
REPUBLIC OF PERU



Recent Economic Developments and Forecast

Fernando Zavala
Minister of Economy and Finance

EMTA Annual Meeting
New York

December 2005

Agenda

- ✓ **Robust economic performance**

Public debt reprofiling

Structural underpinnings for continued growth



Macroeconomic policy framework geared toward continued growth and stability

Key Macroeconomic Indicators

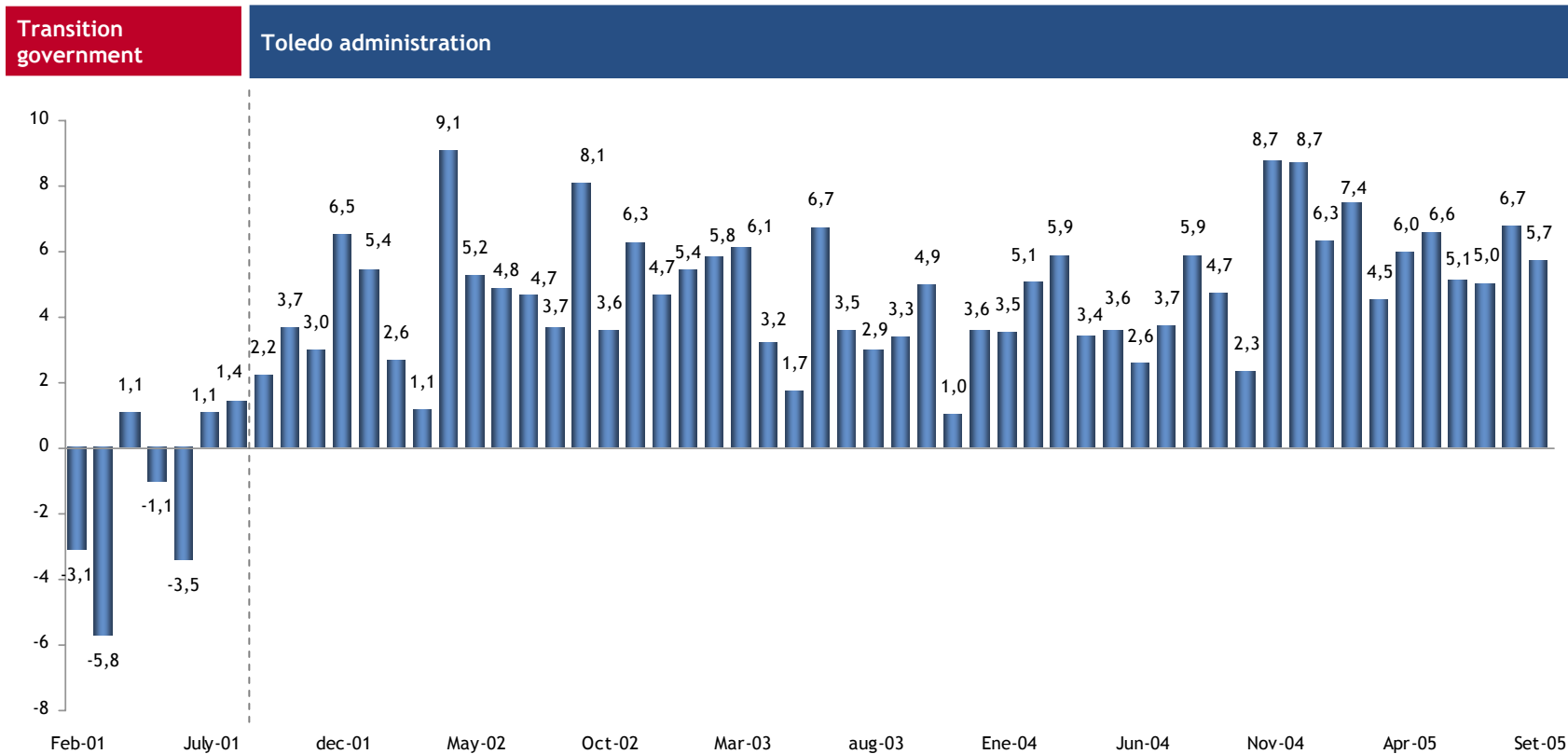
	2001	2002	2003	2004	2005E	2006F	2007F	2008F
GDP growth rate (% , yoy)	0,2	4,9	4,0	4,8	6,0	5,0	5,0	5,0
Per capita GDP (US\$)	2 051	2 112	2 239	2 529	2 744	2 835	2 973	3 025
Current account (% GDP)	-2,1	-1,9	-1,5	0,0	0,3	0,1	0,0	-0,6
Inflation (% change, Dec-Dec)	-0,1	1,5	2,5	3,5	1,4	2,5	2,5	2,5
Exports of goods (% change, yoy)	1,0	9,8	17,8	38,8	32,4	5,2	3,8	5,0
Non-financial public deficit (% GDP)	-2,5	-2,3	-1,7	-1,1	-1,0	-1,0	-1,0	-0,8
Primary balance (% GDP)	-0,2	-0,1	0,4	1,0	1,0	1,2	1,4	1,7
Total public sector debt (% GDP)	46,2	46,9	47,7	45,2	39,2	37,1	36,0	34,3

