 82%, respectively).⁹ Lastly, vulnerable groups such as the LGBTQI+ population and persons with disabilities (77% of whom are economically inactive) face greater difficulties in adequately joining the labor force.
- 1.5 **In addition to the social lags of women, minorities, and diverse groups, Venezuelan migrants are vulnerable.** As of 2020, more than 1.2 million Venezuelans had migrated into Peru.¹⁰ Most of them are of active employment age and have more years of schooling than the Peruvian average, which would represent an opportunity for them to contribute to the Peruvian economy.¹¹ In spite of this, prior to the pandemic, 94% of Venezuelan migrants held informal jobs and the majority had no access to housing or health insurance. The pandemic's arrival made their living conditions harder since they were often employed in sectors affected by the health restrictions, and they were not on the rolls to access social programs.¹²
- 1.6 **In the medium term, the outlook for an economic recovery is optimistic, but Peru faces challenges in terms of institutional quality, governance, and a productive structure able to create new sources of long-term growth.** After expanding by 13.5% in 2021, the Peruvian economy is expected to grow at a rate of approximately 3% over the country strategy period (IMF, 2022). To ensure the sustainability of growth in the medium term and continue to move forward on the path of social development, the country needs to boost productivity as well as public and private investment. This will necessarily require better management, greater institutional capacity, and stronger rule of law with a view to providing quality public services, promoting human capital improvements, and attracting private investment. In turn, a rise in productivity should take place in the context of

⁶ Central Reserve Bank of Peru (2021). Inflation Report - June 2021.

⁷ In 2021, poverty declined to 25.9% nationwide (22.3% and 39.7% in urban and rural areas, respectively).

⁸ In 2020, 6.6 million women provided care services, of whom 2 million were economically inactive.

⁹ These two data are for 2020 rather than 2021, since the National Institute of Statistics and Information Technology (INEI) does not publish these statistics until the second half of the year.

¹⁰ Second-largest migrant host country after Colombia.

¹¹ BBVA Research (2019) Inmigración venezolana a Perú: características e impactos macroeconómicos.

¹² World Bank (2020). Migrantes y Refugiados Venezolanos en El Perú: El Impacto de la Crisis de la Covid-19.

conservation and sustainable use of natural resources so as to protect biodiversity and the environment.

- 1.7 **Coupled with this, domestic and international sources of uncertainty add to the country's development challenges.** The economic recovery depends on the progress made in controlling the pandemic both domestically and internationally. Thus, the favorable outlook stemming from better commodity prices obtained by the country could be overshadowed by an outbreak and spread of new COVID-19 variants. Moreover, the domestic political tensions between executive and legislative branch representatives,¹³ which have persisted since 2016, could erode market and investor confidence in the country's economic situation, as well as diminish the capacity and effectiveness of public policies. There is also uncertainty regarding natural disasters that could affect the country. The domestic sources of uncertainty are compounded by Russia's war on Ukraine. In addition to human losses, this war creates inflationary pressures and, if it persists, could lead to a trade imbalance and disruptions in the delivery of goods for Peru. For example, a drawn-out war could increase the risk to the supply of inputs for the agricultural industry.¹⁴
- 1.8 **The IDB Group country strategy 2022-2026 will address the country's main development challenges¹⁵ through three priority areas.** These areas are: (1) productive development; (2) environmental sustainability and climate change; and (3) institutional strengthening and delivery of basic services. The interventions in these three areas will be served by the support mechanisms of the IDB Group, including new loan operations, both sovereign- and non-sovereign guaranteed, and guarantee operations, knowledge products, technical cooperation operations for knowledge transfer, and the existing project portfolio with the country. In the latter case, the legacy portfolio will be an integral part of the new country strategy, requiring continued work on improving execution in aspects such as training, planning, and management.

II. IDB GROUP PRESENCE IN THE COUNTRY

A. Implementation of the 2017-2021 strategy

- 2.1 **The IDB Group Country Strategy with Peru (2017-2021) (document GN-2889) was aimed at helping the country achieve sustained growth so as to foster social progress in a context of environmental sustainability.** To this end, it prioritized 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. Gender and diversity issues were mainstreamed in these three

¹³ Between July 2016 and the date of this document, the Peruvian Legislature approved one motion for presidential impeachment out of a total of six impeachment motions voted on, while the country's president issued a decree dissolving the Legislature.

¹⁴ According to the Ministry of Foreign Trade and Tourism (MINCETUR), there are seven key inputs whose supply could be affected by the current conflict: urea, diammonium phosphate, potassium chloride, ammonium nitrate, intermediate goods for the steel industry, steel products, and wheat.

¹⁵ These were identified in the CDC as: (i) productivity increase, (ii) promotion of agricultural development and environmental sustainability; and (iii) institutional strengthening.

- strategic pillars, and while institutional capacity and rule of law issues and climate change and environmental sustainability issues were addressed as priority pillars, efforts were made to mainstream them in the other pillars.
- 2.2 **The country strategy projected a financing envelope of US\$1.500 billion for the public sector; approvals doubled this estimate to support management of the pandemic and prevent investment interruptions at a time of political instability.** During the 2017-2021 period, Peru went through five presidents and repeated changes of Cabinet, layering political crises on top of the COVID-19 crisis. Given this context, the Bank's flexible and close support was instrumental in ensuring the continuity of technical dialogue, public investment, and the reform agenda, as pointed out in the Independent Country Program Review (ICPR) issued by the Office of Evaluation and Oversight (OVE). This translated into a demand for sovereign-guaranteed loans for a total of US\$2,986.7 million, comprised of 21 investment loans (US\$1,336.7 million, or 44.75%) and 5 policy-based loans (PBLs) (US\$1.650 billion, or 55.25%), including 2 PBLs with a US\$1.100 billion deferred drawdown option for US\$1.100 billion in 2021.¹⁶ In addition, the Bank approved 84 technical cooperation operations for a total of US\$39.4 million and 3 investment grants for US\$21.7 million, with an emphasis on combating deforestation and climate change, social investment, and water and sanitation.
- 2.3 **During the period, IDB Invest also expanded its presence in the country: approvals doubled (for a total of US\$1.471 billion),¹⁷ and new markets were opened.¹⁸** A total of 21 operations were approved during the period. In all, 46% of these were transactions aimed at supporting access to finance through the financial sector, followed by the transportation (22%), agribusiness (12.5%), energy (12.5%), urban development and housing (4%), science and technology (2%), and corporate (1%) sectors. In addition, IDB Lab approved eight operations for a total of US\$8.7 million, mainly in value chains, regional economic development, and financial inclusion and innovation.
- 2.4 **The IDB Group expanded and became a much more relevant strategic partner for Peru.** As of January 2022, the country's public debt to the Bank accounted for 31% of the total debt to multilaterals, 5.8% of the external debt, and 3.3% of the total public debt.

B. Main outcomes of the IDB Group country strategy with Peru 2017-2021

(i) Productivity

- 2.5 **In labor markets, support was provided for adequate integration into the formal sector as well as the elimination of harassment in the workplace.** One of the challenges was institutional strengthening to promote integration into the formal workforce, with an impact on the most vulnerable population groups. The Bank supported the country in improving and expanding services at employment centers for formal job placement of young people in seven regions.¹⁹ Worth noting

¹⁶ The results of the Independent Country Program Review Peru 2017-2021 (OVE) describe one IDB Group prior to the pandemic and quite a different one following its onset, showing that 2021 was a year in which the Bank provided a great deal of support to the country through new instruments and became a more relevant financial partner.

¹⁷ This amount includes operations approved during the period but not having yet reached financial closing.

¹⁸ Telecommunications and technology, inclusive banking, and urban development.

¹⁹ Arequipa, Ica, Lambayeque, La Libertad, Piura, San Martín, and Metropolitan Lima (PE-L1152).

in this regard is the improvements made in the physical space and service model at the employment centers in these regions. In addition, job board offerings were expanded in 2020 in line with hiring needs, integrating the digital job placement mechanisms of all regions. This made it possible to guarantee an average of 8,000 new job vacancies each month during a critical year. The job board improvements continued in 2021 when an artificial intelligence engine was introduced, putting Peru at the forefront in the region in the use of digital employment platforms through the implementation of job matching. IDB Lab also provided support for this task, working to improve the job skills of the vulnerable population, with a gender and diversity approach. In addition, IDB Invest operations supported the creation of approximately 70,000 jobs and trained more than 140,000 people.²⁰ Moreover, support was given for development of the digital tool ELSA (espacios laborales sin acoso) [harassment-free workplaces] by GenderLab, to implement a culture of evidence-based prevention of sexual harassment in the workplace. In social security, the Bank supported the implementation of a Social Protection Commission (CPS) and the preparation of studies and proposals to reform the Peruvian pension system.

- 2.6 **In competitiveness and innovation, support was provided for the innovation market as well as the digital capacities of micro, small, and medium-sized enterprises (MSMEs).** The main challenges were the low level of private investment, limited human capital available for science, technology, and innovation, poor coordination among innovation system agents, and pronounced weaknesses in the supply of technology and business support services. The program,²¹ executed between 2012 and 2019, helped to consolidate the technological innovation market with a view to boosting competitiveness through business innovation contests, support for dynamic startups and incubators, scientific research and equipment, and support for technological extension activities. In 2016, the Bank approved a project²² aimed at continuing with, and increasing the volume of, matching grants for business innovation, introducing new instruments to support technological extension, collaborative innovation, and promotion of innovation systems at the subnational level. The project helped to boost the digital and quality capabilities of MSMEs, which was a challenge exacerbated by the pandemic.²³ In addition, IDB Invest supported the telecommunications and technology sector with a view to expanding access to mobile broadband and technology services, including in small towns and rural villages. In 2020, nearly two million people benefited by obtaining new access to a mobile network,²⁴ while support was provided for over a million MSMEs from 2017-2021. IDB Lab supported the introduction of digital technologies and tools in productive agroindustrial sectors, optimizing the production processes under an innovate-to-include approach.

²⁰ These outcomes were obtained through operations in the nontraditional agricultural, education, and telecommunications sectors.

²¹ Innovation Project for Competitiveness (PE-L1068, US\$100 million).

²² Project for Improvement of Productive Innovation at the National Level (PE-L1162, US\$100 million).

²³ Thus, as of 2021 the project had entered into 608 contracts for consulting and technology services to reduce productive, quality, and digitalization gaps among MSMEs. In addition, it helped set up five bootcamps in the country for intensive and accelerated programming training.

²⁴ Internet for Everyone, 12361-01.

