



PERÚ

Ministerio
de Economía y Finanzas

PERU

Preserving Sustained Growth and Macroeconomic Stability

Mr. Alfredo Thorne

Minister of Economy and Finance

May/June 2017

InPerú

1 Two adverse shocks

2 The recovery path in 2017

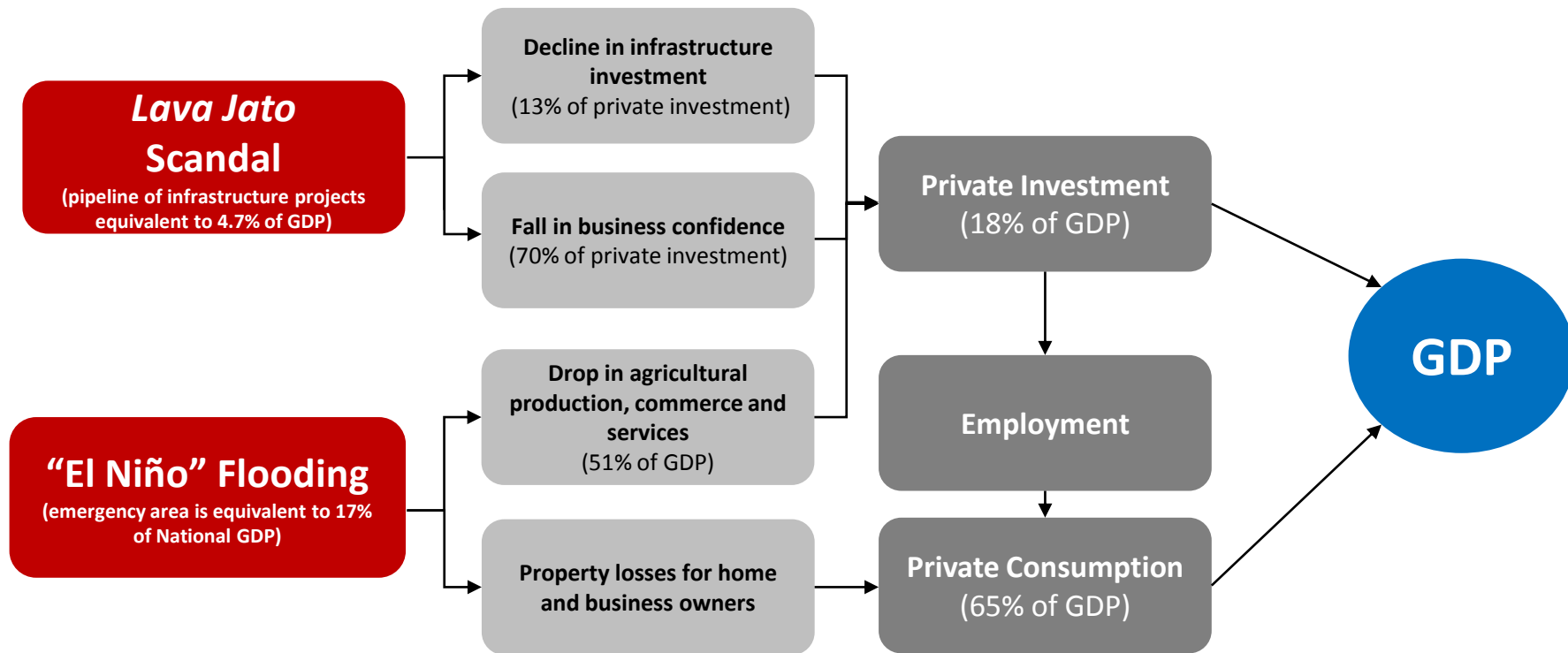
3 A Growth Strategy for the medium term

4 Debt management

5 Capital markets reform

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The Peruvian economy has been affected by two transitory and unexpected shocks



1

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A Growth Strategy for the medium term

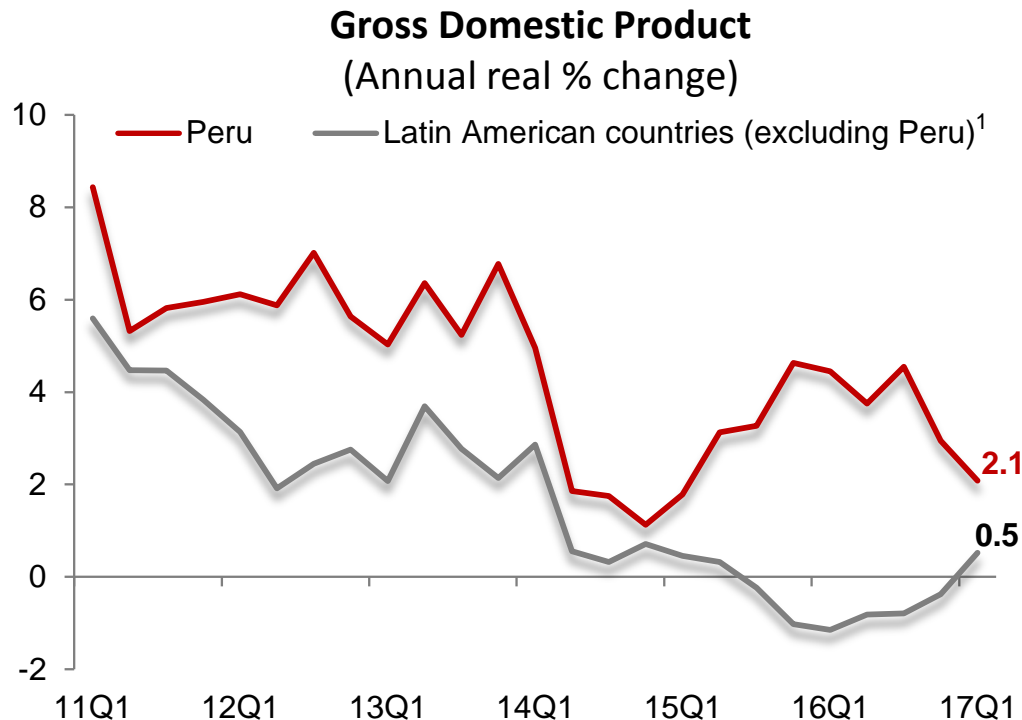
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Debt management

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Capital markets reform

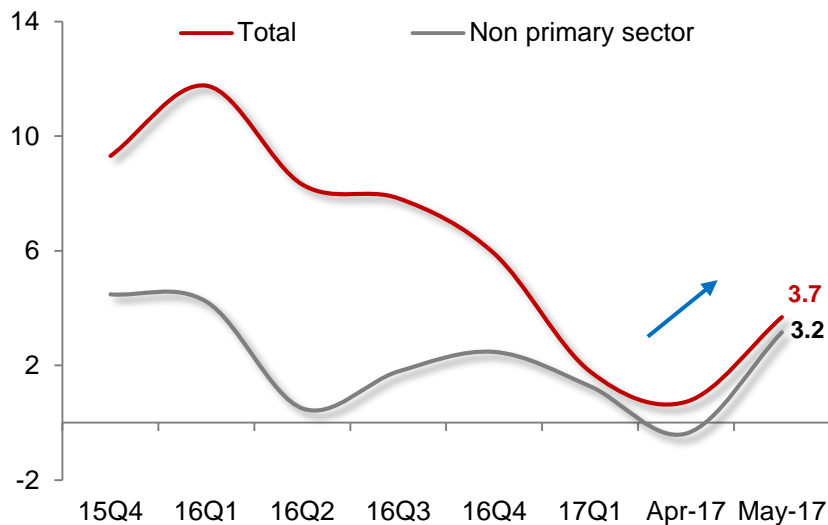
The Peruvian economy has been resilient to both shocks, growing even more than its regional peers in 2017Q1



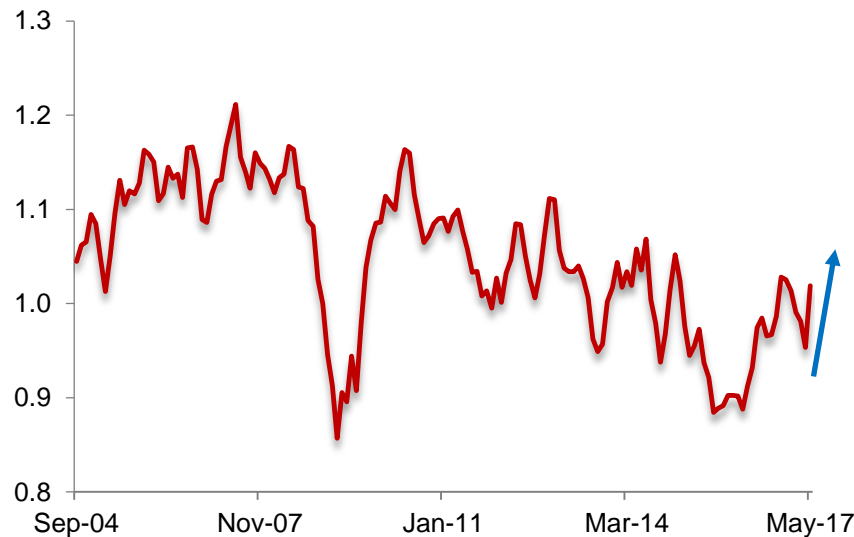
^{1/} Includes Argentina, Brazil, Chile, Colombia and Mexico. For Argentina and Brazil, the median of the Bloomberg survey for 17Q1 is considered.
Source: BCRP, Central Bank of Chile, National Administrative Department of Statistics (Colombia), National Institute of Statistics and Geography (Mexico), Bloomberg.

Leading indicators suggest that the economy has already started accelerating

Electricity demand¹
(Annual real % change)



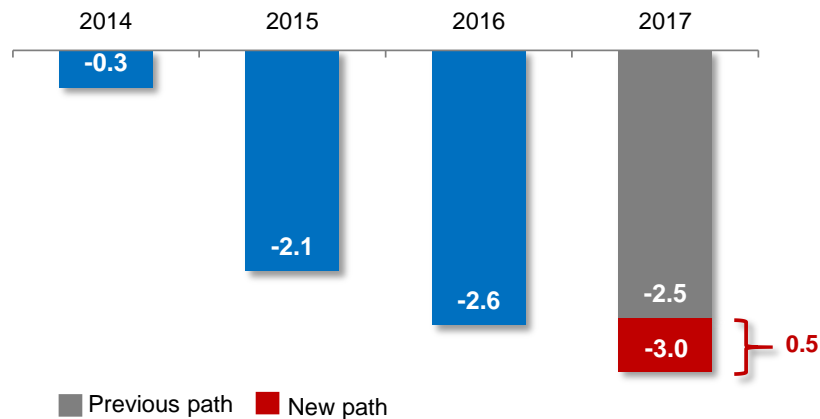
CB's Survey: Purchasing Orders / Inventories Ratio
(Three-month moving average)



1/ As of May 21st, 2017.
Source: COES, BCRP.

Expansionary fiscal policy will be the main driver of growth this year...