Source: MEF & Central Bank
(F) Forecast



Rapid economic growth

Over 4 years of uninterrupted economic growth and the best performance in Latin America
Monthly Growth (% yoy)



Source: INEI



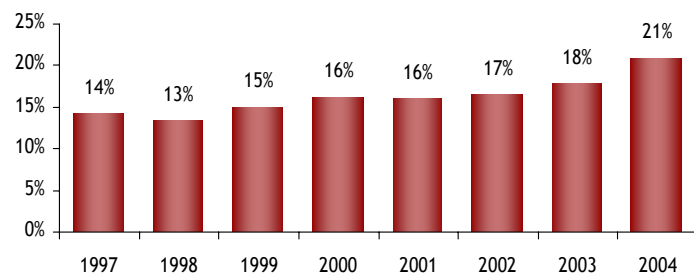
Broad-based sources of growth

Growth has been led by exports, private investment and private consumption. Not by fiscal impulse

y-o-y percent change								
	2001	2002	2003	2004	2005E	2006F	2007F	2008F
Private consumption	1.4	4.6	3.1	3.4	4.1	4.0	4.5	4.5
Exports of goods	1.0	9.8	17.8	38.8	32.4	5.2	3.8	5.0
Private investment	-4.7	0.1	5.6	9.0	12.1	10.0	9.0	9.0

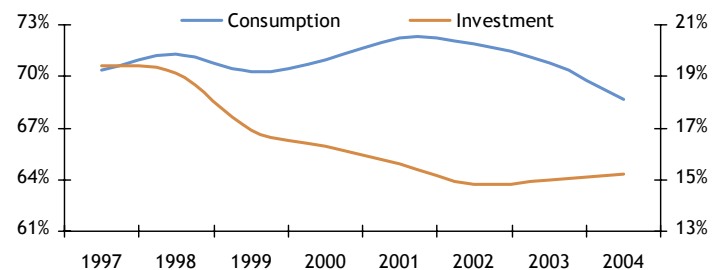
Source: MEF & Central Bank

Exports (% GDP)



Source: Central Bank

Private Consumption and Investment (% GDP)