- 2.7 **Over the country strategy period, the IDB Group was a relevant financing and technical assistance partner in the areas of competitiveness and infrastructure.** The IDB Group provided support in preparing the National Competitiveness and Productivity Plan (PNCP) and the National Infrastructure Plan for Competitiveness (PNIC). Technical assistance was provided to the Consejo Nacional de Competitividad y Formalización [National Competitiveness and Formalization Council] (CNCF), along with inputs based on international experience for preparation, public discussion, and publication of the PNCP. In the PNCP, measures were identified in line with the priority policy objectives and support is being provided for actions aimed at moving forward with their implementation, monitoring, and evaluation. As part of the priority objectives, the PNIC was approved, paving the way for the development of an investment agenda to assist in closing the infrastructure gap. To this end, support was provided for quantifying the infrastructure gaps in transportation, communications, irrigation, electricity, water, sanitation, health, and education. In addition, support was provided to various sectors with a view to properly identifying and prioritizing the project portfolio, considering internal gaps, sector policy guidelines, and budgetary restrictions, among other issues.
- 2.8 **In transportation, it is worth noting the support provided by the IDB Group to address challenges in terms of improving the quality and accessibility of the road infrastructure.** The interventions tackled existing challenges in terms of the quality and accessibility of the country's road infrastructure and helped to reduce transportation costs and travel times, boosting competitiveness. The interventions achieved improvements in the quality of the national road network infrastructure and in the local road network. With regard to rural transportation, the Bank is supporting the goal of rehabilitating 2,200 kilometers (km) of roads and maintaining an additional 2,000 km. The program in execution also includes actions underway to strengthen the capacities of local governments. In 2021, the Bank approved an operation for road improvements in the departmental road network,²⁵ setting a goal of 5,000 km of local roads. IDB Invest financed projects to improve connectivity, such as expansion of the Lima Airport and construction to complete Road Network No. 4 and the Chimbote bypass.
- 2.9 **In energy, the public and private windows supported institutional strengthening and energy diversification to advance toward a more sustainable energy matrix.** One of the challenges for the sector was the slowdown in the growth of power production between 2017 and 2019.²⁶ The IDB Group approved two operations²⁷ focused on institutional strengthening in the electricity sector to support the integration of energy planning, modernization of State-owned enterprises, and strengthening of regulation and supervision of the national electricity market. In addition, it sought to prepare the groundwork for the sector to migrate toward an orderly energy transition and to consolidate regional integration. Furthermore, IDB Invest financed two operations: one was aimed at building a second natural gas distribution network in nine districts of the city of

²⁵ PROREGION program.

²⁶ It fell by 7% in 2020, from 52,889 to 41,187 GWh. Energy access was unequal in urban and rural areas (96.8% and 79.1%, respectively).

²⁷ Program for Efficient and Sustainable Management of Peru's Energy Resources (PROSEMER) (PE-X1007) and Support for Peru's Energy Sector Transformation (PE-T1449).

Lima and the Constitutional Province of Callao,²⁸ while the other was designed to expand wind energy and thus contribute to the government's objective of diversifying and enhancing the security of the country's energy matrix.²⁹

- 2.10 **In foreign trade, the IDB Group has played a relevant role in promoting improvements by strengthening and upgrading the foreign trade single window (VUCE).** The IDB Group has worked with the Port Authority in supporting the development of a smart port in Callao, preparing a road map to automate and digitalize manual processes. In regional integration, it has assisted the Pacific Alliance. IDB Invest promoted the financing of transactions in the amount of US\$274 million.
- 2.11 **In education, the IDB Group supported quality improvements in the higher education segment.** During the previous country strategy period, higher (university and vocational) education was of poor quality and limited relevance. In view of this, in 2018, the Bank supported and financed a public investment program³⁰ that will be in execution until 2023, to improve the quality and relevance of higher education. The program has included conducting a census of infrastructure and equipment at all public universities and vocational institutes, gleaning information to identify gaps and target new investments. In addition, 14 competitive grants have been provided for universities and vocational institutes with a view to improving management capacity and offering virtual education. IDB Invest financing benefited approximately 140,000 students through operations to support employment initiatives in the agriculture sector and in secondary and higher education for providing quality teaching and modern infrastructure at affordable prices.³¹
- 2.12 **In housing and urban development, the IDB Group worked on enhancing historic centers for adequate conservation of the nation's heritage.** The main challenge has been the highly precarious state of cities and urban areas. With a view to strengthening management of the urban heritage, the Bank, together with the Spanish Agency for International Development Cooperation (AECID), has implemented the Patrimonio Vivo [Living Heritage] program in Peru in the cities of Ayacucho (2019), Trujillo (2021), and Arequipa (2021). Planning processes developed as part of the program have resulted in strategic heritage plans for the historic centers of participating cities.

(ii) Institutional strengthening and delivery of basic services

- 2.13 **In terms of strengthening public management, integrity, and transparency, it is worth noting the contribution of the IDB Group to progress on digital government and administrative simplification.** During the previous country strategy period, the Bank supported the creation of the Public Integrity Secretariat in the Presidency of the Council of Ministers (PCM)³² and the strengthening and modernization of the Office of the Comptroller General of Peru (CGR). In addition,

²⁸ Gas Natural de Lima y Callao S.A – (Calidda), 13146-01.

²⁹ Enel Green Power Peru, 13446-01.

³⁰ PE-L1227.

³¹ Universidad San Ignacio de Loyola University Expansion (PE-L1141); Colegios Peruanos: Quality Private Education for Emerging Social Classes in Peru (PE-L1120); Danper II (12180-01).

³² PE-L1222, Project to Improve and Expand Support Services for the National Delivery of Services to Citizens and Businesses.

- it helped to consolidate State services in the gov.pe platform and to simplify and standardize administrative procedures in regional and local governments. Moreover, support was provided for implementation of the National Digital Government Platform (PNGD) and modernization of the National Civil Status and Identification Registry (RENIEC). In complementary fashion, it supported implementation of the regulatory quality reform, which is intended to reduce overload, requirements, costs, and time for investors and business owners.
- 2.14 **The IDB Group supported structuring of projects under a public-private partnership (PPP) modality and strengthening of regulatory and institutional frameworks.** In addition to the limitations of the regulatory and institutional framework, there are obstacles to steering PPPs toward health-, education-, and water and sanitation-related projects. The IDB Group was a partner in structuring two social projects through PPPs.³³ Additionally, taking a regional public consultation into account, work has begun on preparing a strategic document aimed at improving the efficiency and transparency of the PPP system in the country.
- 2.15 **In fiscal management, the IDB Group supported public finance strengthening through revenue recovery and improved expenditure efficiency.** The main challenges were to facilitate voluntary compliance and tax control with a view to reducing evasion; strengthen the capacity for public investment, especially in subnational governments; and modernize financial and budgetary State administration. During the country strategy period, four operations were approved, to help reinforce the public finance management systems and their digital transformation. In addition, the country's economic and fiscal recovery is being supported through measures designed to boost public revenue and improve expenditure management. At the same time, the Bank has provided support to the National Superintendency of Customs and Tax Administration (SUNAT) to strengthen its capacity to facilitate voluntary compliance and tax control as well as make the tax and customs service more efficient.
- 2.16 **In health, with IDB Group support, the country achieved a significant expansion of comprehensive health insurance coverage amidst an advancing pandemic.** The sector faced the challenges of transforming the network of care, increasing public expenditure, and ensuring the availability of benefits and quality of services with a view to achieving universal health coverage. To address these challenges in the midst of a pandemic, the Bank approved operations³⁴ aimed at providing the population with adequate access to timely, efficient, and quality health care services at the first level of care and improving access to public health care, strengthening the regulatory framework for effective coverage and expanding the use of telehealth care. The main accomplishment was the expansion into universal coverage through regulatory changes that resulted in millions of Peruvian citizens being added to the Comprehensive Health Insurance (SIS). Thus, the insured population went from 73.3% in 2017 to 99% in 2021 (SUSALUD, 2021). In addition, Peru has reinforced the use of digital health care with the Bank's support.

³³ Hospitals in Piura and Chimbote and wastewater treatment plant in Puerto Maldonado.

³⁴ Program to Create Integrated Health Care Networks (PE-L1228, US\$100 million) and Program to Support Social Policies to Protect the Vulnerable Population in Peru (PE-L1262, US\$600 million).

- 2.17 **In citizen security, the Bank’s support made it possible to maintain a stable policy line amidst changes at the helm in the Ministry of the Interior (MININTER) and the National Police.** The sector’s institutional framework was strengthened as the “Perfil Policial Peruano” [Peruvian Police Profile] tool was made official. Other teaching tools will need to follow, such as curricula, a student admission profile, and a teaching professional profile in police academies. Transforming the police education system is one of the areas in which MININTER has requested increased support, as is also the case with preparing the “Bases para el Fortalecimiento y la Modernización de la Policía Nacional del Perú” [Terms for Strengthening and Modernizing the National Police Force of Peru].
- 2.18 **In water, sanitation, and solid waste management, the IDB Group assisted in closing gaps in urban and rural areas.** The sector’s challenges included ensuring that the areas of residence of vulnerable population groups met basic hygiene conditions by reducing the coverage gaps in terms of access to drinking water and basic sanitation, with an emphasis on rural areas. Thus, the Bank assisted in preparing the National Sanitation Plan 2017-2021. In the urban area, it helped to close the gap for a population of 100,000 beneficiaries.³⁵ In addition, access to services was expanded and improved in rural areas in nine of the country’s regions,³⁶ benefiting more than 40,000 people. Furthermore, garbage collection coverage was expanded from 76% to 90%,³⁷ and sanitary landfills were built and put in operation in eight cities.³⁸ At the same time, IDB Lab provided support for the low-income population to access water and sanitation through the nongovernmental organization Agualimpia, which executed an indoor plumbing project providing 80,000 people with water and sewage systems through a financial instrument, CREDIAGUA, as well as with technical assistance.
- 2.19 **In gender and diversity, the IDB Group was key to strengthening the role of the Ministry of Women and Vulnerable Population Groups in the area of prevention.** Peru faces a significant challenge in reducing gender violence and discrimination. In terms of gender violence, Peru lags behind globally, ranking 125th out of a total of 156 countries in the health category, which considers the prevalence of gender violence.³⁹ With the support of the IDB Group, a National Prevention Strategy was approved and implemented, as well as a protocol of care for Women’s Emergency Centers, among other progress. In addition, with financing and technical assistance from IDB Invest, close to 100,000 women became beneficiaries of programs such as those aimed at developing gender and diversity action plans, including women benefiting through jobs⁴⁰ and/or training/studies.⁴¹ Persons with disabilities face significant barriers in terms of urban access to health care facilities (29.3%), bus stops (23.0%), markets (21.3%), and rehabilitation centers (18.9%), among others (INEI, 2014). To address this

³⁵ Cajamarquilla, Nievería, and Cerro Camote Scheme - Expansion of the Drinking Water and Sanitation Systems (PE-L1060).

³⁶ Comprehensive Rural Water and Sanitation Program (PE-L1226) in Amazonas, Loreto, Piura, San Martín, Ucayali, Puno, Cajamarca, Junín, and Ayacucho.