Non-Financial Public Sector Overall Balance
(% of GDP)



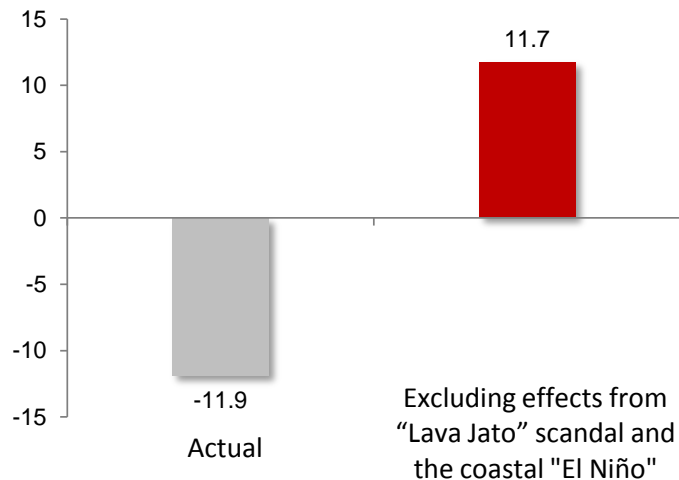
The Government has taken measures to accelerate the disbursement of public spending:

- A fiscal stimulus of 1.3% of GDP, in addition to the 2017 public budget.
- Prioritization of public investment projects under execution but lacking budget.
- Quick win: increase in maintenance spending.
- Transfers to subnational governments earlier in the year (Q1 vs. historical Q3).
- Simplified procurement scheme for emergency areas that reduces the timeline of procedures up to 120 days.

..., primarily, in the second half of 2017

Public Investment¹ in 2017Q1

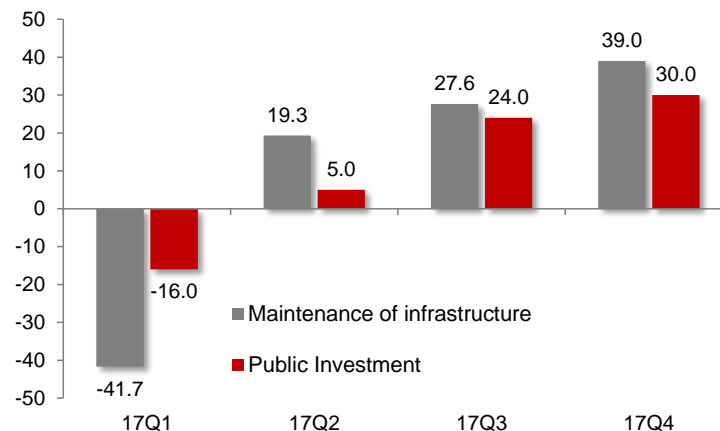
(Annual real % change)



- Public investment in emergency areas is equivalent to 60% of total public investment.
- In 2017Q1, public investment in emergency areas fell 23.5% in real terms. Excluding the "Lava Jato" scandal and "El Niño", public investment would have grown 11.7%.

Public Investment and Maintenance of Infrastructure

(Annual real % change, 2017)

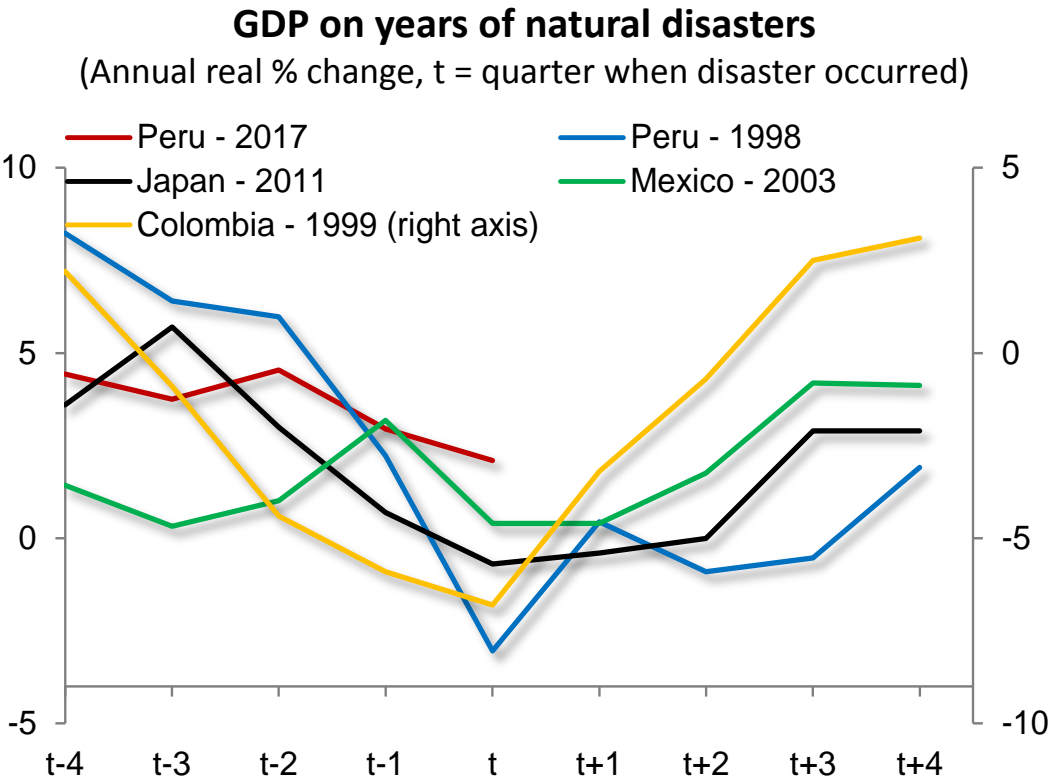


- Public investment in the first quarter reached approximately 14% of total annual public investment (2009-2016 average).
- Maintenance expenditure in the first quarter represents 17% of total annual maintenance (2009-2016 average).

1/ General government public investment.

Source: MEF.

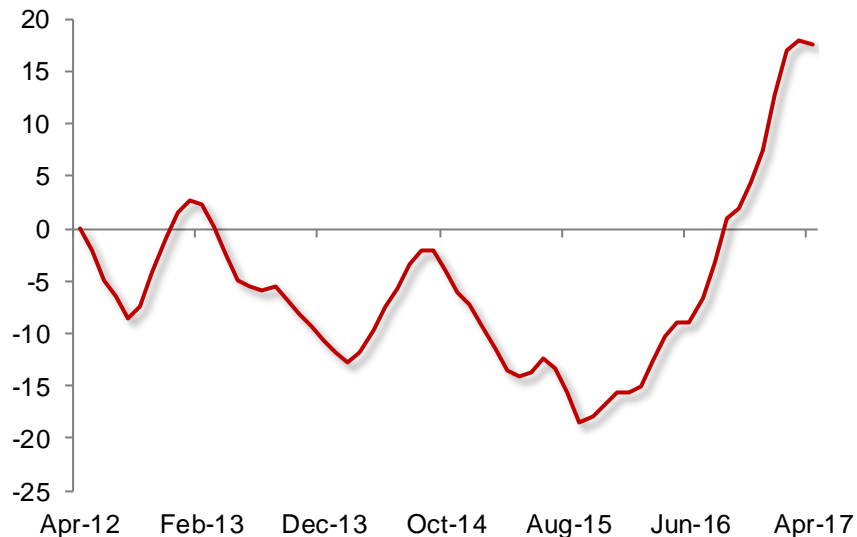
Empirical evidence suggests that the economy should accelerate during the first two quarters after the natural disaster



Global conditions are favorable to the Peruvian economy, even with recent volatility

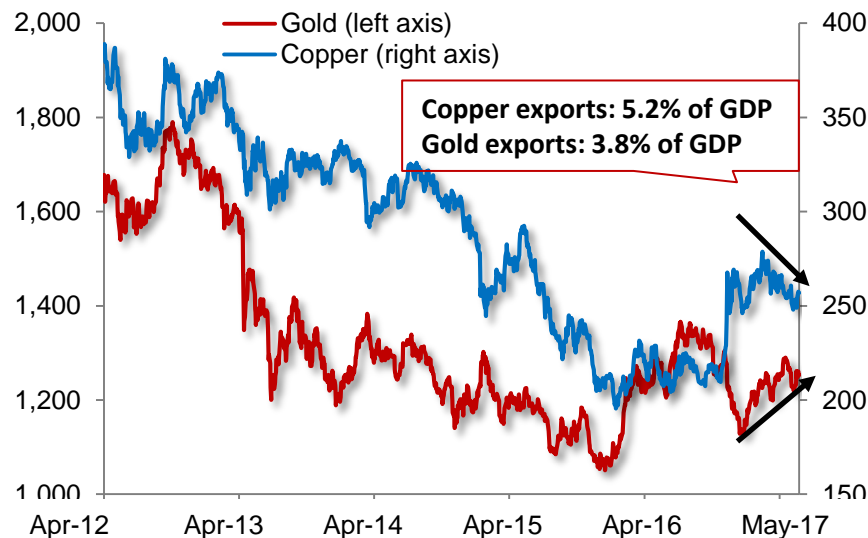
Export prices index

(Three-month moving average of annual % change)



Gold and copper prices

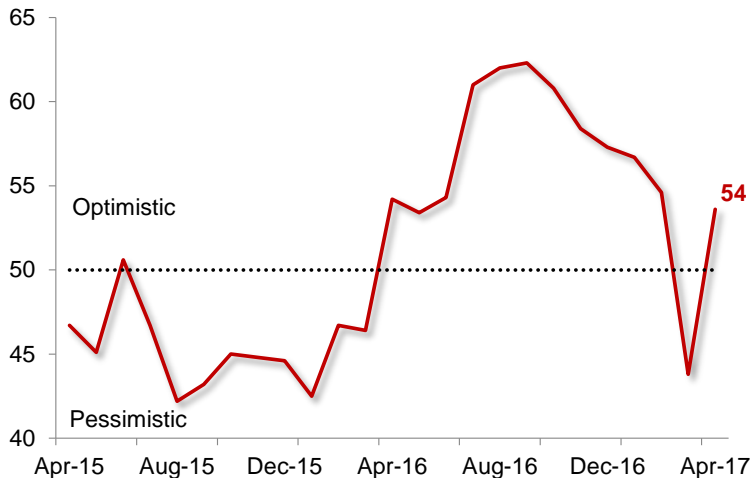
(US\$/troy oz., US\$/lb.)