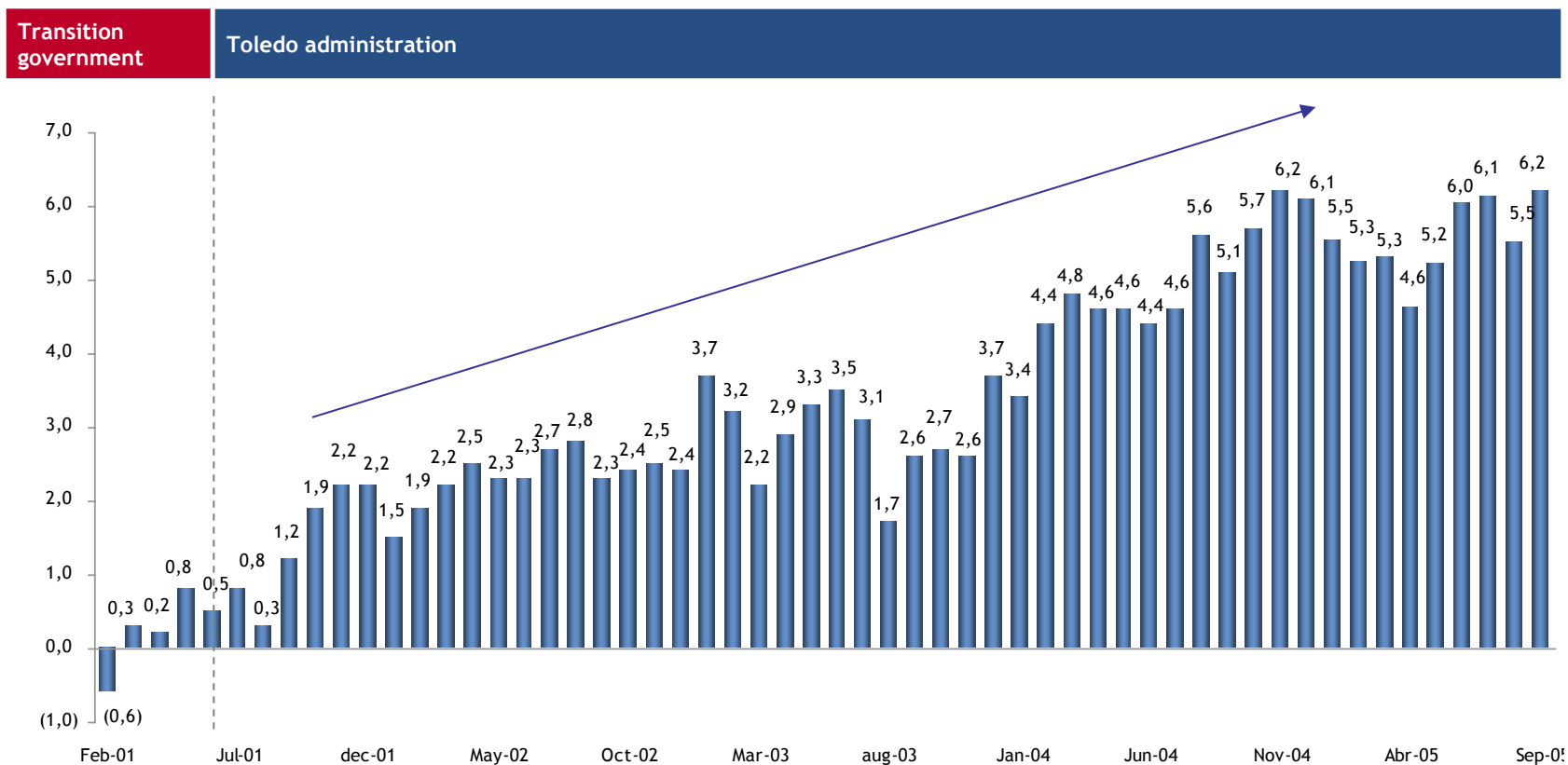


Source: Central Bank



Growth has generated employment

*Monthly employment growth in Lima
(Real growth rate) Companies with more than 100 employees*



Source: INEI



Real income is on the rise

- Growth in real income has strengthened domestic sources of growth.