³⁷ Program to Develop Solid Waste Management Systems in Priority Areas (PE-L1153).

³⁸ Bagua, Oxapampa, Pozuzo, Huamanga, San Juan Bautista, Andahuaylas, Chancay, and Yauyos.

³⁹ World Economic Forum. Global Gender Gap Report (2021).

⁴⁰ The operation Danper II (12180-01) accounts for 51% of all beneficiaries.

⁴¹ In turn, the operation Universidad San Ignacio de Loyola - Expansion (PE-L1141) accounts for 27% of all beneficiaries, while Colegios Peruanos (PE-L1120) accounts for 18%.

problem and raise awareness of the importance of inclusion, the Bank assisted the Ministry of Health (MINSA) in establishing a support network for comprehensive care of persons with disabilities and in the inclusion of persons with disabilities through the practice of Paralympic sports.⁴²

2.20 **In these two pillars, the IDB Group was a key partner for the country in addressing and mitigating the effects of the COVID-19 pandemic.** For example, it supported job protection for more than 300,000 workers and survival of one third of the country's formal businesses by helping to maintain the payment chain, while also assisting in small and medium-sized enterprise (SME) digitalization. It also supported access to higher education services to improve the digital capacity of teachers for distance education,⁴³ and worked on reforms to make fiscal management more sustainable and facilitate the post-pandemic economic recovery.⁴⁴

(iii) Environmental sustainability and climate change

2.21 **In rural development, the IDB Group supported work aimed at improving agricultural productivity.** Agriculture in Peru was characterized by low land and work productivity, and production growth relied on land and workforce expansion. With Bank support, a legal physical diagnostic assessment was performed on 140,000 individual rural parcels, 47 campesino communities, and 190 native communities,⁴⁵ and a methodology was designed for the National Agricultural Survey (ENA).⁴⁶ In addition, the nationwide yield per hectare of priority crops (potato, yellow corn, coffee, rice, and quinoa) was boosted through an increase in technology transfer to, and adoption by, agricultural sector institutions and through dissemination activities targeting producers.⁴⁷ IDB Invest approved loans to boost production, expand operations, and increase exports of agricultural products.⁴⁸ It also facilitated access to agricultural services and investments for over 1,300 agricultural producers.

2.22 **In climate change, the IDB Group worked on biodiversity conservation.** In terms of the environment, the challenges were associated with climate change issues, with an emphasis on adaptation, conservation, and sustainable use of resources, solid waste management, and support for the circular economy. At the same time, there were existing environmental problems that required attention, such as the loss of forest cover.⁴⁹ Another challenge was how to address the frequent natural disasters resulting from the country's high exposure to multiple intense natural phenomena. In this regard, with Bank support, it is expected that the objectives of adequate conservation of the forest landscape biodiversity in the

⁴² Program for Social Inclusion of Persons with Disabilities (RG-T2892).

⁴³ Program to Improve the Quality and Relevance of National Higher (University and Vocational) Education Services (PE-L1227/4555/OC-PE) at 52 public universities and 342 public institutes.

⁴⁴ PE-L1267.

⁴⁵ Through the Rural Land Cadastre, Titling, and Registration Project in Peru – Third Phase (PTRT-3) (PE-L1026).

⁴⁶ Through the Project to Improve the Agricultural Statistical Information System and the Agricultural Information Service for Rural Development in Peru (PE-L1122).

⁴⁷ Potato, corn, coffee, rice, and quinoa. Project for the Improvement of the National Agricultural Innovation Program's Agricultural Innovation Strategic Services (PE-L1125).

⁴⁸ Agrícola Cerro Prieto, 12015-02; Danper II, 12180-01; Agrícola Pampa Baja S.A.C., 12217-01.

⁴⁹ Peru has the fifth highest deforestation rate in the world and the third highest in Latin America.

Puerto Maldonado-Iñapari Corridor and the Amaraeri Communal Reserve will be met, and that deforestation mapping services in the Amazon forests will be provided. In addition, the Bank performed a cost-benefit analysis of reaching carbon-neutrality by midcentury.⁵⁰

- 2.23 **In mining, the IDB Group supported institutional strengthening for better environmental management.** The Bank supported the Ministry of Energy and Mines in implementing the Mining Promotion and Sustainability Office (DGPM) as well as specific actions to: (i) empower women leaders in sector management and in communities in mining areas; (ii) create a road map for comprehensive and systematic management of environmental liabilities; and (iii) reinforce best practices in transparency and access to information. The Bank was also instrumental in creating the Centro de Convergencia y Buenas Prácticas Minero-Energéticas [Center for Convergence and Good Practices in Mining and Energy] (RIMAY).

C. Portfolio in execution and lessons learned

- 2.24 **As of May 2022, the Bank's active portfolio⁵¹ consists of 33 operations for US\$2,397.3 million**, including 32 investment operations for US\$1,897.3 million, 28% of which (US\$670.24 million) has been disbursed.⁵² The portfolio contains a PBL with a deferred drawdown option for a total of US\$500 million and a guarantee in the transportation sector for US\$60 million. The Bank's current portfolio of technical cooperation operations includes 41 operations for US\$28.58 million, distributed as follows: climate change and sustainable development (56%), infrastructure (14%), strengthening of public management (8%), and social sector (9%).

- 2.25 **IDB Invest's active portfolio has an exposure of approximately US\$530 million**, distributed as follows: access to financial resources through cooperatives and financial institutions (42%), agriculture and rural development (26%), energy (19%), urban development (7%), science and technology (3%), transportation (2%), and tourism (1%). In addition, IDB Invest manages third-party funds for a total of US\$18.09 million. IDB Lab has 27 projects for US\$24.1 million, of which 12 are technical cooperation operations, 14 are loan operations, and 1 is an investment grant. IDB Invest provided technical assistance totaling US\$1.6 million.⁵³

- 2.26 **The implementation of the country strategy yields strategic lessons.** These lessons include: (i) the need to have the program prioritize sectors/areas in which the IDB Group offers greater value added and a lasting relationship, to maximize impact and minimize the transaction cost of preparation and execution (in line with OVE's conclusions in the ICPR); (ii) the importance of moving forward on a high-level dialogue with the government (MEF-PCM) to strengthen its strategic

⁵⁰ It is worth noting that Peru has Contingent Credit Facility coverage that has not been activated and will have to be renewed in 2024.

⁵¹ The current portfolio includes operations that have been approved by the Bank's Board of Executive Directors and have yet to achieve operational closing; i.e., the final operational financial audit report has not yet been approved in accordance with the Bank's fiduciary manuals.

⁵² The average age of the entire portfolio is 4.2 years.

⁵³ In the following areas: environmental sustainability, gender, water resource optimization, integration of indigenous population, and PPPs.

planning capacity,⁵⁴ the execution of operations, and the quality of public investment; (iii) the need to develop a strategy to raise the visibility of the IDB Group as a technical leader in sectors in which it has comparative advantages; (iv) the importance of aligning the areas of action of the IDB Group's three windows, as noted by OVE in its report. In this latter area, the public-private alignment to support the formulation and structuring of infrastructure and health projects under a PPP modality and the implementation of a common knowledge agenda was an example of a success case. In addition to these lessons, since Peru has broad access to capital markets, it is essential to gauge the appetite of the counterparts for innovative financial facilities, such as debt-for-nature swaps and new risk mitigation hedges, among others. Along these lines, creating a supply of financial products denominated in local currency is important for IDB Invest, primarily so that it can better match the currency of business revenues with the credit to the private sector.

- 2.27 The implementation of the country strategy also yields operational lessons.** These lessons include: (i) support the application of the Bank's fiduciary policies; (ii) continue to provide close support to the execution units; and (iii) explore the possibility of capacity transfer to subnational governments, which have weaknesses in executing investment projects and will be crucial for satisfactory implementation of the new country strategy. In addition, there are lessons learned in projects that did not receive disbursement period extensions and were canceled. These lessons include: (i) the importance of an adequate institutional structure that includes specialized areas with the capacity to lead the technical implementation of complex projects;⁵⁵ and (ii) a search for mechanisms that can ensure that the members of the project execution units remain in their positions despite potential political changes, and introduction of strict professional requirements for such positions.⁵⁶

III. PRIORITY AREAS⁵⁷

- 3.1 The IDB Group country strategy with Peru 2022-2026 will support sustained growth so as to foster social progress in a context of environmental sustainability and under a decentralized approach that prioritizes the rural areas.** Based on the lessons learned, the country development challenges identified in the CDC, and the dialogue with the government, this country strategy prioritizes three areas: (1) productive development, with an emphasis on the job market and higher education, integration into value chains, business environment, and infrastructure; (2) environmental sustainability and climate change, with an emphasis on adaptation and adequate risk management, agroindustry, and the fishing industry; and (3) institutional strengthening and delivery of basic services at the regional level, with an emphasis on public and fiscal management, education, health, water and sanitation, citizen security, and social inclusion of

⁵⁴ During the 2017-2021 period, Peru went through five presidents and the concomitant changes of Cabinet. Against this backdrop of constant political changes, the flexible, dynamic, and close assistance provided by the Bank was instrumental in enabling the country to achieve record approval and disbursement figures in 2021 in both policy-based loans and investment loans. The Government of Peru has consistently stated that the value added provided by the Bank's technical assistance is one of the most important for its governance.

⁵⁵ Lima Metro, lines 2 and 4 (PE-L1147).

⁵⁶ Rural Land Cadastre, Titling, and Registration Project in Peru – PE-L1026.

⁵⁷ All references are in the CDC (Annex I), along with a detailed analysis of the development challenges addressed in this document.

migrants. In addition to issues of gender, diversity, and digitalization, the topics of climate change and sustainability, and institutional capacity and rule of will also be addressed in crosscutting fashion. The priority areas and crosscutting issues will be addressed through the existing portfolio as well as through new loan and guarantee operations, knowledge products, and technical cooperation operations.

3.2 These priority areas continue along the lines set out in the 2017-2021 country strategy,⁵⁸ but with distinctively new components and areas of emphasis.

The 2022-2026 country strategy continues the work performed under the previous country strategy but focuses on those areas of work that have greater potential impact and a track record of long-term support. This is in line with OVE's comments set out in the ICPR 2017-2021. In addition, in accordance with the Bank's dialogue with the government, there will be emphasis on issues such as capacity transfer at the regional level, while at the same time supporting the country's participation in foreign markets and regional value chains, boosting work in the Peruvian Amazon,⁵⁹ and consolidating policies on violence against women and support for migrants, among other issues. Moreover, the Bank will work on new financing and technical support instruments for the country.