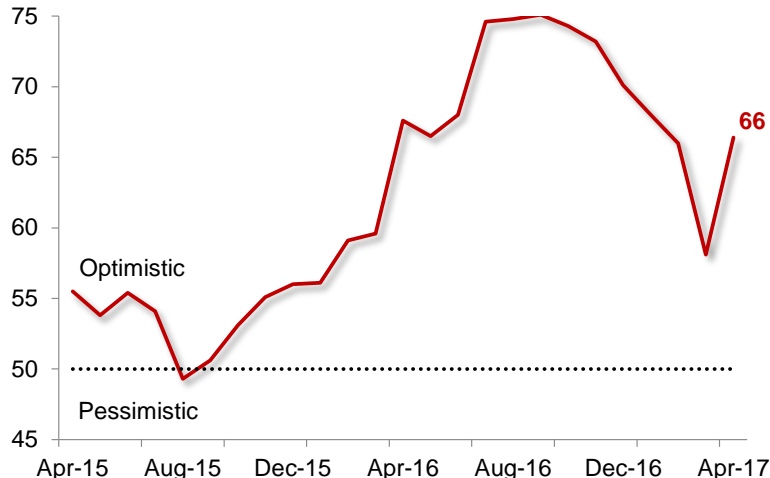
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The expansionary measures taken by the Government and the recent signs of gradual recovery have boosted confidence indicators

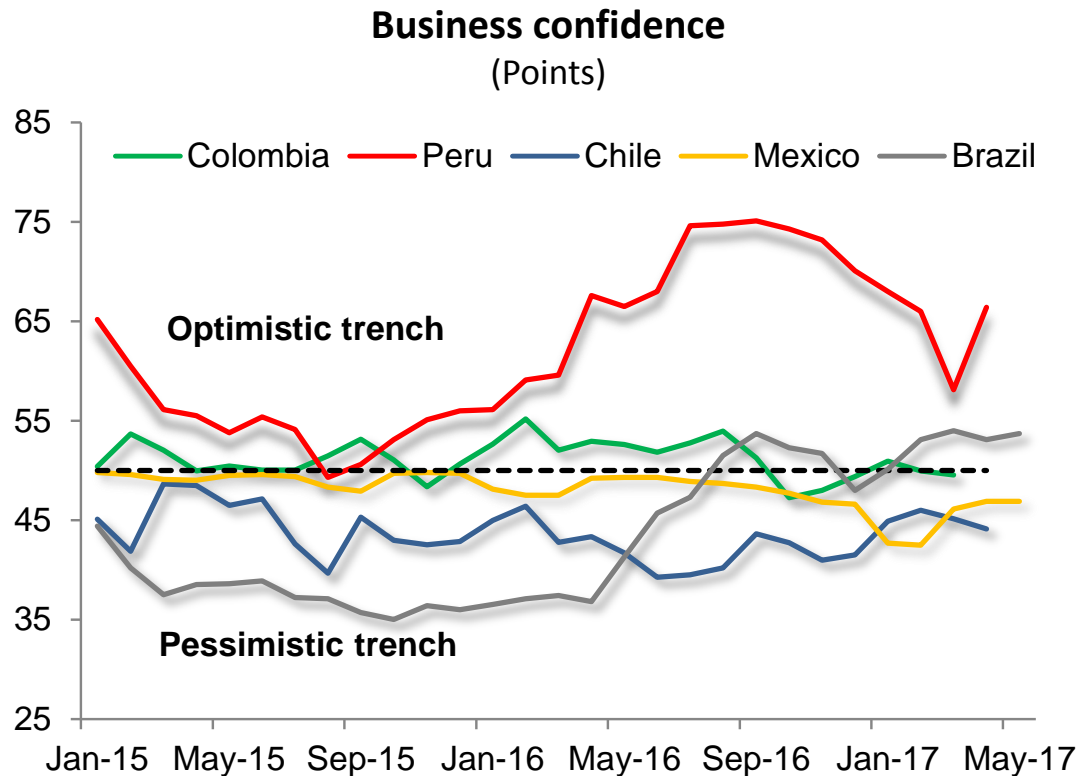
3-month ahead economic expectations
(Points)



12-month ahead economic expectations
(Points)



In fact, business confidence in Peru surpasses its regional peers



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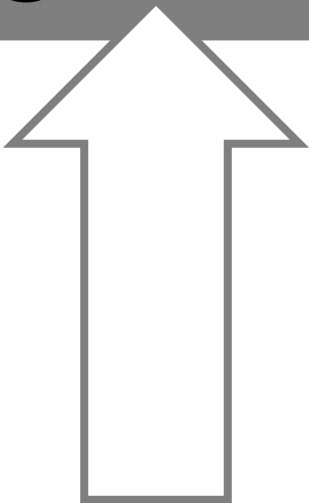
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Three pillars to consolidate the economic growth in the medium term

In a stable macroeconomic framework

3 The Reconstruction Plan

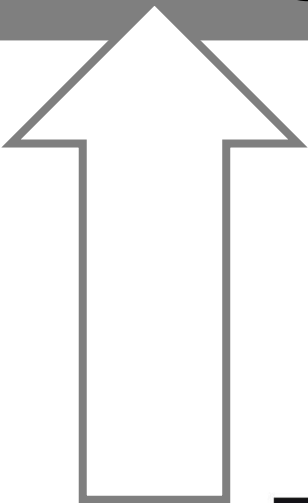
1 Accelerate investment: Infrastructure and mining



- National Infrastructure Plan
- Infrastructure Fund
- Creation of Invierte.pe
- Reform of PPPs and Work for Taxes
- Unlock projects already awarded
- Environmental regulation for mining exploration

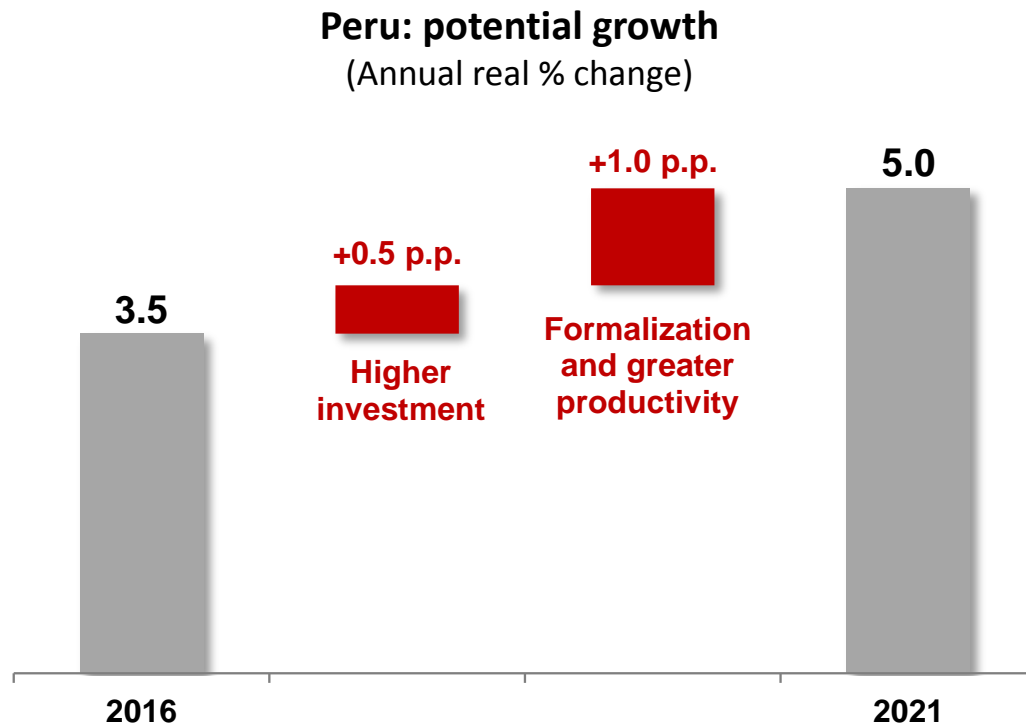
Increase formalization: Competitiveness shock

2



- Tax System Reform
- SUNAT Transformation
- Improvement of the Social Security System
- Red tape removal

Implementing structural reforms will increase potential growth...

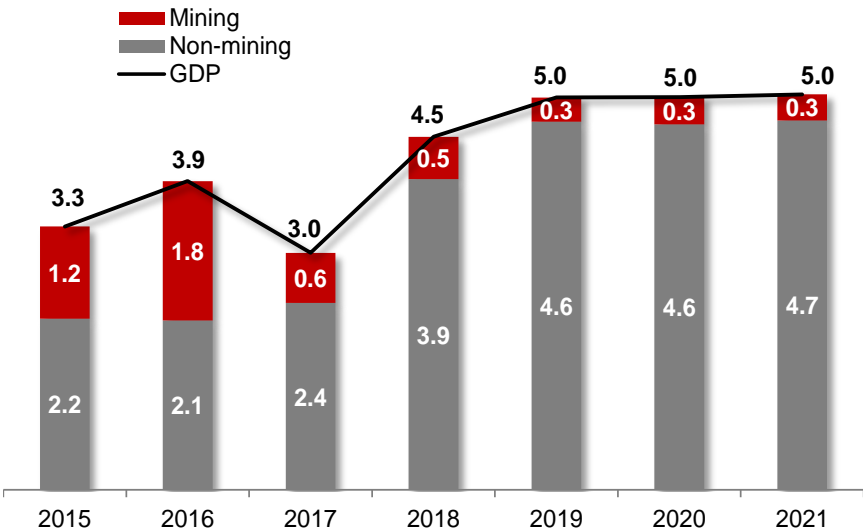


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... and diversify the engines of growth

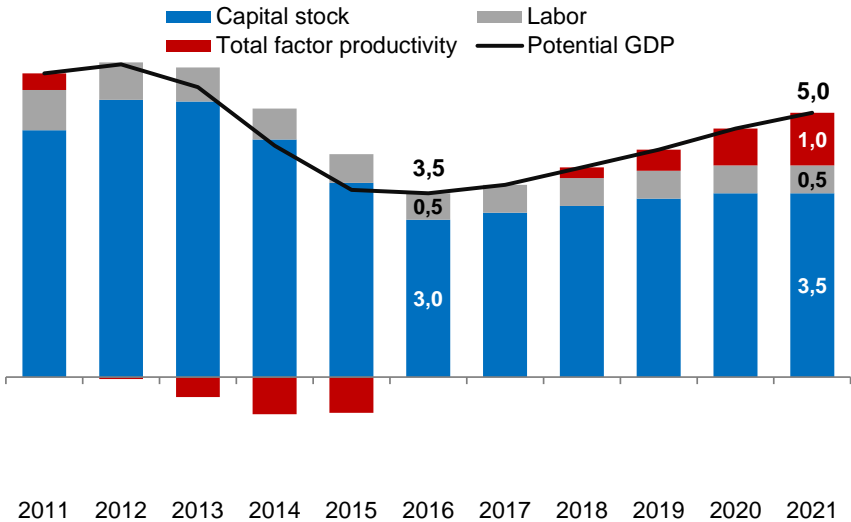
GDP Peru

(Annual real % change, contribution in percentage points)



Potential GDP growth

(Annual real % change, contributions in percentage points)



Source: BCRP, MEF forecasts.