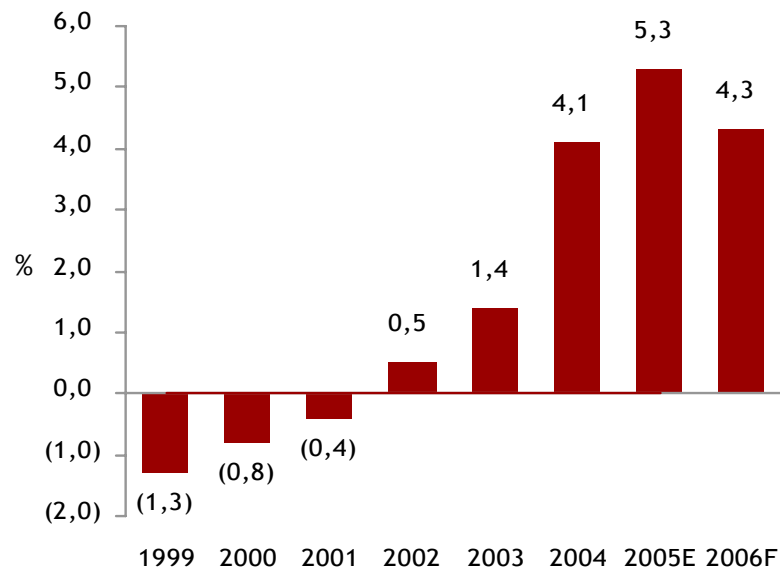
Monthly household income, metropolitan Lima (US\$)						
Population groups	2002	2003	2004	2005	2005 vs. 2002	2005 vs. 2004
A	3 254	3 498	3 505	3 555	9.3%	1.4%
B	816	890	893	913	11.9%	2.2%
C	322	353	389	391	21.4%	0.5%
D	192	203	221	239	24.5%	8.1%
E	143	146	158	163	14.0%	3.2%
Total	419	434	465	508	21.2%	9.2%

Source: Apoyo Opinión y Mercado



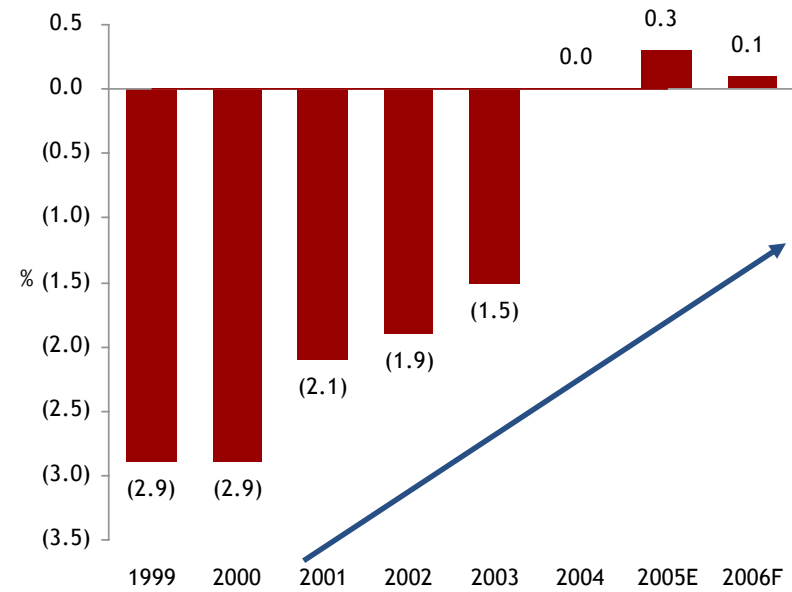
Exports are leading growth

Trade Balance / GDP (%)



Source: MEF & Central Bank

Current Account Balance / GDP (%)