3.3 The actions envisaged under this strategy are aligned with the General Policy of the Government of Peru.⁶⁰

The first priority area is aligned with the first pillar of the Policy ("creation of social protection and welfare through food security") in the line of intervention aimed at reducing the gap in access to energy infrastructure, and with the second pillar ("reactivation of the economy and production activities through agrarian and rural development") in the lines of intervention aimed at creating decent jobs, formalizing productive units, promoting public and private investment, and boosting competitiveness, among others. The second priority area is aligned with the second pillar ("reactivation of the economy and production activities through agrarian and rural development") in the line of intervention aimed at promoting productivity at the regional level, and with the seventh pillar ("efficient management of risks and threats to the rights of individuals and their environment") in the line of intervention aimed at strengthening environmental management and preventive measures against natural disaster risks. Lastly, the third priority area is aligned with 9 of the 10 pillars; worth noting are lines of intervention in health, such as expanding health care coverage; in water and sanitation, such as reducing the gap in services between urban and rural areas; and in citizen security, such as strengthening the operating capacity of the police.

3.4 Below is a brief diagnostic assessment for each priority area and a list of the IDB Group's principal areas of action.

A. Priority area I. Productive development⁶¹

3.5 Despite the economic reforms and social progress made over the last 20 years, Peru has not succeeded in narrowing the development gap with

⁵⁸ The Independent Country Program Review Peru, 2017-2021, highlights the benefits of maintaining long-term relationships with some sectors, which would serve to mitigate the constant turnover of authorities.

⁵⁹ Based on the Bank's new Environmental and Social Policy Framework (ESPF).

⁶⁰ The General Government Policy for 2021-2026 was approved by Supreme Decree 164-2021-PCM.

⁶¹ The actions envisaged in this area are aligned with United Nations Sustainable Development Goals (SDGs) 4 (quality education); 8 (decent work and economic growth); 9 (industry, innovation, and infrastructure); 10 (reduced inequalities); and 11 (sustainable cities and communities).

advanced countries. Between 1960 and 2019, per-capita GDP in Peru remained at about 10% of its United States equivalent, without showing increased signs of convergence. The factors accounting for this include the limited productivity contribution⁶² to growth in the last three decades, including a negative average contribution between 2014 and 2019 (-0.2 percentage points). The country's low productivity is due to: (i) concentration of the export basket in a small number of products; (ii) lags in competitiveness and in the business environment; (iii) access and quality gaps in infrastructure, education, health, labor market, and trade integration; (iv) an unfinished agenda in innovation, digitalization, financial inclusion and, more recently, migrant inclusion; and (v) lags in rural productive development, particularly in remote areas such as the Amazon. In Peru, productive resources are not efficiently allocated since interaction between the employment and tax systems and the social insurance architecture creates perverse incentives⁶³ and results in the fragmenting of economic activity into a multiplicity of small and unproductive businesses, along with high self-employment and informality.

- 3.6 **Shortcomings in the labor market stand in the way of adequate integration into the formal workforce.** In 2019, informal employment was 73% of total employment; following the COVID-19 shock, in 2021, it went to 76.8%. Thus, Peru has one of the highest rates of employment informality in the region (47.5%).^{64,65} This is primarily a result of: (i) shortcomings in labor legislation creating disincentives to formality (nonwage expenditures account for 70% of the average formal salary);⁶⁶ (ii) limited oversight, since the National Superintendency of Labor Inspection (SUNAFIL) has limited capacity;⁶⁷ and (iii) problems in the educational and job training system leading to workers lacking the skills required by formal employers (47% of businesses have trouble filling their job vacancies).⁶⁸ These problems translate into the creation of low-productivity jobs as a structural feature. In addition, formal sector workers receive low retirement benefits, operating in a system split into the National Pension System (SNP) and the Private Pension System (SPP).⁶⁹ The problems in the system are exacerbated by the decreasing number of young contributors, the progressive aging of the population, and the approval of measures to tap retirement savings during the health emergency.
- 3.7 **In addition, there are wide gaps in labor market integration affecting women and vulnerable groups.** Women are more likely to work part-time, be self-

⁶² The Conference Board. Total Economy Database.

⁶³ Levy, S. (2016), http://www.grade.org/wp-content/uploads/Levy_inaugural.pdf.

⁶⁴ International Labor Organization (ILO).

⁶⁵ Informality is frequently associated with low productivity and with poorly paid and unskilled jobs (World Bank, 2021). In the region, the countries with higher productivity levels tend to have lower informality at the same cost as formality (Alaimo et al., 2015).

⁶⁶ Nonwage employment expenditures include bonuses, vacation, health insurance, membership in retirement plans, and other payroll taxes. In Peru, these expenditures account for about 70% of the average salary of a formal worker (Jaramillo, 2004).

⁶⁷ For example, in 2019, the average labor audit took 291 days from submittal of a complaint to a first instance ruling, and 392 days to a second instance ruling.

⁶⁸ Novella et al. (2019).

⁶⁹ The SNP only provides a pension if the member has made social security contributions for more than 10 years. Thus, members receive a monthly pension of S/250 if they contributed for 10 to 14 years, S/350 if they contributed for 15 to 19 years, and S/500 to S/893 if they contributed for more than 20 years. In addition, in view of the decreasing number of young contributors, the SNP faces the risk of becoming fiscally unsustainable.

- employed, and work informally and in less productive businesses.⁷⁰ Furthermore, 89% of indigenous Peruvians and 82% of Afro-Peruvians work in the informal sector. As a result, the monthly earnings of women, indigenous peoples, and Afro-descendants are equivalent to close to 70% of the earnings of men, mestizos, and whites.⁷¹ Moreover, many members of the LGBTQI+ collective work in poorly paid sectors or occupations, and 33% of those who describe themselves as employed (INEI, 2017) report not having been paid the promised amount, while 25% report having been physically, verbally, or sexually assaulted.⁷² Persons with disabilities also suffer from similar gaps: only 23% form a part of the economically active population⁷³ and are in low-wage occupations.⁷⁴ In recent years, these labor inclusion challenges have been compounded by the arrival of Venezuelan migrants. While migration from Venezuela could represent an opportunity to raise the country's productivity (80% of migrants are of working age and 58% have higher education), more than 90% of these migrants work in the informal sector and have elementary jobs.⁷⁵
- 3.8 **Higher education needs to make a greater contribution to productivity and an adequate transition to higher education needs to be consolidated from basic education onward.** The skills gap is a result of low quality and limited coverage of higher education offerings. Evidence of the former is the fact that close to 25% of those with non-university higher education and 8.5% of those with a university education were underemployed in 2018.⁷⁶ As evidence of the latter, between 2014 and 2018, only 35.7% of basic education graduates made an immediate transition to higher education in the face of academic, information, and financial barriers.⁷⁷ Reinforcing quality and coverage will require moving forward with implementation of the National Policy on Higher and Vocational Education approved in 2020.
- 3.9 **Peru should continue its integration process and boost value added toward other countries.** The country's productive apparatus is poorly integrated into that of the rest of the world. This is evidenced by the fact that in the 2017-2019 period, the foreign value added in Peruvian goods exports was 9.8%, higher than in the 2000-2002 period (8.2%), but well below the average in LAC (18.1% for 2017-2019) or the European Union (43.3% in the same period).
- 3.10 **The business environment continues to be skewed toward informal small and medium-sized enterprises, limiting gains in productivity.** The business sector consists primarily of microenterprises and small businesses, which in 2019 accounted for 95% of businesses and employed 47% of the economically active population. However, 84% of Peruvian microenterprises and small businesses are

⁷⁰ Jaramillo and Ñopo (2020).

⁷¹ Alcázar (2019).

⁷² Instituto de Estudios Sindicales [Institute of Trade Union Studies]. Discriminación hacia LGBTQI en el entorno laboral peruano (2016-2020).

⁷³ Of those who are economically inactive, 23.1% reported not having been able to get work because of discrimination. Of those who are economically active, 28.4% are unskilled service workers, 18.2% are skilled personal service workers, and 14.4% are farmers and skilled agricultural workers.

⁷⁴ INEI (2014).

⁷⁵ Morales and Piérola (2020).

⁷⁶ INEI (2019).

⁷⁷ IDB (2020). <https://blogs.iadb.org/educacion/es/futuroeducacionsuperiorperu/>.

informal, which limits their productivity and access to financial markets. Thus, 45% of microenterprises face credit access constraints of one type or another and the microenterprises and small businesses that obtain access to the financial system do so at a higher cost. At the same time, while larger businesses have access to finance in the credit market, they face restrictions in financing larger-scale projects due to the lack of depth of capital markets. Worth noting is the significant potential of the bioeconomy for productive development and financial inclusion of vulnerable groups and rural communities.

- 3.11 **In infrastructure, quality and quantity gaps stand in the way of adequate delivery of services and complementarity with the private sector.** The literature recognizes the existence of a positive relationship between the availability and quality of transportation infrastructure, its contribution to business productivity through complementarities with private capital, and the dynamism of economic growth.⁷⁸ In Peru, an infrastructure gap continues to exist, and an investment equivalent to 49% of GDP would be required to converge in 20 years to the levels of basic access to infrastructure in the OECD.⁷⁹ In this regard, sectors such as transportation and energy pose challenges. In transportation, only 15% of the secondary road network and 7% of the local road network are in good condition. The sector faces problems such as: (i) high informality resulting from the fragmentation of business units in the freight transport sector;⁸⁰ (ii) high degree of congestion and insecurity in maritime transport and in the port environment; (iii) limited resilience of infrastructure to natural disaster events and climate change; and (iv) limited availability and use of public mass transit, among others. In the energy sector, there are problems associated with operations. For example, in 2017, 52% of businesses experienced power failures, adversely affecting the business environment. In addition, there are quality challenges due to: (i) the limited financial mechanisms available to public distribution companies, which restricts their investment plans; and (ii) the need for greater regional integration to stabilize the supply of hydroelectric energy in view of the country's vulnerability to natural disaster events and climate change, among other factors.
- 3.12 **There is also a lag in infrastructure development financing through public-private partnerships (PPPs) that can enable an adequate distribution of risk between the public and private sectors.** Beginning in 2014, Peru witnessed a reduction in the number and size of projects awarded under a PPP modality. This is due to weaknesses in the regulatory system in terms of efficiency and transparency, and it could lead to low execution levels in transportation, health, and education infrastructure in the coming years. In addition, this problem could create a risk for implementation of the National Infrastructure Plan, which contains PPP projects yet to be awarded.
- 3.13 **There is informality in urban development and a housing access problem for the most vulnerable sectors.** In Latin America, 90% of the urban growth in the past two decades took the form of informal land tenure, as in Lima, where informal construction and self-building have been prevalent. There is a quantitative housing deficit of 4.8% (455,000 homes) and a qualitative deficit of 11.2% (1,054,000

⁷⁸ Escribano and Guasch (2012) and Cockburn et al. (2013).

⁷⁹ Castilleja-Vargas and Deza (2020).