1. Accelerate investment

Nov.16

D.L. N° 1250

Strengthen the Work for Taxes mechanism

D.L. N° 1251

Strengthen of PPPs and projects on assets

D.L. N° 1252

Creation of 'Invierte.pe'

Jan. 17

D.L. N° 1333

APIP

D.L. N° 1334

Creation of "Fondo de Adelanto Social"

D.L. N° 1341

The new Procurement law

Feb.17

D.S. N° 022-2017-PCM

Creation of the Vice-Ministry of
Territorial Governance

D.S. N° 027-2017-EF

Regulation of the national system of multi-annual programming
and investment management

Mar.17

D.S. N° 036 - 2017-EF

Regulation of Work for Taxes

D.S. N° 068 - 2017-EF

Regulation of PPPs and projects on assets

D.S. N° 056 - 2017-EF

Regulation of The Procurement law

Portfolio of mining projects accounting for
US\$ 18,700 million

PPP
Project portfolio in 2017-2018: US\$ 14,410 million

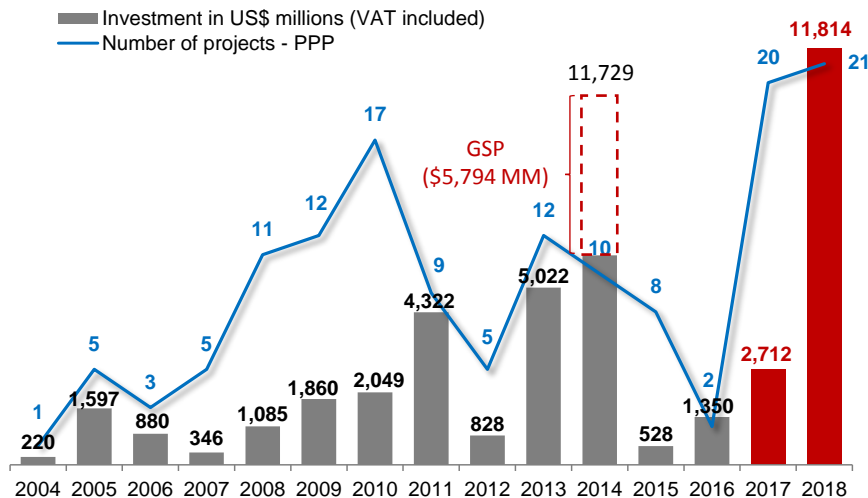
May.17

R. M. N° 169-2017-MEM

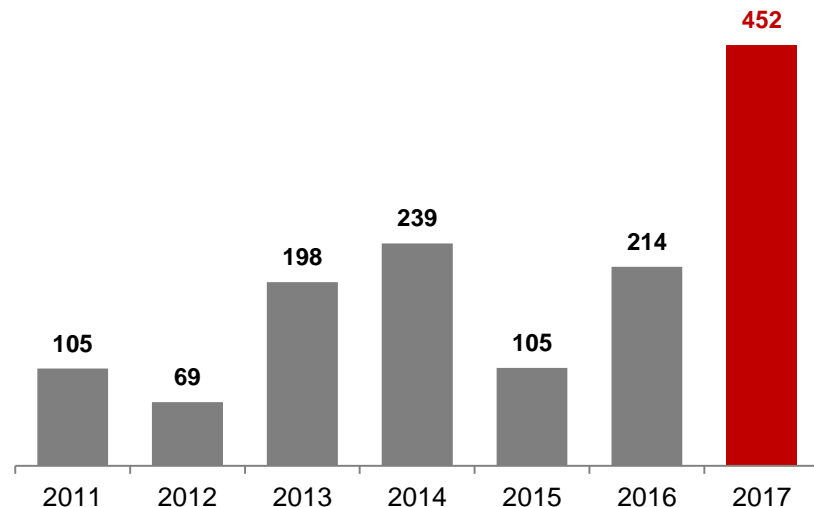
Environmental Protection Regulation for mining exploration activities

An important pipeline of infrastructure projects will be awarded in the next months under a more modern institutional framework

Public-Private Partnership projects¹
(Number of projects, US\$ million)



Works for taxes¹
(US\$ million)

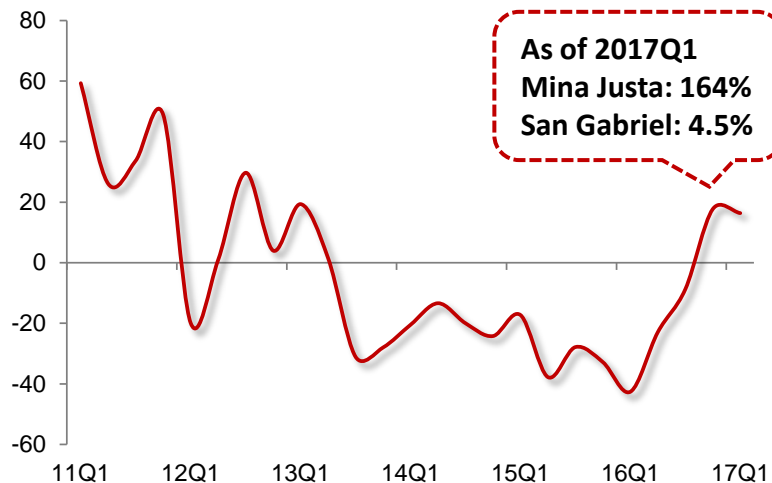


1/ Red bar indicates forecasts and targets set by ProInversion. PPPs do not include Michiquillay for 2017 neither Colca nor Jalaoca for 2018.

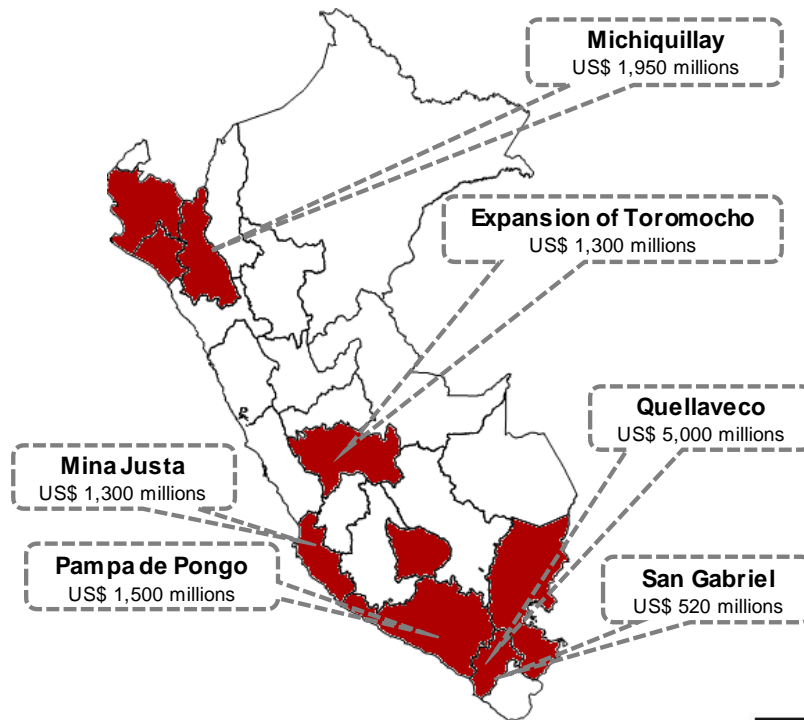
Source: ProInversion.

A new cycle of mining investment is expected in the coming years due to higher metal prices, low cash cost and policy measures

Investment in mining exploration
(Annual % change)



Main prioritized mining projects over US\$ 18 billion portfolio



2. Increase formalization

Dec.16

D. L. N° 1269

Creation of the new tax regime for Micro and Small enterprises

D. L. N° 1259

Special regime for VAT recovery

D. L. N° 1264

Repatriation of capital regime

D. L. N° 1257

FRAES

D. L. N° 1258

Deductions for personal income tax

Jan. 17

R. M. N° 017-2017-EF/10

Call for a Social Protection Committee

Feb.17

D. S. N° 026-2017-EF

Regulation of the "IGV Justo"

Mar.17

Economic Stimulus Plan

Flexible credit line for medium and small enterprises conditional to new tax regime

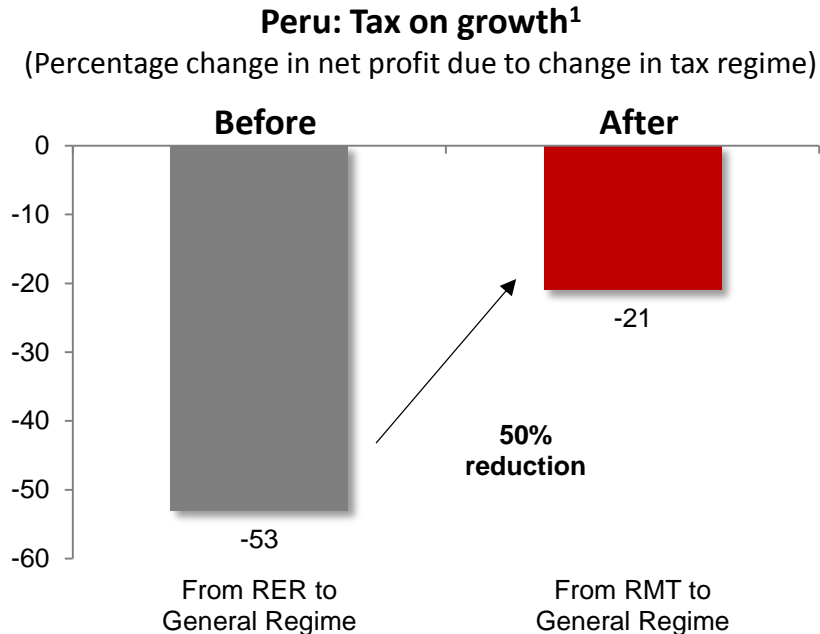
D.S. N° 049-2017-EF

Regulation of FRAES

D.S. N° 067-2017-EF

Regulation of repatriation of capital

Formalization strategy seeks the reduction of tax distortions faced by micro and small enterprises



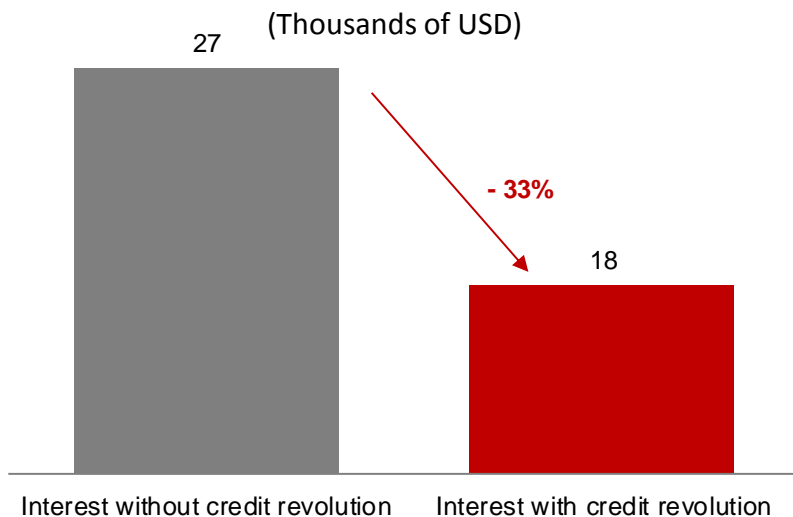
Tax reform strategy includes:

- Increase of the tax base through the formalization of the value chain.
- Use of invoices and electronic payment vouchers.
- More progressive regime.
- Reduced compliance costs.

¹/ RER accounts for Special Regime and RMT accounts for the new MSE Tax Regime.
Source: Pagés (2010), SUNAT, MEF.