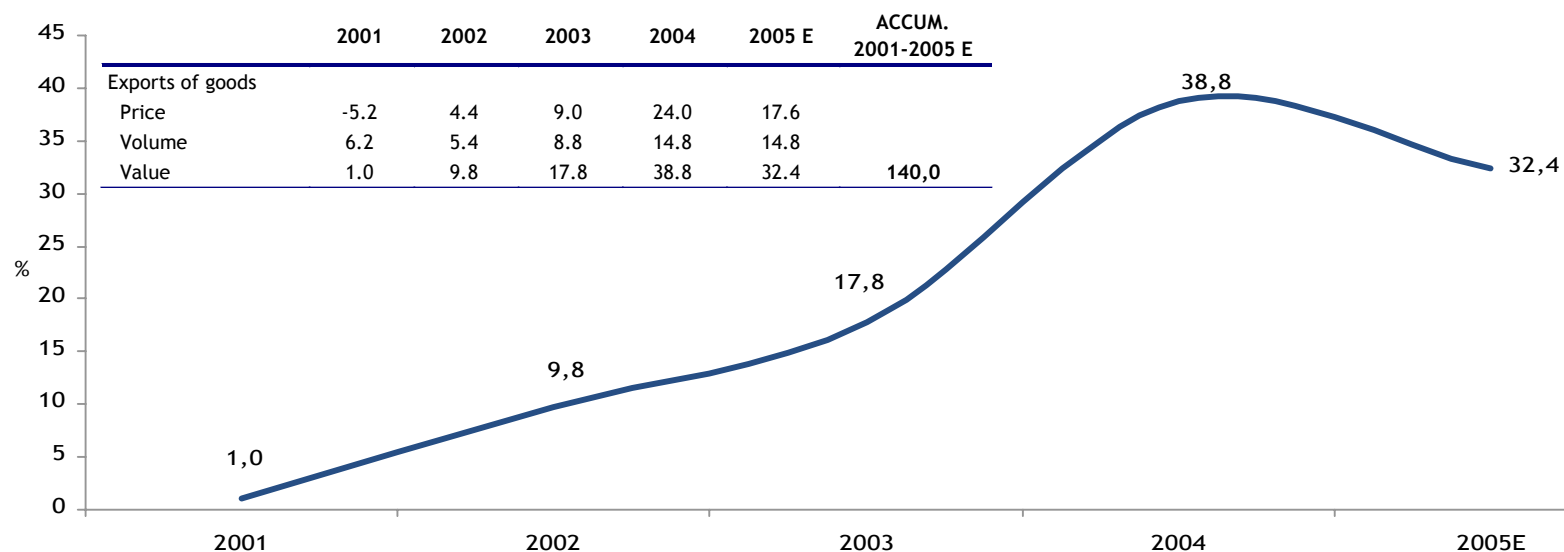
Source: MEF & Central Bank



Exports are leading growth

Both in value and volume terms

Merchandise export (% chg YoY)



Source: MEF & Central Bank

- Export growth has picked up significantly over the past four years
- The main driver behind 2001-2004 export growth has been volume expansion
- More subdued growth is expected in 2005



Diversified export base

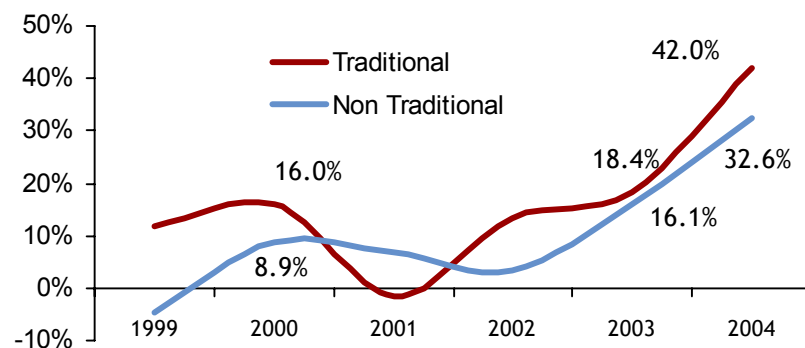
- Non-traditional exports have been an important driver of Peru's export growth

Exports of goods (US\$ MM)