⁸⁰ Some 90% of freight transportation companies have only between one and four vehicles.

homes). In addition, city and historic centers have suffered from social and urban decay as a result of insufficient use of urban management tools.

- 3.14 **Sustainable tourism could contribute to the economic recovery but it has significant institutional lags.** In 2019, the World Economic Forum's Competitiveness Index ranked Peru 49th out of 149 countries in travel and tourism due to the country's extensive natural resources (13th) and cultural resources (27th), as well as its high degree of international openness (8th). However, the sector showed significant lags in its institutional structure, largely as a result of a limited tourism budget (2012-2020 average: 0.3% of the public budget), limited human capital, and poor coordination between the public and private sectors. Private-sector participation in tourism-related activities and in the economy as a whole is influenced by perceptions of the business climate and legal certainty, which are in turn dependent on institutional capacity and the rule of law.
- 3.15 **Closing the digitalization gap poses an opportunity for productive development.** Peru exhibits a considerable lag in the adoption of digital technologies, in terms of the smart phone penetration rate (Peru: 52%, LAC: 66%) and the percentage of the population living in areas with 4G coverage (Peru: 52%, LAC: 65%, OECD: 97%). In addition, based on geographic area, there are differences in Internet access between urban and rural households (59% versus 20%). Furthermore, Internet access among indigenous peoples is also low (27%). This lag in digital inclusion is a significant barrier to adequately adapting education, health care, and work activities in the aftermath of the pandemic. In the business environment, microenterprises and small businesses report a lag in Internet use with respect to medium-sized and large enterprises (60% compared to 90%). In fact, as of 2018, 30% of all microenterprises and small businesses had a sales website, 2.4% engaged in online distribution, and more than 35% did not make any online banking transactions, impairing their ability to operate. This shortcoming was partially offset by governmental digitalization initiative, which were of limited scope and access and should be accompanied by a cybersecurity policy.
- 3.16 **Consistent with the preceding analysis, during the validity period of the 2022-2026 country strategy, the IDB Group will prioritize the following areas:** In labor markets, it will support the strategy to protect formal jobs and reduce informality, assessing, among other things, the perceived benefits of formalization, labor legislation, and strengthening of SUNAFIL. Support will be provided under approaches that address gender and ethnicity gaps as well as inclusion of the migrant population, the LGBTQI+ community, and persons with disabilities. In higher education, the Bank will support strategies that promote an adequate transition that starts with basic education, with an emphasis on the Afro-descendant, indigenous, and female population. To achieve these objectives, it will seek to back private-sector investments that complement public-sector efforts, as well as the implementation of PPP projects. In foreign trade, it will seek to boost participation in regional value chains and support the integration process through participation in subregional initiatives, among other efforts. In business development, the Bank will seek to deepen digitalization and reinforce the scale of innovation. In addition, IDB Invest will support the design of green financing arrangements and promote progress in the fintech industry. In infrastructure, support will be provided to improve management and planning under an intersectoral and services approach (IDB, 2020), helping to integrate a sustainable infrastructure approach into the National Infrastructure Plan 2022-2025. In PPPs,

the Bank will support strengthening the regulatory and institutional framework, among other actions. In digitalization, it will work to expand the fiber optic and 5G networks, placing priority on areas with lower access. In addition, it will support initiatives aimed at improving last-mile infrastructure, greater access to mobile connectivity, and cybersecurity.

3.17 **Alignment.** The proposed actions in this strategic area contribute to the following objectives of Vision 2025 and the institutional strategy: foster policies with a gender and diversity approach and boost the digital economy. These initiatives contribute to the strategic priorities of the IDB Invest Business Plan 2020-2022⁸¹ with regard to infrastructure development (particularly in transportation and energy), improved SME access to finance, particularly through financial institutions and value chains, sustainable tourism, and support of the crosscutting themes of gender and diversity and environmental sustainability.

B. Priority area II. Environmental sustainability and climate change⁸²

3.18 **Despite having made strides, Peru should continue to work on environmental sustainability and on reducing its vulnerability to climate change.** High pollution exposure increases susceptibility to respiratory diseases, and it aggravated the impact of COVID-19.⁸³ The structural shortcomings surrounding environmental management range from centralization and duplication of roles among agencies and authorities, coupled with capacity shortcomings at subnational governments,⁸⁴ to insufficient coverage and limited suitability of the available environmental management instruments. Oversight capacity is limited by gaps in equipment, protocols, and transparency systems. In the last decade, Peru experienced a slight increase in the Index for Risk Management (2013: 41/100 points; 2019: 46/100 points). However, there is still room to improve the framework for managing natural disaster risk. This is evidenced by the consequences of the coastal El Niño event in 2017, which destroyed 2,600 km of roads and rendered about 46,000 homes uninhabitable. In addition, Peru faces risks stemming from the country's vulnerability to climate change. For example, in 2018, 80% of all emergencies were caused by climate phenomena. Thus, climate change management and environmental sustainability require planning focused on reducing the country's vulnerability. Lastly, Peru has an opportunity to consolidate the green bond market by implementing market incentives and favorable policies in terms of climate and financial markets.⁸⁵ In fact, in late 2021, Peru carried out its first issue of sustainable sovereign bonds, which are designed to finance projects that have environmental impacts and promote equitable, quality access to health care, housing, and education services.

3.19 **The agricultural sector faces a series of challenges ranging from the need for improvements in productivity to environmental stability issues.** In recent decades, agriculture was a significant factor in external markets and in the rural workforce, bringing about a decline in extreme poverty in Peru's rural sierra (2007:

⁸¹ Document CII/GA-80-1.

⁸² The actions envisaged in this area are aligned with SDGs 6 (clean water and sanitation); 13 (climate action); 14 (life below water); 15 (life on land); and 16 (peace, justice, and strong institutions).

⁸³ World Bank (2020).

⁸⁴ Corderi and Goy (2017).

⁸⁵ Climate Bonds Initiative (2019).

- 40.2%; 2018: 11.9%), coupled with a 74% rise in productivity between 1990 and 2018.⁸⁶ However, productivity levels continue to be lower than in comparable countries⁸⁷ due to: (i) high informality; (ii) low rates of land ownership; (iii) rural infrastructure gaps; (iv) limited access to finance; (v) high logistic costs; (vi) vulnerability to natural disasters and climate change; and (vii) limited diversification of exported products. Agricultural development has gone hand in hand with greater deforestation and water stress. Agricultural activities are the cause of about 90% of deforested areas.⁸⁸ Furthermore, agriculture accounts for more than 80% of water use due to inefficient irrigation systems and the limited area under irrigation (58.3% of the total) that makes formal use of water.
- 3.20 **Artisanal fishing grew haphazardly and now requires suitable management to avoid jeopardizing environmental sustainability.** Between 2012 and 2019, the number of artisanal vessels and fishermen expanded by 93.2% and 72.7%, respectively, while catch per effort and average fisherman's income declined. This shows the overharvesting of marine resources, which erodes the sector's value. The value annually being lost as the opportunity cost of failing to implement suitable policies and management actions for the artisanal fishing sector is estimated at approximately US\$375 million (IDB, 2021).
- 3.21 **Mining requires institutional arrangements that can provide for continuity of the investment cycles in the sector.**⁸⁹ In 2019, 29% of the gold production originated in informal or illegal mining. This led to forest losses, in turn creating impacts on the environment and conflicts with indigenous peoples. At the same time, between 2005 and 2021, the proportion of social conflicts associated with the formal mining industry increased from almost 20% to more than 60%. A persistence of these conflicts causes investment project delays or halts.
- 3.22 **In line with the preceding analysis, during the validity period of the 2022-2026 country strategy, the IDB Group will support Peru in the following areas:** In environmental management, through advisory and financing services, it will support the promotion of more effective mechanisms for civil society participation in environmental regulations, improvement of information systems, evaluation and licensing of investments, and adoption of clean technologies. In disaster risk management, it will help to strengthen the governance and effectiveness of regulations. With regard to climate change, it will help in implementing the nationally determined contributions (NDCs) and the National Climate Change Strategy, adapting interventions to bring them more in line with the long-term decarbonization strategies, and updating the legal framework to better protect the country's natural capital and introduce new mechanisms for resource mobilization (sovereign green bonds, thematic bonds, and others). In addition, the IDB Group will work on the development of public investment profiles for disaster risk reduction within the framework of the National Climate Change Adaptation Plan.

⁸⁶ World Bank. Gaining momentum in Peruvian agriculture: Opportunities to increase productivity and enhance competitiveness.

⁸⁷ In 2019, the productivity of Peru's primary sector was equivalent to 39% of Colombia's and Mexico's, 28% of LAC's, and 18% of Chile's.

⁸⁸ Global Green Growth Institute (2015) and Ministry of the Environment (MINAM) (2016).

⁸⁹ The IDB will not knowingly finance, directly, or indirectly through financial intermediaries, projects involved in the production, trade, or use of the products, substances, or activities listed in Annex I IDB Environmental and Social Exclusion List of the Environmental and Social Policy Framework (ESPF).

In agriculture, work will be done on interventions aimed at shoring up the sector's productivity and sustainability. To this end, it will support the delivery of public goods in rural areas and a deepening of technology adoption in the sector. In addition, it will support the development of sustainable fish farming, particularly in the Amazon region.

3.23 **Alignment.** The proposed actions in this strategic area contribute to the Vision 2025 and institutional strategy objectives associated with the economic and social impacts of climate change adaptation and mitigation and natural disaster risk management. In addition, these initiatives contribute to the following strategic priorities under the IDB Invest Business Plan: development of water infrastructure; improvement of business sector access to finance and capacities, with particular emphasis on the agroindustrial sector, including all agricultural value chain stakeholders; and support for environmental sustainability.

C. Priority area III. Institutional strengthening and delivery of basic services at the regional level⁹⁰

3.24 **A key area for improving the delivery of goods, works, and services is institutional modernization.** Despite the strides made during the previous country strategy period in strengthening center-of-government roles, digital government, transparency of public works, and the national control system, significant institutional capacity challenges persist. These challenges primarily include: (i) strengthening civil service management where, as a result of weak implementation of the Civil Service Law approved in 2013, more than 70% of executive positions are held by public servants in positions of trust, 40% of the staff work under temporary employment contracts, there is high turnover, and only 4% of the staff are adequately trained; and (ii) strengthening the internal control system, which has a direct effect on public-sector transparency and integrity and partially accounts for the country's two-place drop in the perceived corruption index from 2020 to 2021 (105th out of 180 countries).