Credit constraints on formal firms will be eased through a “Credit Revolution” that reduces financing cost and boosts credit supply

Impact of the “Credit Revolution” over financial costs for MSEs¹



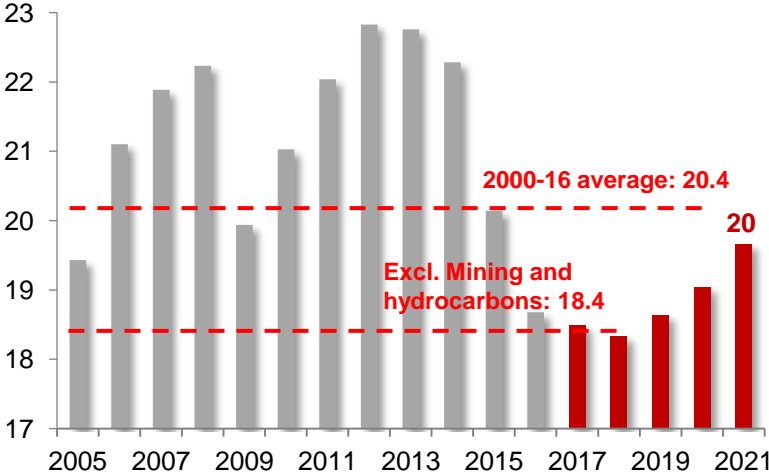
The “Credit Revolution” includes:

- Credit lines provided by the Development Bank of Peru (COFIDE) for more than US\$ 240 million with lower interest rates to reduce the cost of financing for micro and small enterprises.
- VAT refund for the acquisition of machinery and equipment.
- “Bono de Buen Pagador”.

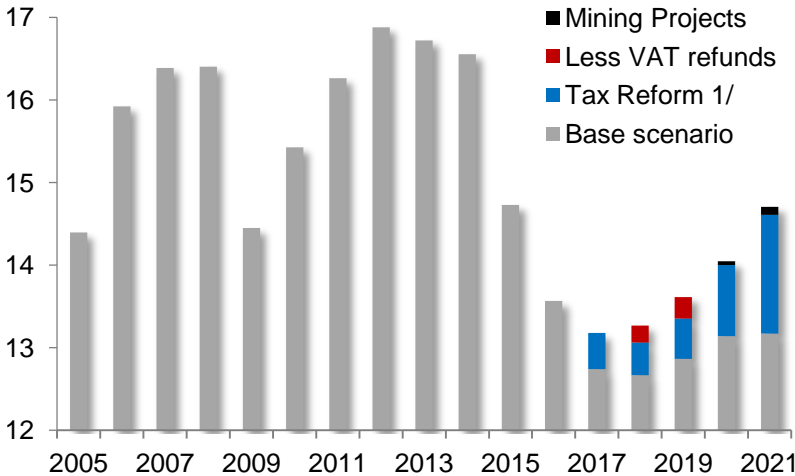
^{1/} It takes for assumption a credit of USD 30 thousand to be paid in 5 years at an interest rate of 33%. The credit revolution includes the benefits for good payer bonus and VAT refunds. It is assumed only one change over the credit principal.

Increasing formalization will permanently boost fiscal revenues in the medium term

General Government Revenue
(% of GDP)

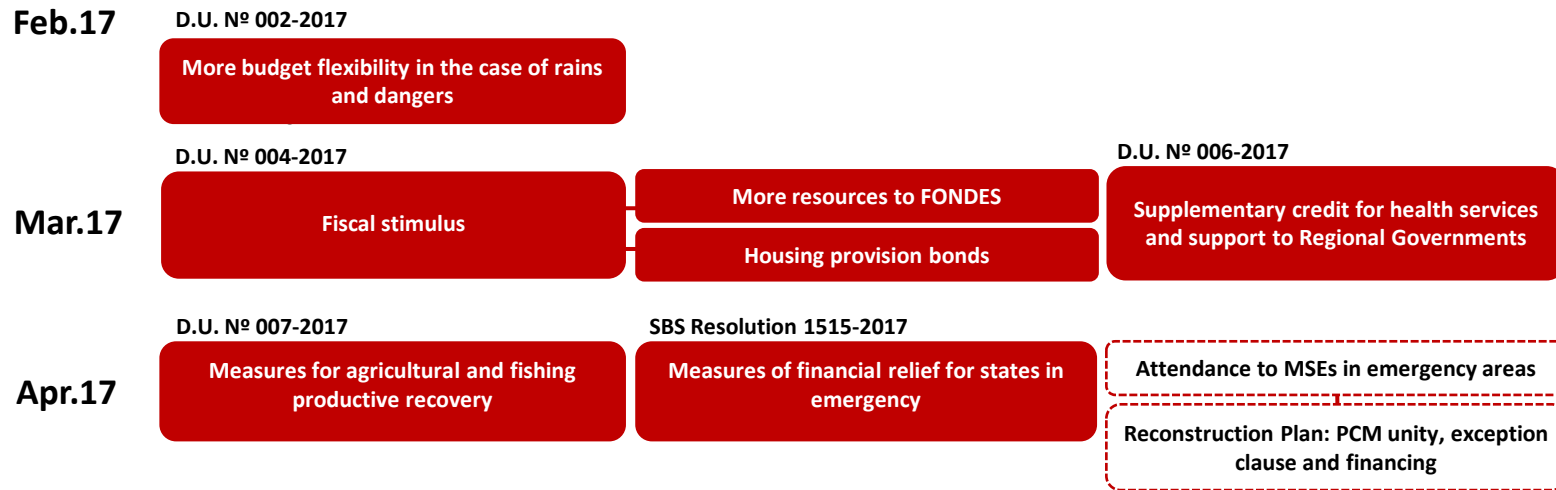


Central Government Tax Revenue
(% of GDP)



1/ It Includes revenues from capital repatriation and the deepening of this tax reform.
Source: SUNAT, BCRP, MEF Forecasts.

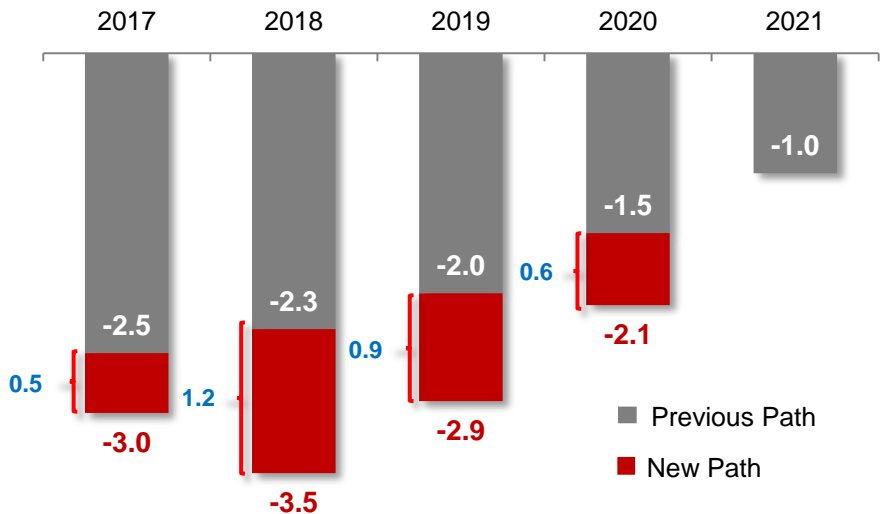
3. The Reconstruction Plan



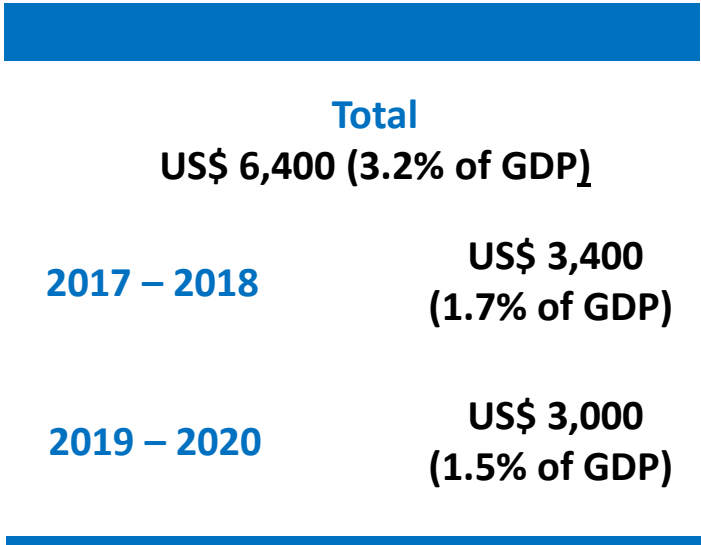
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First, the fiscal deficit will widen by 3.2% of GDP between 2017-2020 to finance the reconstruction plan...

Non-Financial Public Sector Overall Balance
(% of GDP)



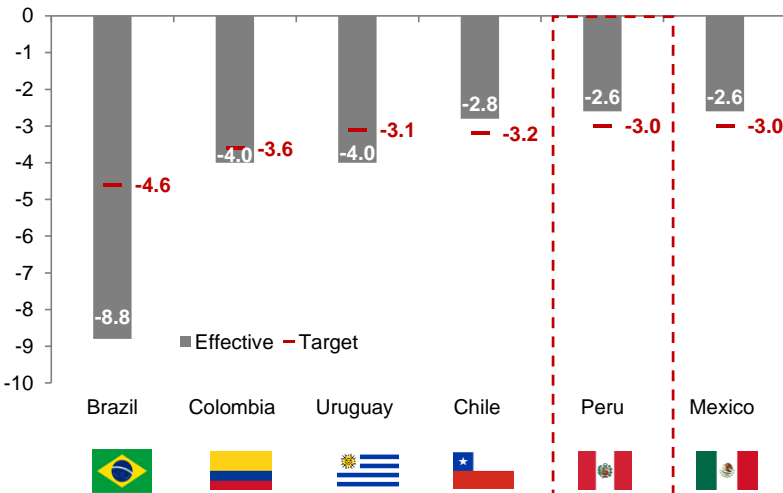
Allocation to FONDES^{1,2}
(US\$ Millions, % of GDP)







1/ FONDES: Fondo para Intervenciones ante la Ocurrencia de desastres naturales. It is an intangible fund to finance interventions in case of natural disaster events.
 2/ Estimates consider 2017 nominal GDP forecast.
 Source: MEF.

...without hurting our macro and fiscal stability

Overall fiscal balances and its targets¹, 2016
(% of GDP)



Credit Rating Outlook

	S&P	Moody's	Fitch
 Peru	Stable	Stable	Stable
 Chile	Negative	Stable	Negative
 Mexico	Negative	Negative	Negative
 Colombia	Negative	Stable	Stable

1/The fiscal deficits have the following coverage: Central Government (Chile, Colombia), Non-Financial Public Sector (Peru, Brazil), Federal Public Sector (Mexico), and Consolidated Public Sector (Uruguay). Also, the fiscal targets shown are the ones established in 2015 for the formulation of 2016 public budget.
Source: MEF, Ministries of Finance of other countries, Bloomberg.