Products	2000	2001	2002	2003	2004
Traditional	4 804	4 730	5 369	6 356	9 028
Fishing	955	926	892	821	1 103
Agricultural	249	208	216	224	325
Mineral	3 220	3 205	3 809	4 690	6 953
Petroleum and derivatives	381	391	451	621	646
Non Traditional	2 044	2 183	2 256	2 620	3 476
Total	6 955	7 026	7 723	9 091	12 617

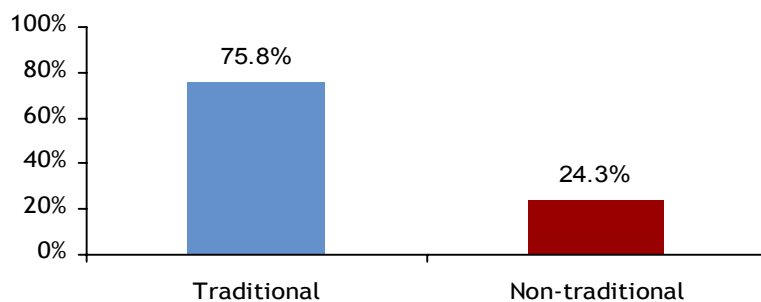
Source: Central Bank

Traditional and non traditional export growth (1999 - 2004)



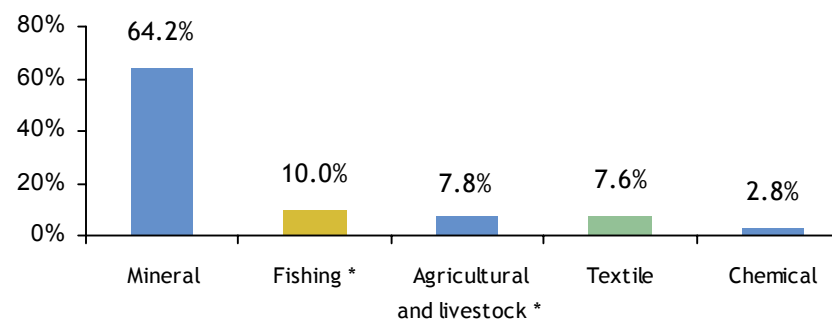
Source: Central Bank

Contribution to export growth (2003 - 2004)



Source: Central Bank

Contribution export growth by product group (2003 - 2004)