3.25 **The country needs to improve the quality of services delivery by generating more fiscal resources and through adequate expenditure efficiency, with a regional focus.** The public-service delivery problems are related to, among other things, the State's limited revenue collection capacity, and they are more pressing at the regional level. In 2019, Peru's tax pressure reached 16.6% of GDP, below the LAC average (22.9% of GDP), its own tax collection potential (30% of GDP),⁹¹ and the OECD average (34% of GDP), as a result of structural factors (high job and business informality) and high tax avoidance, tax evasion, and tax benefits, among other factors. There are also challenges in terms of the level and quality of expenditure. Before the pandemic, public spending was one of the lowest in the region and was characterized by limitations in execution (91% of budgeted expenditure at the national level and 72% at the local level). At the same time, there are inefficiencies that primarily relate to public procurement, payroll, and targeted transfers and stem from the lack of a strategic approach to public procurement and inefficient coordination by the National Supply System, among other factors. These shortcomings create risks to fiscal sustainability in a context

⁹⁰ The planned actions in this area are aligned with SDGs 3 (good health and wellbeing); 5 (gender equality); 6 (clean water and sanitation); 10 (reduced inequalities); and 16 (peace, justice and strong institutions).

⁹¹ Fenochietto and Pessino (2013).

of higher expenditure due to the pandemic. The government made an explicit commitment to restoring the fiscal deficit to the level of 1% of GDP by 2026 and lowering public debt to below 30% of GDP within 10 years (by 2032). Strengthening these commitments will require reinforcing the fiscal institutional structure, which in turn means reinstating fiscal rules as of 2022⁹² and shoring up the role of the Fiscal Board.

- 3.26 **Advances in social inclusion have been uneven.** In recent years, Peru has made progress in early childhood care. According to INEI, chronic child malnutrition declined between 2000 and 2020 from 37% to 12%, and the percentage of three-year-old children who had completed the Cuna Más [Cradle Plus] program and were starting early-childhood education increased between 2015 and 2019 from 51% to 57%.⁹³ However, this progress was uneven, with disadvantageous results in rural areas and low-income households.⁹⁴ In addition, the closing of institutions led to revenue and future productivity losses estimated at 10.5% of GDP (IDB, 2020). At the same time, institutional weaknesses, particularly those associated with the justice system, adversely affect women. According to the Ministry of Women and Vulnerable Population Groups (MIMP), 63% of women between the ages of 15 and 49 were victimized by their partners at some point in their lives, and 11% experienced physical or sexual violence in 2020.⁹⁵ Moreover, the number of annual femicides rose from 83 in 2012 to 136 in 2021.⁹⁶ Lastly, institutional deficiencies affected Venezuelan migrants due to their inability to regularize their immigration status, resulting in restrictions on access to formal job markets and to health, education, and housing services.⁹⁷
- 3.27 **Education involves challenges in terms of improving quality and adapting to the post-pandemic period.** Quality and equity gaps continue to exist, translating into learning gaps along urban/rural, gender, and ethnicity lines. This is partly due to the scarcity of teachers and educational materials.⁹⁸ The IDB Group will help to improve basic education with an inequity-reduction, decentralized, and inclusive focus that is tailored to the challenges that will arise in the aftermath of the pandemic. Achievement of this objective will boost collaboration on expanding the supply of teachers, adapting educational content to accommodate hybrid and inclusive learning modalities, and introducing equity and efficiency into the school management system.
- 3.28 **The health sector continues to exhibit lags owing to an insufficient level and quality of public expenditure and system fragmentation.** The health care system is characterized by low effective coverage, inequity, and low service

⁹² Through Emergency Decree 079-2021, the government established that the fiscal deficit and the public debt may not exceed 3.7% of GDP and 38% of GDP, respectively, by 2022.

⁹³ Ministry of Education.

⁹⁴ Demographic and Family Health Survey (ENDES) and National Household Survey (ENAHO).

⁹⁵ MIMP (2020).

⁹⁶ MIMP (2021).

⁹⁷ According to Plan International, in 2020, 86% of working Venezuelan migrants did not receive benefits and 55% felt they were being exploited (working up to 7 days a week, 9 to 12 hours a day). In terms of health care, 74% of households had no health insurance and 51% of pregnant women were not given prenatal checkups. In addition, 77% of Venezuelan households lived in overcrowded conditions.

⁹⁸ For example, in the 2019 teacher appointment competition, only 7.5% of competitors passed the test, leaving most of the available positions vacant and making it necessary to resort to temporary teachers.

quality. While 99% of the population had some type of insurance (2021), a majority (73%) belonged to the Comprehensive Health Insurance (SIS), which offers limited coverage.⁹⁹ In addition, health care infrastructure is obsolete and inadequate. The problems of effective and quality coverage primarily stem from insufficient public expenditure in health care, the fragmented and segmented nature of the system, and the existence of an inefficient model for delivering care. The fragmented institutional structure creates a fragile governing role for the Ministry of Health (MINSA) in view of the coexistence of three independently operating actors: (i) the public sector, which includes the SIS, for which MINSA is responsible, as well as regional and local governments; (ii) social security, provided through the public health insurance plan (EsSalud), whose members are the formal sector workers; and (iii) the private sector, including out-of-pocket payors and private insurers.

- 3.29 **In water and sanitation, there are gaps based on geographic area and also affecting ethnic groups in the Amazon region.** Peru exhibits gaps in terms of basic services associated with water, sanitation, and storm drainage. As of June 2020, only 39% of the population consumed water containing adequate chlorine levels, while 57% of the population had 24-hour access to water. Measured along geographical and ethnic lines, water access was uneven: 95% in urban areas, 76% in rural areas, 85% for indigenous peoples, and 84% for Afro-Peruvians.¹⁰⁰ Similarly, sewerage coverage in rural areas is low (19%). Moreover, the 2017 coastal El Niño event showed that the urban storm drainage system lacks adequate planning and infrastructure for floods. These shortcomings make it difficult to satisfy hygiene measures in places of residence of vulnerable population groups, schools, and health facilities in rural and remote areas such as the Amazon region.
- 3.30 **Citizen security continues to emerge as one of the population's most pressing problems—an area with significant institutional weaknesses.** Insecurity, both actual and perceived, has exhibited a clearly upward trend. Thus, crime is the second most important perceived problem.¹⁰¹ The proportion of citizens who reported having experienced violence of some type increased from 31% in 2014 to 36% in 2018 (the highest proportion in the region).¹⁰² This is in line with citizens' opinions of the institutions responsible for providing security and justice: 12% of survey respondents trust the judiciary, 15% trust the Public Prosecutor's Office, and 19% trust the police.¹⁰³ Institutional continuity is a determining factor for ensuring an effective and sustainable citizen security response. The programmatic instruments that have been designed¹⁰⁴ could be important for overcoming sector difficulties such as the institutional weakness of the Ministry of the Interior (MININTER) and the difficulties in adequately compiling and processing crime data.

⁹⁹ For example, only 10% of women members had Papanicolau test coverage (INEI, 2020).

¹⁰⁰ INEI.

¹⁰¹ INEI (2020). National Household Survey. Governance, transparency, and democracy module.

¹⁰² The Political Culture of Democracy in the Americas: First Glance at Topline Results, 2019.

¹⁰³ INEI (2020). National Household Survey. Governance, transparency, and democracy module.

¹⁰⁴ In 2021, MININTER conducted an institutional consensus exercise with the support of civil society organizations to create a profile of the Peruvian police officer of the future. This instrument can serve as a basis to begin a reform of the police education system. In addition, the Terms for Strengthening and Modernizing the Peruvian National Police were prepared. This instrument is being used to plan investment actions and decision-making within the National Police.

3.31 Consistent with the preceding analysis, the IDB Group will prioritize the following areas during the validity period of the 2022-2026 country strategy:

In the public management area, the IDB Group will be a partner in achieving more efficient and effective public procurement, fostering transparency through digital transformation for the delivery of public goods, works, and services, and advancing in strengthening the civil service and internal control system. At the same time, it will work closely with the regions to support institutional capacity improvements. In the fiscal area, it will assist in the implementation and simplification of the tax systems and the design of a new municipal tax collection system linked to the fiscal cadastre, among other actions. In the social protection area, it will work to strengthen early childhood services and the role of institutions that can improve the socioeconomic conditions faced by women, the indigenous population, and migrants, ensuring socially and culturally appropriate interventions based on lessons learned from prior interventions. In addition, the IDB Group will work to consolidate policies for the prevention of violence against women by assessing the effectiveness of current programs. Lastly, it will help to expand the capacities of institutions associated with regularizing the status of migrants and to adapt the country's immigration policy. In the health care area, it will work on the transition to universal health care coverage with equitable and efficient services. It will also support the implementation of activities and processes that can help to unify the health care system. In water and sanitation, it will support the implementation of investments aimed at bridging the infrastructure gaps, improving the delivery of services, and strengthening the financial capacity of sanitation service providers. It will also endeavor to foster a multisector approach (including solid waste and urban storm drainage) with a water security perspective, increased access to sanitation, and resilience to climate change, with an emphasis on the neediest regions. In citizen security, it envisages accelerating implementation of the Proyecto Barrio Seguro [Safe Neighborhood Project], strengthening the police education reform process as well as the information systems and their interoperability, among other things.

3.32 Alignment. The initiatives contribute to the following Vision 2025 and institutional strategy objectives: strengthen institutional capacity and the rule of law and boost the digital economy. These initiatives also contribute to the 2020-2022 IDB Invest Business Plan's strategic priority of supporting the development of social infrastructure and strengthening the capacities of the corporate sector.

D. Crosscutting issues and areas of dialogue

3.33 Crosscutting issues will be addressed in complementary fashion. Gender and diversity issues will be mainstreamed in the three strategic pillars, and while institutional capacity and rule of law issues and climate change and sustainability issues are addressed as priority pillars, efforts will be made to mainstream these issues in the other pillars.

3.34 Peru continues to exhibit gender disparities. The country was ranked 62nd (out of a total of 156 countries) in the 2021 Global Gender Gap Report.¹⁰⁵ Worth noting in this regard, as indicated above, are the quality gaps in terms of access to the labor market for women, ethnic groups such as the indigenous population and

¹⁰⁵ World Economic Forum. Global Gender Gap Report (2021). Country rankings are established by considering the following categories: (i) educational attainment; (ii) health and survival; (iii) economic participation and opportunity; and (iv) political empowerment.

Afro-Peruvians, and vulnerable groups such as LGBTQI+ and persons with disabilities. The IDB Group aims to support the country in narrowing the gender gaps and increasing diversity in market access for minorities. To achieve this objective, it will seek to support knowledge products, loan operations, and technical cooperation operations that prioritize addressing the needs of vulnerable groups, create progress in terms of equitable access to public services and social protection networks, and prioritize financing for women-led enterprises. It should be noted that actions in this regard will need to be addressed in a decentralized manner since disparities become sharper when comparing urban and rural areas.