With significant financial assets (17% of GDP) and low debt, the government can finance the reconstruction without surpassing the debt limit of 30% of GDP

Financial assets and debt items that could be used quickly to finance the fiscal deficit

Concept	% of GDP
1 Contingent Credit Lines	2.1
2 Savings of non financial public sectors	2.3
3 Fiscal Stabilization Fund (FEF)	4.2
Total (1+2+3)	8.6

The Reconstruction Plan will be a key driver to accelerate the execution of public spending projects in the coming years

Who manages the resources?

Without the Plan

- Ministries, Subnational Governments

With the Plan

(Reconstruction Law)

- Centralized resources in just one fund

Who designs and executes the reconstruction?

- Ministries, Subnational Governments

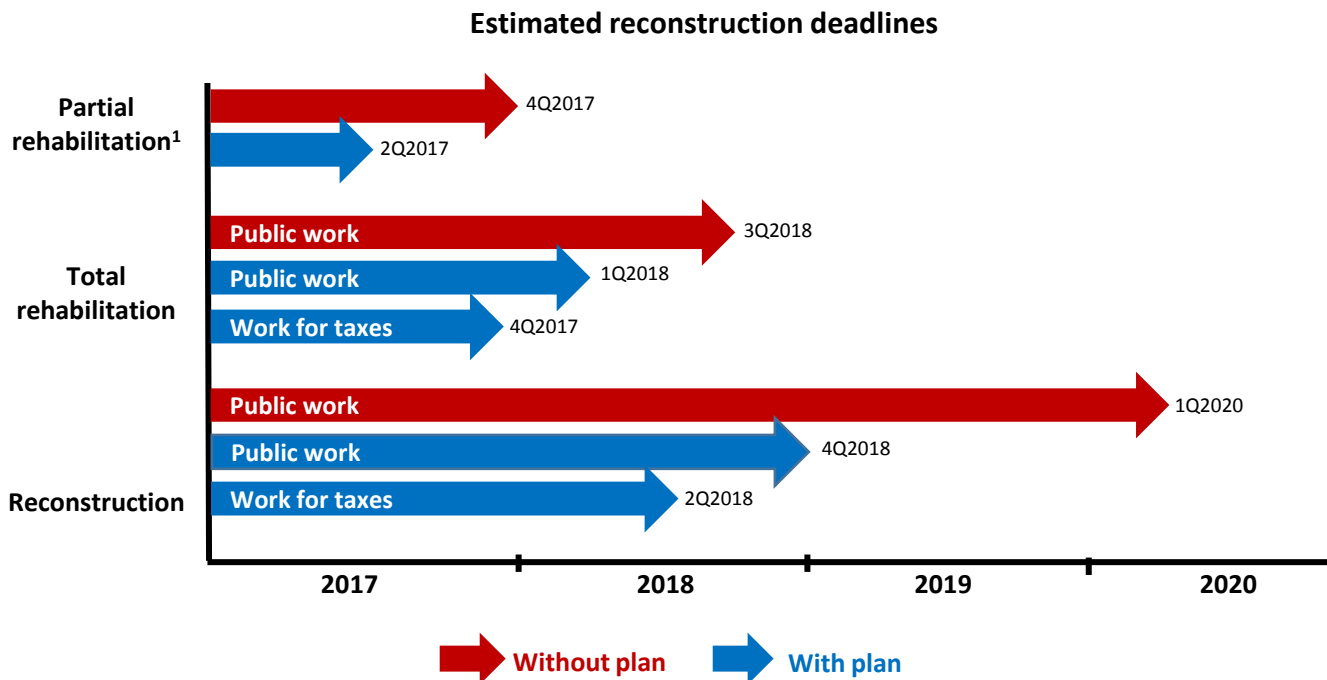
- One entity decides what, who and through which modality it is executed

Which are the costs and benefits?

- Project atomization
- Low implementation
- Absence of capacity of monitoring the Executive branch

- It facilitates the transmission of resources to suppliers.
- Centralized plan:
 - ✓ In order to make something better than before
 - ✓ Includes territorial planning and prevention

The Reconstruction Plan will reduce the estimated deadlines for the start of reconstruction up to 50%



1/ Maintenance of general infrastructure and equipment reposition.
Source: Apoyo Consultoría and experts in public investment, MEF.

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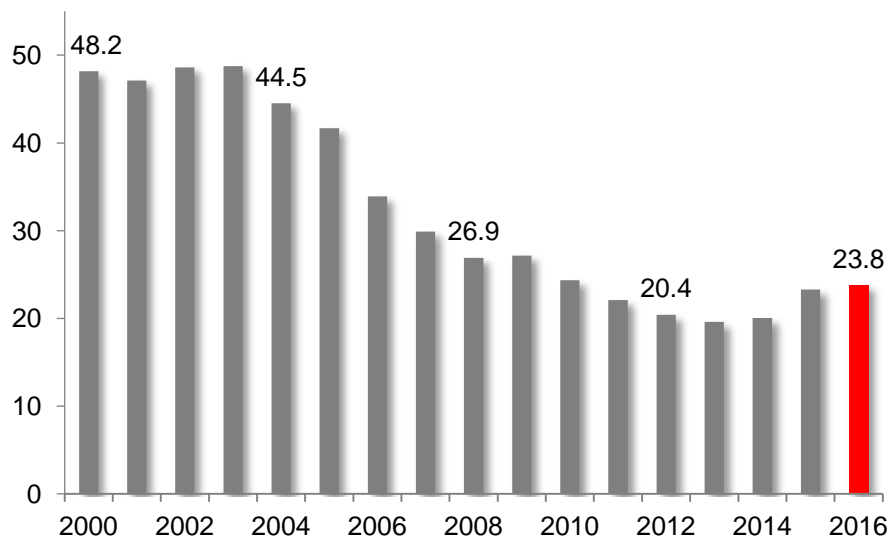
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Capital markets reform

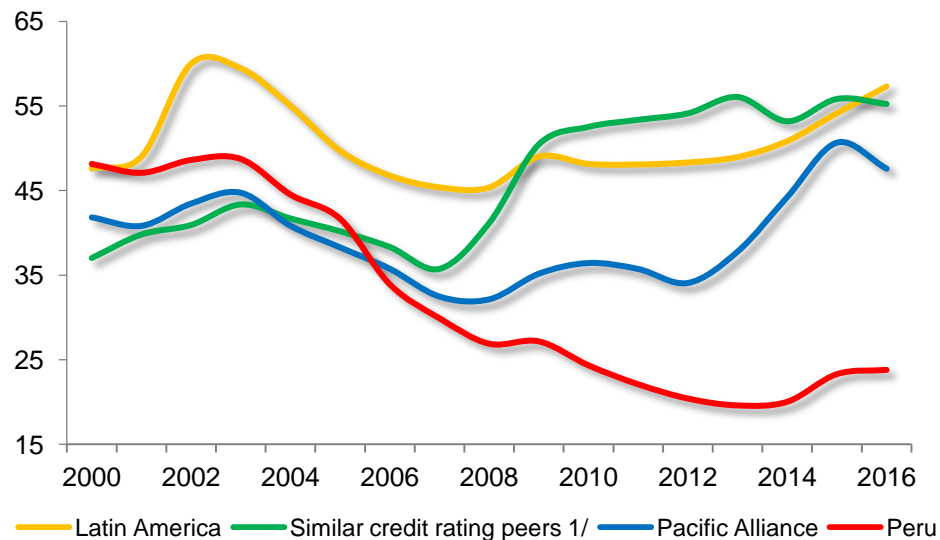
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Peru is in a sound fiscal position with a public debt to GDP ratio well below its regional peers and economies with similar credit rating

Peru: Public Debt
(% of GDP)



Public Debt, 2000-2016
(% of GDP)



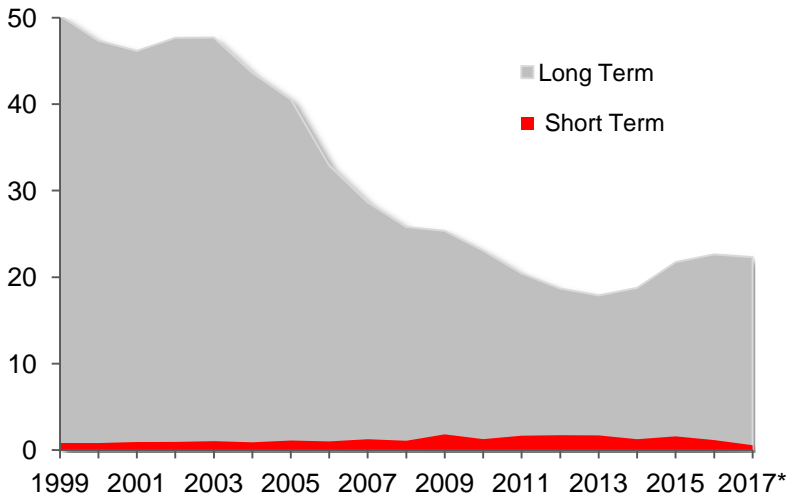
1/ Similar credit rating peers include economies with A3 credit rating by Moody's and BBB+ by S&P Global Ratings and Fitch Ratings.

Source: IMF, BCRP.

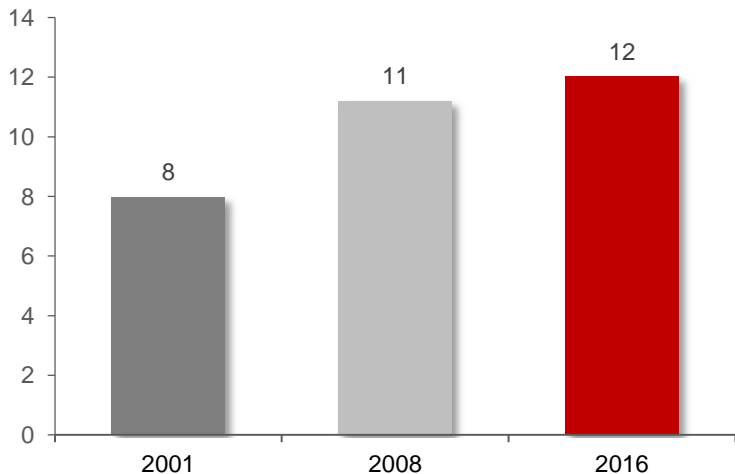
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The treasury expects debt levels to remain low and below its regional peers as debt profile and composition remain solid

Short-term and Long-term Debt
(% of GDP)