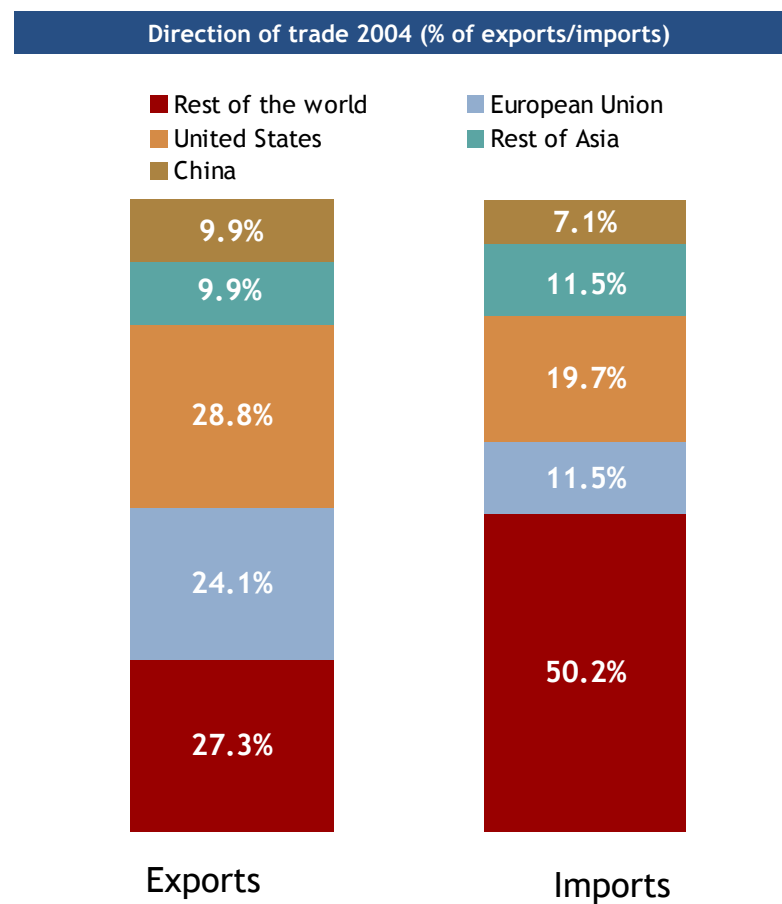
Source: Central Bank

* Considered traditional and non traditional goods



FTA provides good prospects for the export sector

- Consolidation of preferential access to the US market (major commercial partner with 28.8% of exports)
- Consolidation of trade openness
- Next steps: Negotiations with EU and possibly Asian APEC nations (Thailand)

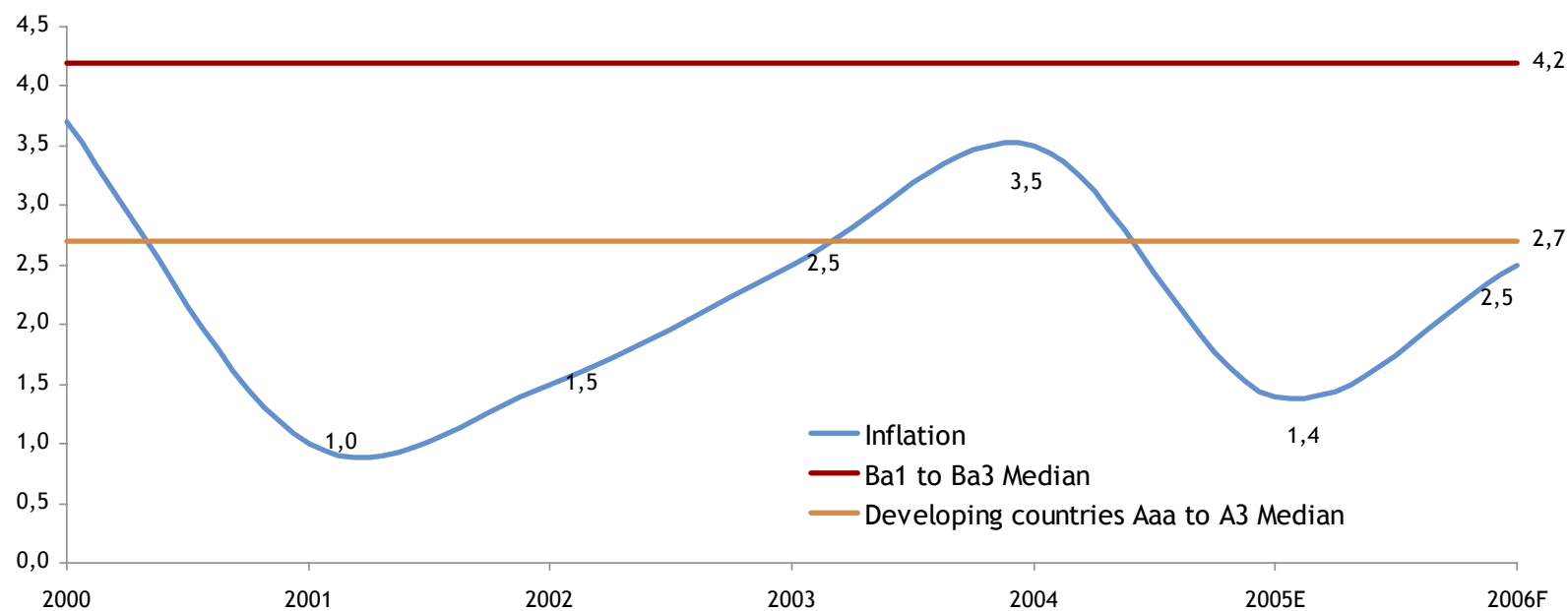


Source: SUNAT



Prudent monetary policy resulted in price stability

CPI % Change (Dec/Dec)