- 3.35 **Given its size and diversity of environments, Peru is vulnerable to climate change.** In 2018, 80% of all emergencies were caused by climate phenomena. Thus, climate change management and environmental sustainability require program and project planning aimed at adaptation and mitigation to reduce the country's vulnerability. In this area, the Bank will support measures that can contribute to implementation of the NDCs and the National Climate Change Strategy 2050. In addition, it will emphasize work in the Amazon region aimed at implementing strategies to promote and develop alternative livelihoods for native communities, including through the use of existing resources under the Amazon Initiative. It will also emphasize integrating forest goods and services into biobusiness value chains as part of a fair transition toward lower emissions from land-use change. Furthermore, the Bank will promote non-extractive and regenerative business models for sustainable development of the Peruvian Amazon, as well as facilitating investments to restore and protect natural capital assets. Lastly, it will support implementation of the Law on Reward Mechanisms for Ecosystem Services by developing offset instruments such as habitat banking.
- 3.36 **Institutional development and strengthening of the rule of law will be priority issues in the future work agenda.** These are defining issues for this strategy, since an adequate public institutional structure with a solid foundation of transparency and integrity will determine the effectiveness of the design and implementation of public policies and make it possible to sustain the economic recovery. The IDB Group will support strengthening the institutional capacities of subnational governments and moving forward toward greater transparency in the management of resources and decision-making.
- 3.37 **Digitalization has become a priority issue for the country.** As the health emergency expanded worldwide, digitalization became more relevant for the operability of the business sector, delivery of basic services, and conduct of public management. For this reason, digitalization is a core issue under this strategy. The IDB Group plans to build on the social progress achieved to date by boosting connectivity for the population and for public service providers. Interventions will be aimed at making greater use of information and communication technologies for investments and at supporting the delivery of services through greater connectivity in health care and education.
- 3.38 **Areas of dialogue.** In the dialogue with the authorities, there is potential for support in the following areas, among others: (i) expenditure management at the subnational level; (ii) support in the delivery of care services to boost job recovery for women; (iii) support in updating and monitoring development of the competitiveness and infrastructure plans (PNCP and PNIC, respectively); and (iv) support in local investment plans.

IV. PROJECTED LENDING FRAMEWORK

- 4.1 **The sovereign-guaranteed lending framework projects annual approvals for an average of US\$600 million or a total of US\$3.000 billion for 2022-2026.** To achieve this level of approvals, the Bank will emphasize its technical support in the strategic areas. During the strategy implementation period, the IDB Group will continue to explore options such as a commodities (gold or copper) hedge, treasury, or other instrument that can provide local currency efficiently and profitably. While the Peruvian government is expected to have continued access to financial markets on favorable terms, the differential between the Bank's sovereign-guaranteed financing conditions and the financial markets has been narrowing in recent years.
- 4.2 **The Bank will continue to be a strategic partner for the country.** The expected approvals, coupled with the expected disbursements, should enable the Bank to maintain a 5%-8% share of the country's total external debt.

V. STRATEGY IMPLEMENTATION

- 5.1 **Portfolio execution.** The active portfolio will be an integral part of the new country strategy. To ensure its smooth implementation and its contribution to the outcomes identified in Annex I, the Bank will closely assist the executing agencies and continually work to strengthen their capacity to handle procurement, planning, and project management issues. In addition, the Bank will be in constant communication with the Ministry of the Economy and Finance (MEF) to prioritize the interventions and seek adequate budget allocations within any restrictions imposed on the country by the fiscal rules.
- 5.2 **Program flexibility and joint work by the windows.** The IDB Group's contribution will need to be provided in a comprehensive manner, endeavoring to bring flexible solutions and innovative tools such as guarantees and use of financial hedges. Coordination among the IDB, IDB Invest, and IDB Lab will adhere to 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 having evident synergies; (iii) organization of joint activities (workshops and seminars) aimed at disseminating the work of IDB Invest to expand and diversify its portfolio of potential clients; (iv) maximization of operational synergies, including IDB and IDB Invest scaling up IDB Lab projects; and (v) joint knowledge products that are relevant for an operational dialogue with clients.¹⁰⁶ The IDB Group will need to identify opportunities to add value based on the existing strategic positioning in the country and the changes of context. In this regard, the repeated turnover of authorities in recent years could frame the IDB Group as a constant in a volatile environment.
- 5.3 **Coordination with other donors.** The Bank foresees close collaboration with: (i) Kreditanstalt für Wiederaufbau (KfW) and the Government of Spain in water and sanitation and in urban development; (ii) KfW and the Japan International Cooperation Agency (JICA) in solid waste management and institutional strengthening; (iii) the International Fund for Agricultural Development (IFAD) in agriculture; (ii) the World Bank in the areas of innovation, energy, health, and rural

¹⁰⁶ This will measure each window's contribution to knowledge products.

infrastructure, jointly with the Development Bank of Latin America (CAF); (iii) the UK Sustainable Infrastructure Program (UKSIP) in the energy area; (iv) the Clean Technology Fund (CTF) in electromobility; (v) the United Nations (United Nations Children's Fund (UNICEF), United Nations Development Programme (UNDP), and United Nations Women) in implementing the National Care System; (vi) the United Nations Educational, Scientific, and Cultural Organization (UNESCO), in cultural and creative industries; (vii) the Swiss State Secretariat for Economic Affairs (SECO) in integration into value chains and trade facilitation; (viii) the Government of Norway, UNDP, and United States Agency for International Development (USAID) in the National Forest Conservation and Climate Change Strategy; and (ix) the Canadian International Development Agency (CIDA) in mining and foreign trade. Also worth noting is the coordination with the Governments of Israel, Switzerland, and the Republic of Korea on innovation and competitiveness issues and with the Government of Germany on green fiscal policies. In addition, the Amazon Initiative will offer resources (including donor funds) to promote sustainable and inclusive social and environmental development models (including for vulnerable groups such as indigenous communities and women-led enterprises in the Amazon region) and fast track compliance with the Sustainable Development Goals in the communities and territories in Peru's Amazon.

- 5.4 **Use of country systems.** At present, the Bank makes full use of the budget, treasury, accounting and reporting, and external control subsystems. In October 2017, the Bank's Board of Executive Directors (document GN-2358-22) approved advanced use of Peru's RCP public procurement system in operations¹⁰⁷ financed by the Bank and executed by the agencies forming part of this system, pointing out that use of the RCP's subsystems for electronic catalogues for framework agreements and reverse auctions was approved back in 2013 and has progressively been implemented since that date. The advertising subsystem of the Electronic Government Procurement System (SEACE) will continue to be used for contracts of all types. The diagnostic assessment of Peru's SAP public procurement system, which uses the OECD/MAPS methodology, was completed in 2016 and is expected to be updated during the new country strategy period, subject to a new State Procurement Law now in the design stage. Under loan contract 4428/OC-PE, Project to Boost Efficiency in Public Investment Management and Public Procurement, the Bank is financing: improvements to the SEACE's transactional procurement portal; the process of modernizing the Government Procurement Oversight Agency (OSCE); capacity-building for RCP operators; and improvements to bidding processes and documents. By means of technical cooperation operations aimed at reinforcement and use of the country systems, the Bank provides support for modernizing public procurement through an analysis of the regulations in effect and inclusion of sustainability criteria.
- 5.5 **The public finance management system has made significant strides.** Since 2018, Peru has a new regulatory framework for modernizing the financial administration of the public sector. This framework is aimed at improving the management, productivity, efficiency, and effectiveness of government entities, including by strengthening interoperability, coordination, and integration among the national systems forming part of the Public Sector Financial Administration (AFSP). Peru has been among the countries that have made the greatest progress

¹⁰⁷ The term "operations" encompasses loan operations, technical cooperation operations, and investment grants.

in implementing International Public Sector Accounting Standards (IPSAS) in the region; however, it is acknowledged that this process needs to continue. In 2021, the Peruvian government approved a digital transformation plan that envisages modernization of the Integrated Financial Administration System (SIAF), including new processes and computer modules. However, there is still room for improvement in terms of the AFSP processes, computer systems, and technological infrastructure, as identified in the diagnostic assessment performed by the Bank as part of the design of loan operation 5301/OC-PE.¹⁰⁸ In addition, there is a need to continue to strengthen public external control through the capacities of the CGR, which the Bank has been supporting under loan operation 4724/OC-PE.¹⁰⁹ The use of Peru's country systems and the actions envisaged for this country strategy period are summarized in the following table:

Use of country systems	2022 Baseline	2026 Projected use	Planned actions
Budget	100%	100%	Dialogue and monitoring
Treasury	100%	100%	Assistance in consolidating use of the treasury single account
Accounting and reporting	100%	100%	Support to the government in the process of implementing IPSAS to close gaps with international standards
Internal audits	0%	0%	Dialogue and monitoring
External audits	100%	100%	Assistance in the process of improving the governmental control systems (loan 4724/OC-PE).
Information system	100%	100%	The SEACE advertising subsystem will continue to be used for contracts of all types. Assistance will be provided in implementing an updated version of SEACE.
Shopping	50%	100%	Strengthening of the execution units regarding implementation of the subsystem.
Individual consultants	7%	10%	Update to the diagnostic assessment of the RCP public procurement system through the OECD/MAPS methodology. Strengthening of the execution units regarding implementation of the subsystem in order to increase its use.
Partial NCB	0%	50%	Update to the diagnostic assessment of the RCP public procurement system through the OECD/MAPS methodology. Strengthening of the execution units regarding implementation of the subsystem in order to increase its use.
Advanced NCB	10%	50%	Update to the diagnostic assessment of the RCP public procurement system through the OECD/MAPS methodology. Strengthening of the execution units regarding implementation of the subsystem in order to increase its use.

¹⁰⁸ Project to Improve the Financial Administration of the Public Sector through Digital Transformation.

¹⁰⁹ Project to Enhance Control Services for Effective, Preventive, and Enabling Control for Public Management.