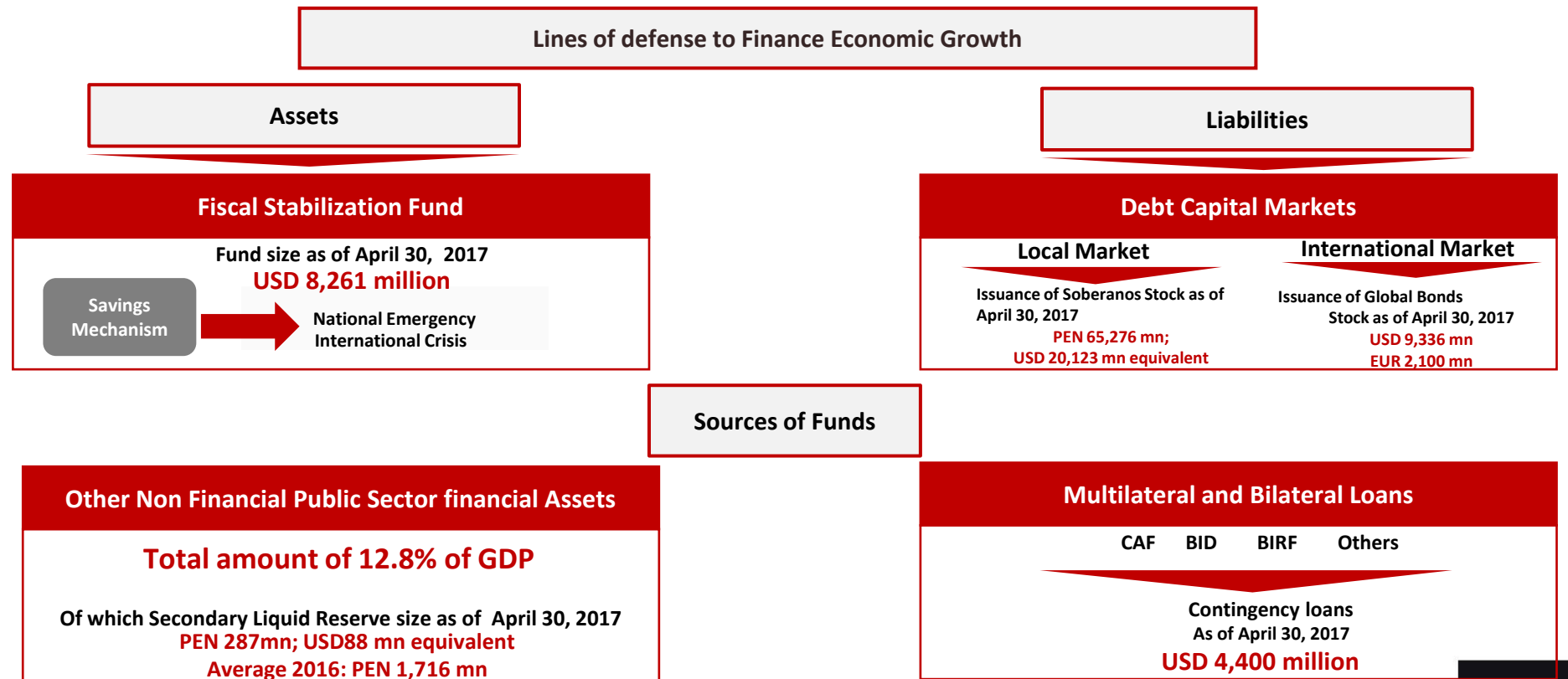
Debt Average Term to Maturity
(Years)



* BCRP March 2017.
Source: BCRP.

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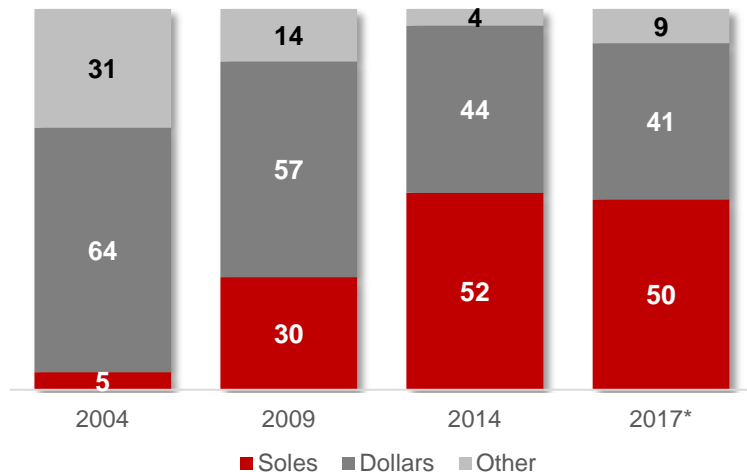
The sources of financing come from asset management and internal and external liabilities



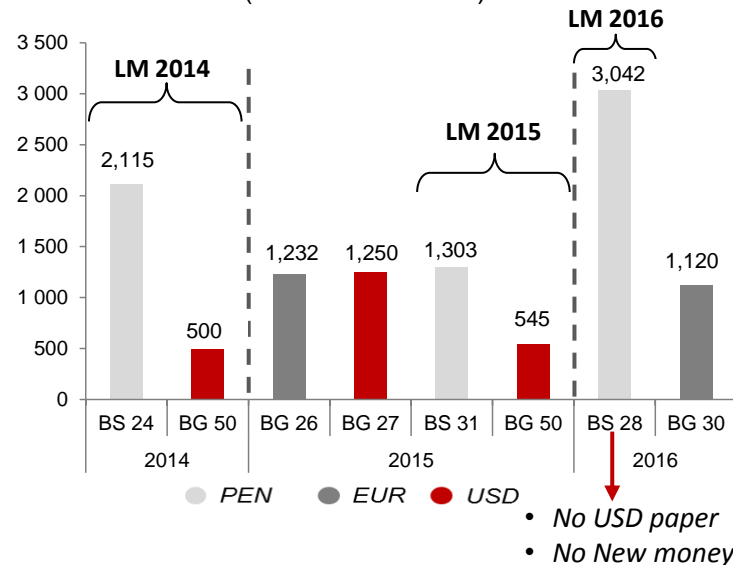
Source: BCRP, MEF.

"Solarize" debt and develop local debt capital markets

Composition of Public Debt by Currency
(% of total debt)



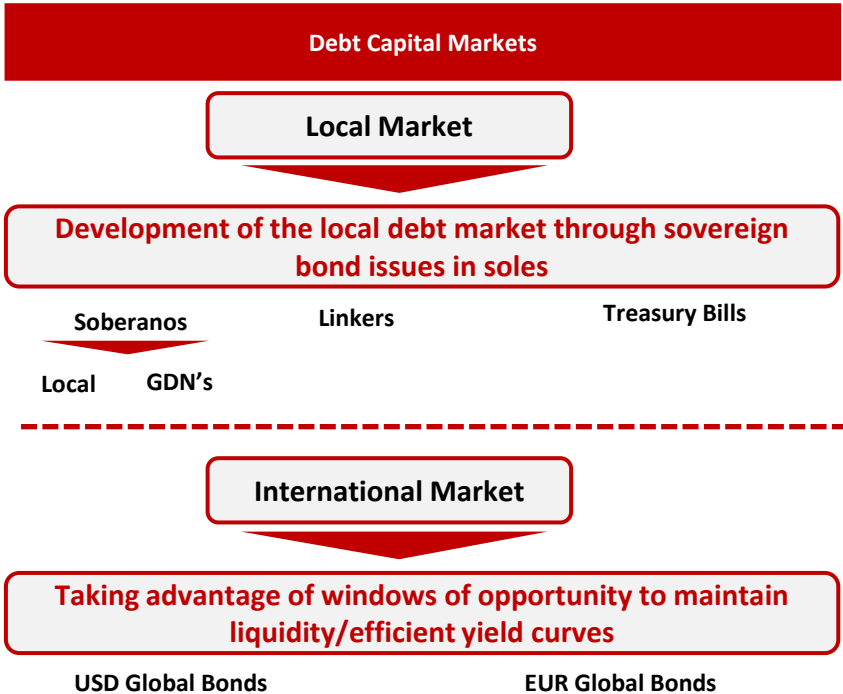
Liability Management (LM) 2014 – 2016
(Millions of dollars)



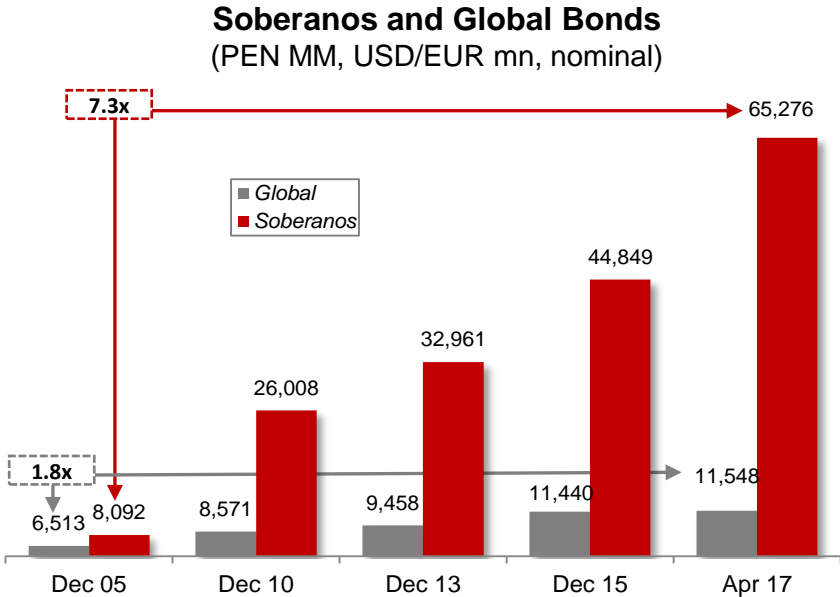
* MEF-March 2017.
Source: MEF.

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Peru has significantly increased its Soberano (PEN) debt stock by focusing on international format debt issuances (GDNs)

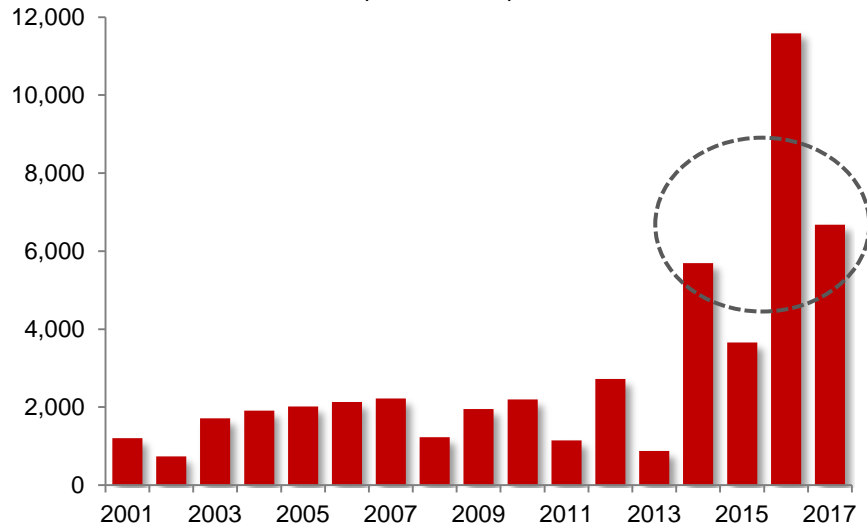


Since 2005, Peru has successfully increased its Soberanos (PEN) debt stock by 7.3x compared to a growth of 1.8x for its Global Bond (USD and EUR) debt stock...