VI. RISKS

- 6.1 **Political risks and institutional coordination.** To ensure execution within the framework of the country strategy, the IDB Group will maintain an ongoing dialogue with the authorities in the Presidency of the Council of Ministers (PCM) and Ministry of the Economy and Finance (MEF). At the same time, it will work with the MEF to strengthen the capacity for strategic planning of public investment, especially at the subnational level. Furthermore, considering the high turnover of authorities (including the staff of the project execution units), it is also working with the MEF to identify specific provisions in the loan contracts that can mitigate this risk and ensure the continuity of operations. The Bank will continue to monitor this risk through periodic governmental coordination and portfolio review meetings.
- 6.2 **Macroeconomic risks.** These notably include (i) lags in the economic recovery due to the COVID-19 shock; (ii) erosion of business confidence in an environment of political uncertainty; and (iii) persistence of Russia's war on Ukraine, which could aggravate inflationary pressures. An erosion of business confidence could affect decision-making at businesses and thereby compromise the growth of private investment in the coming years.
- 6.3 **Natural disaster risks.** The occurrence of natural disasters could once again lay bare the vulnerabilities of environmental risk management and the urban infrastructure. In addition, it will be important to fulfill the country's mitigation commitments for 2030 as reflected in the nationally determined contributions (NDCs). Peru is exposed to multiple intense natural phenomena, which could destroy part of the capital stock, jeopardize the flow of goods and services production, and thus create an impact on potential GDP. In fact, the country recently suffered the consequences of the 2017 coastal El Niño event, which (i) destroyed road infrastructure (particularly roads and bridges), impacting business activity and services in the neighboring departments; (ii) rendered homes uninhabitable, revealing their vulnerability due to a failure to adhere to formal guidelines and obtain construction insurance; and (iii) affected primary activities such as fish landings (due to anomalous sea conditions) and agricultural production (due to interruption of the planting and harvesting cycle).
- 6.4 **Social and environmental risks.** In view of the exacerbated deforestation and degradation of natural habitats, particularly in the Amazon region, and the significant presence of vulnerable groups (indigenous peoples and rural communities), it will be important to adopt international good practices to ensure that the country is prepared to adhere to international conventions and abide by the Bank's new Environmental and Social Policy Framework.
- 6.5 **Execution risk.** The weakness of some executing agencies in terms of their capacity to manage investment projects is one of the main execution risks. 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 with a view to achieving the outcomes agreed upon by the Government of Peru and the IDB Group. Recognizing the challenges involved in executing the portfolio and the lending framework envisaged in this strategy, the

plan is to: (i) focus interventions on larger-scale operations, mitigating potential execution risks in units that have no experience working with the IDB Group, and provide 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. This risk could be even greater than in the past, since the Bank envisages the possibility of working closely with subnational governments, which tend to have less institutional capacity than the national government. The Bank will monitor this risk through periodic portfolio review meetings.

ANNEX I: RESULTS MATRIX

Government priorities	The Bank's strategic areas	The Bank's strategic objectives	Expected outcomes	Indicators	Baseline (Source and year of measurement)
Economic recovery	A. Productive development	1. Support formal job placement and labor market productivity	Increase the percentage of workers who contribute to social security	Active workers who contribute to social security (percentage of total workers)	2019: 22.50% (Labor Markets and Social Security Information System (SIMS), IDB)
			Increase the percentage of students completing basic education who move on to higher education	Transition to higher education (percentage of graduates from the previous educational level)	2019: 36.6% (Educational Quality Statistics Unit (Escale), Ministry of Education (MINEDU))
		2. Improve the supply of infrastructure	Reduce the short- and long-term infrastructure gap	Progress in financial execution of the portfolio of projects prioritized in the PNIC (percentage progress compared to the total investment commitment)	2019: 11.0% (National Infrastructure Plan for Competitiveness (PNIC), MEF)
			Narrow the digital divide in Internet access	Percentage of Internet users (percentage of total population)	2019: 60.0% (Latin American Economic Outlook, OECD)
		3. Strengthen the business environment and business climate	Expand access to financial markets for microenterprises and small businesses	Microenterprises and small businesses that have performed a credit transaction in the financial system (percentage of total enterprises in the respective segment)	2019 Microenterprises: 4.0%; small businesses: 44.5% (Ministry of Production (PRODUCE))
Efficient management of risks and threats	B. Environmental sustainability and climate change	4. Strengthen environmental management with a focus on sustainability and climate change	Improve environmental quality and ecosystem vitality	Environmental performance index (score: 0-100)	2018: 61.92 / 100 (Yale Center for Environmental Law & Policy)
			Strengthen information systems for water resources	Watersheds with interoperable information services for multisector planning and management of water resources, with a climate change approach (percentage of total)	2019: 11% (National Climate Change Adaptation Plan, MINAM)

Government priorities	The Bank's strategic areas	The Bank's strategic objectives	Expected outcomes	Indicators	Baseline (Source and year of measurement)
Economic recovery		5. Improve agroindustrial productivity	Expand credit access for agricultural producers	Agricultural producers who obtained credit (percentage of total number of producers who applied for credit)	2018: 10.04% (National Agricultural Survey (ENA), INEI)
Institutional and civil service strengthening		6. Boost the effectiveness and institutional structure of public administration	Enhance the effectiveness of governance	Government effectiveness index (score: -2.5 – 2.5)	2019: -0.1 (Worldwide Governance Indicators, World Bank)
			More forward on digitalization of the public sector	E-government or digital government index (score: 0-1)	2018: 0.65 (E-Government Survey, United Nations)
			Reduce the crime rate in the population	Population over 15 years of age that has been the victim of a crime that threatens safety, violates rights, or involves danger in urban areas (percentage of the total population)	2019: 26.6% (National Survey of Budget Programs (ENAPRES), INEI)
Creation of welfare and social protection	C. Institutional strengthening and delivery of basic services at the regional level	7. Improve social inclusion	Reduce the percentage of women who experience violence	Women who experienced psychological, physical, or sexual violence (percentage of all women)	2019: 57.7% (Demographic and Family Health Survey (ENDES), INEI)
			Boost employment of the indigenous and Afro-Peruvian population	Adequate employment rate (percentage of total economically active population) in the Amazon region	2019: 45.1% (National Household Survey (ENAHO), INEI)
		8. Improve the coverage and quality of basic health care, water, and sanitation services	Increase the proportion of health care expenditure	Current health care expenditure (percentage of GDP)	2019: 5.22% (World Health Organization (WHO))
			Increase drinking water coverage	Drinking water coverage in urban and rural areas (percentage of the total population)	2019: Urban: 84.4%; rural: 7.2% (National Survey of Budget Programs) (ENAPRES), INEI)
			Increase basic sanitation coverage	Basic sanitation coverage in urban and rural areas (percentage of the total population)	2019: Urban: 90.1%; rural: 18.9% (National Survey of Budget Programs) (ENAPRES), INEI)

ANNEX II. COUNTRY SYSTEMS MATRIX

The Bank's strategic objectives	Expected outcomes	Indicators	Unit of measurement	Baseline	Baseline year	Main objective	Periodicity	Alignment with the CRF
Strengthening of country fiduciary systems	Closing of gaps with international standards (IPSAS)	Progress in implementation of IPSAS through Bank support initiatives related to advisory services and training/forums	Number of support initiatives	0	2021	4	At the end of the strategy period	Institutional capacity and rule of law. Productivity and innovation.
	Modernization of public procurement systems	Diagnostic assessment update of the country procurement system using the OECD/MAPS methodology	Number of diagnostic assessments	0	2021	1	At the end of the strategy period	Institutional capacity and rule of law.
Increase in the operational efficiency of the Bank portfolio	Shopping	Percentage of Bank-financed operations that use shopping	Percentage of the Bank's active portfolio	50%	2021	100%	At the end of the strategy period	Productivity and innovation.
Increase in use of the country fiduciary systems	Partial national competitive bidding (NCB)	Percentage of Bank-financed operations that use partial NCB	Percentage of the Bank's active portfolio	0%	2021	50%	At the end of the strategy period	Productivity and innovation.
	Advanced NCB	Percentage of Bank-financed operations that use advanced NCB	Percentage of the Bank's active portfolio	10%	2021	50%	At the end of the strategy period	Productivity and innovation.
	Individual consultants	Percentage of Bank-financed operations that use individual consultants	Percentage of the Bank's active portfolio	7%	2021	10%	At the end of the strategy period	Productivity and innovation.

ANNEX III. MAIN ECONOMIC AND SOCIAL INDICATORS

Year	2015	2016	2017	2018	2019	2020	2021
Social indicators							
Population (millions)	30.5	30.9	31.4	32.0	32.5	33.0	33.4
Life expectancy at birth (years)	75.8	76.0	76.3	76.5	76.7	76.9	
Literacy (% population age 15 and over)	94.2	94.2	94.1	94.4	94.4	94.5	
Nationwide unemployment (% EAP)	3.5	4.2	4.1	3.9	3.9	7.4	5.7
Production and Prices							
Real GDP (real % change)	3.3	4.0	2.5	4.0	2.2	-11.0	13.3
CPI (% change, period average)	3.5	3.6	2.8	1.3	2.1	1.8	4.0
CPI (% change, end of period)	4.4	3.2	1.4	2.2	1.9	2.0	6.4
External Sector							
Exports (nominal % change)	0.2	13.1	16.0	8.5	0.1	-12.3	61.0
Imports (nominal % change)	4.6	1.1	5.5	9.4	1.8	-14.8	54.9
Current account (% of GDP)	-4.7	-2.3	-0.9	-1.3	-0.7	1.2	-2.3
Net international reserves (US\$ billion)	61.5	61.7	63.6	60.1	68.3	74.7	78.5
Monetary Sector							
Monetary liquidity (M2, % change, end of period) 1/	11.6	4.4	8.8	9.7	9.1	28.8	2.7
Credit to the private sector (% change, end of period) 2/	7.2	5.5	6.3	8.9	7.1	11.0	4.4
Public Sector 3/							
Revenue (% GDP)	20.1	18.6	18.0	19.1	19.6	17.8	21.0
Primary expenditures (% GDP)	21.2	19.8	19.9	20.0	19.9	24.7	22.2
Primary balance (% GDP)	-0.9	-1.3	-1.8	-1.0	-0.2	-7.3	-1.0
Economic balance (% GDP)	-1.9	-2.4	-3.0	-2.3	-1.6	-8.9	-2.5
Debt							
Total external debt (% GDP)	38.1	38.3	35.6	34.7	34.8	44.2	45.2
Total public debt (% GDP)	23.3	23.7	24.7	25.6	26.6	34.6	36.9
Domestic (% GDP)	12.1	13.4	16.0	16.8	18.1	19.8	16.5
External (% GDP)	11.1	10.3	8.7	8.8	8.5	14.9	19.5
GDP							
Nominal GDP (US\$ billion)	192.0	195.7	215.9	226.9	232.4	205.7	225.4
GDP per capita (current US\$)	6229	6205	6711	6958	7028	6127	6643

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

1/ Includes the liquidity of deposit institutions at the current exchange rate.

2/ Includes deposit institutions.

3/ Corresponds to the nonfinancial public sector.

ANNEX IV. DEVELOPMENT EFFECTIVENESS MATRIX (SUMMARY)

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX	
<p>In August 2008, the Board of Directors approved the Development Effectiveness Framework (document 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's 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>	

COUNTRY STRATEGY: PERU

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.

EFFECTIVENESS

These measure 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 buildup of country systems.

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	Yes
II. Priority Areas Diagnostics	%
- That clearly identify and dimension, based on empirical evidence, the	100%
- That clearly identify and dimension, based on empirical evidence, the	100%
- That provides corresponding policy recommendations	100%
III. Results matrix**	%
- The strategic objectives are clearly defined	100%
- The expected outcomes are clearly defined	100%
- The strategic objectives and expected results that are directly related	100%
- The indicators are outcome indicators and are SMART	100%
- The indicators have baselines	100%
IV. Vertical logic	Yes/No
- The CS has vertical logic	Yes