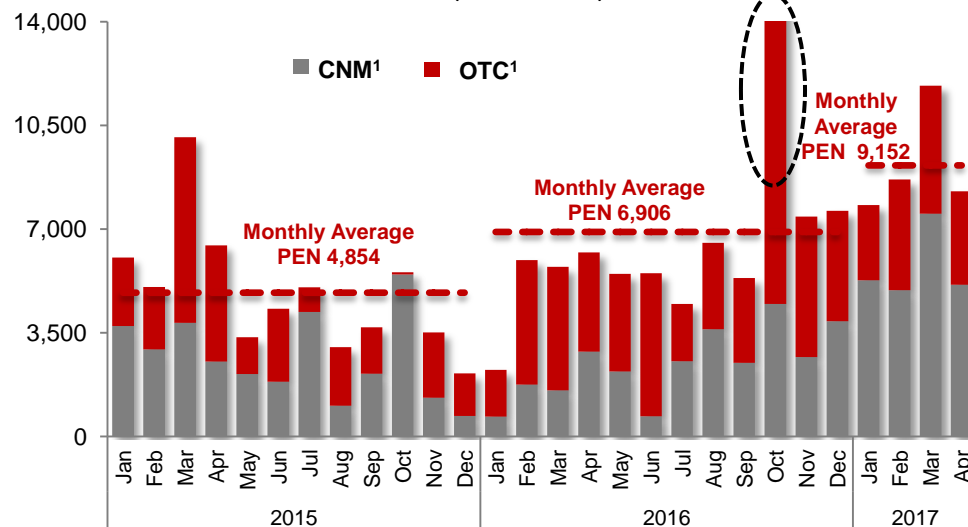


Peruvian Sovereign Bonds in local currency

Primary Market Activity
(PEN million)



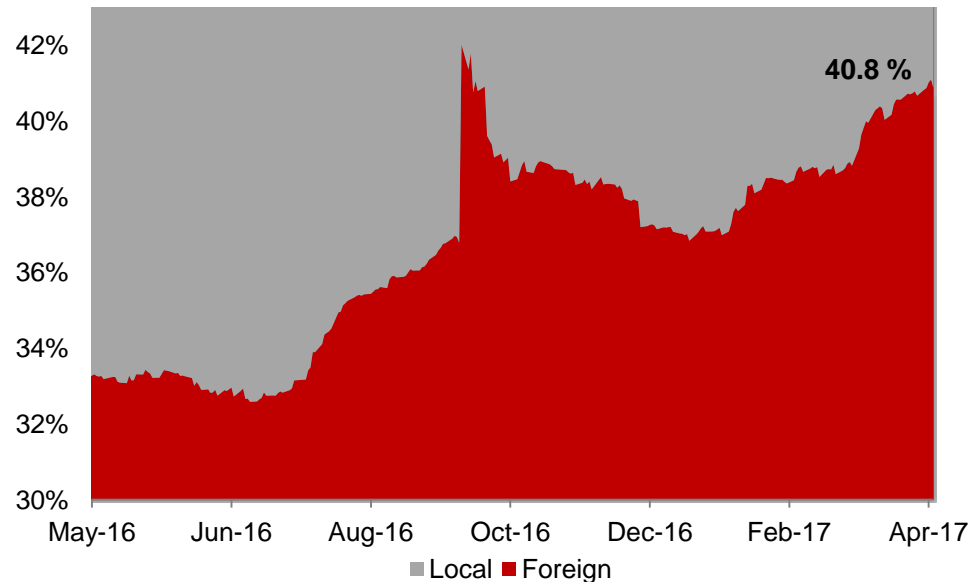
Secondary Market Activity
(PEN million)



- In the last 3 years, sovereign bond trading has increased in volume. The monthly average trading in 2015 was PEN 4,853 mn, in 2016 PEN 6,906 mn, while in the first four months of 2017 it was PEN 9,152 mn.
- This is in line with the primary market activity which also increased the volume of the annual issuances in that years.

Diversification of non-resident investor base for local bonds

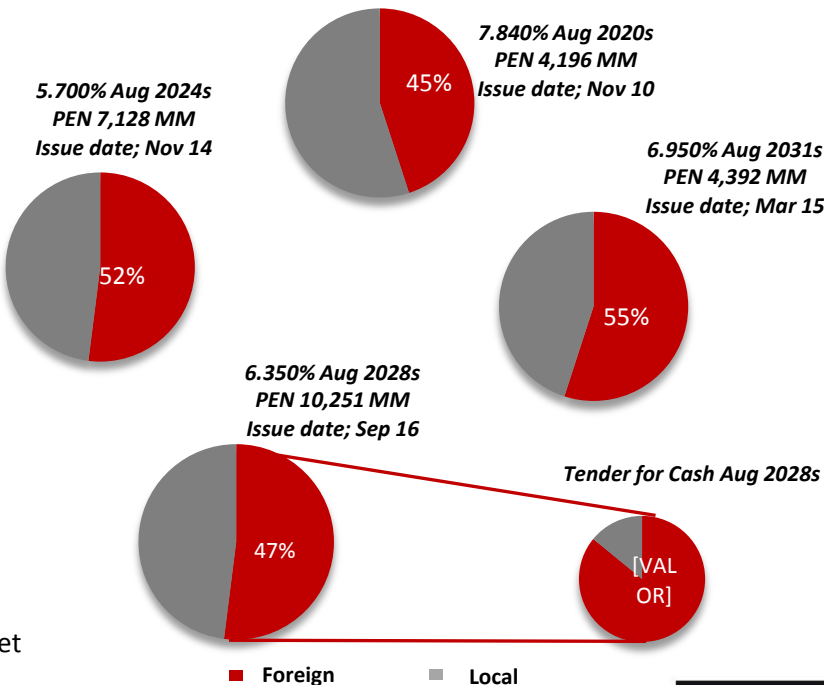
Historical Series of Holdings – Soberanos Bonds
(% by investor class)



- PEN-denominated international issuances have further developed the PEN market and significantly increased foreign-ownership of bonds.

Source: MEF, Bloomberg.

Foreign Ownership Holdings – Soberano Bonds
(% by investor class)



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The government will continue to develop the local market and strengthen its position as one of the leading issuers in the region

Action Plan to Enhance Public Debt Market

1	Repurchase Agreement (REPO)	Develop and increase repo transactions (i.e. Repo to term).
2	Sovereign Debt Fund	Develop Peruvian Treasury Index / Securities Lending.
3	Market Maker Program	Increase the depth and liquidity of including treasury bills.
4	Liability Management Exercises	Manage debt stock to optimize cost and debt profile.
5	Relevant Benchmarks	Issue benchmarks with large volumes (To increase liquidity).
6	International Settlement Platforms (Euroclear, Clearstream)	Diversify investor base.

Next steps:

7	Securities Lending / Short Selling	Provide liquidity to the secondary market.
8	Liability Management in local market	Optimize debt profile.

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Developing a competitive local capital market

Local market strengthening	Local market sophistication	Integration strategy
<ul style="list-style-type: none"> Development of financial schemes for infrastructure and SME financing. 	<ul style="list-style-type: none"> Development of more sophisticated products, channels and processes. 	<ul style="list-style-type: none"> Strengthen the integration process with strategic partners, such as the Pacific Alliance - PA.
<ul style="list-style-type: none"> Diversify the set of available financial products. 	<ul style="list-style-type: none"> Improve the framework of incentives to promote a more active participation in the local market. 	
<ul style="list-style-type: none"> Increase the participation of local and foreign investors. 	<ul style="list-style-type: none"> Sophistication of participants. 	



Promote greater liquidity in the capital market

By leveling the playing field with traditional financial instruments

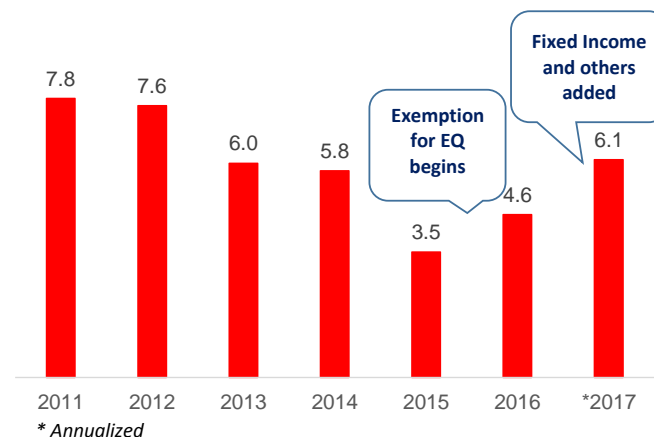
Tax incentives:

- Capital gains tax exemption for equity, fixed income, listed mutual funds, REITs and receivables listed in public exchanges.
- REITS and factoring tax structure for individuals, including via investment funds and trusts.

Benefits:

- Greater liquidity in the Lima Stock Exchange.
- Aligning the tax structure to that of our partners in the Pacific-Alliance.

Value traded in the Lima Stock Exchange
(In US\$ Billions)



Enhancement of the capital market's depth and diversity

By developing new products and segments

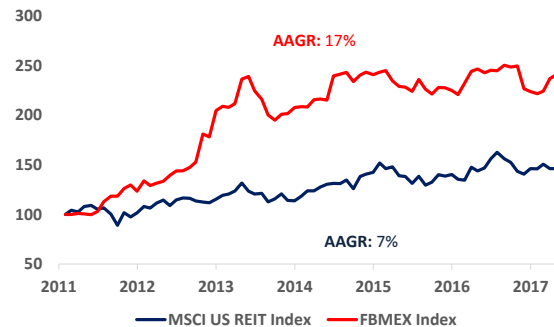
- **REITs¹:** Better regulatory framework:
 - Investment funds: 2 operating, US\$ 30 million AUM, starting in 2016
 - Trusts: created in 2016, based on Mexican FIBRA

Tax incentives for REITs (capital gains and deferral of income and real-estate taxes).

- **Factoring:**
 - Improving operational regulation
 - Promoting electronic issuance systems
 - Tax incentives for individuals (5%), including via investment funds and trusts

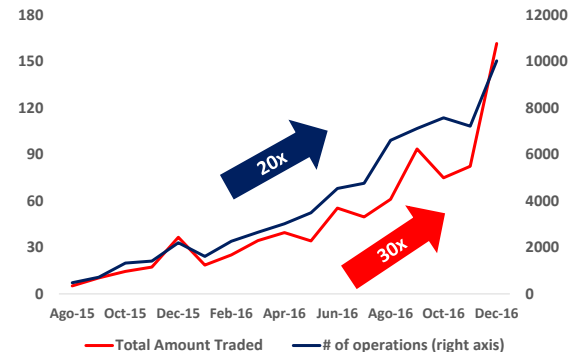
¹/ Real Estate Investment Trust
Sources: Bloomberg, MEF.

Potential of REITs in emerging markets
(Index 2011=100)



AAGR: Annual Average Growth Rate

Factoring market development
(Millions of US\$)





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Ministerio
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PERU

Preserving Sustained Growth and Macroeconomic Stability

Mr. Alfredo Thorne

Minister of Economy and Finance

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InPerú