Source: Moody's Statistical Handbook. Country Credit,

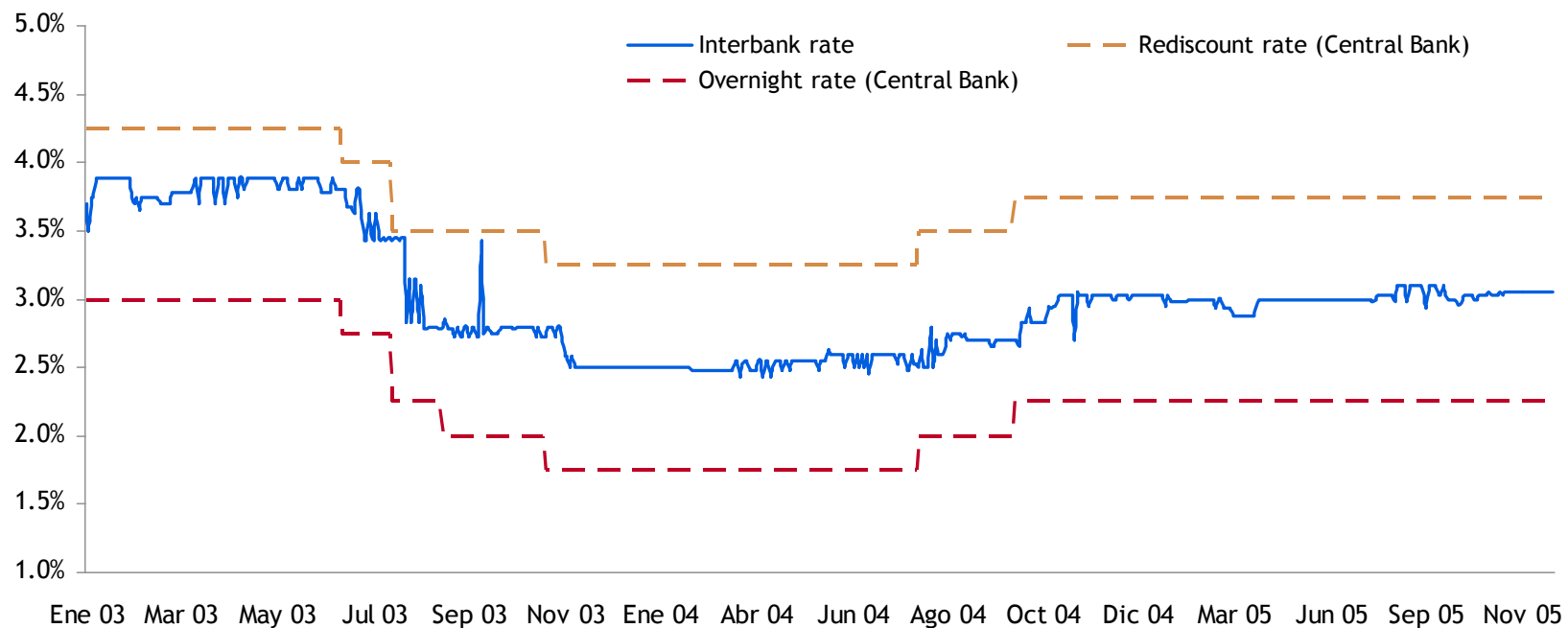
Note: Ba1 to Ba3 median and Aaa to A3 (developing countries) median were calculated for 2000-2006

- Peru has an excellent record of monetary stability even when compared to many investment-grade countries
- Stabilized inflationary expectations are instrumental for growth sustainability



Interest rates on downward trend

Interbank and Central Bank referential Interest rates (nuevos soles)

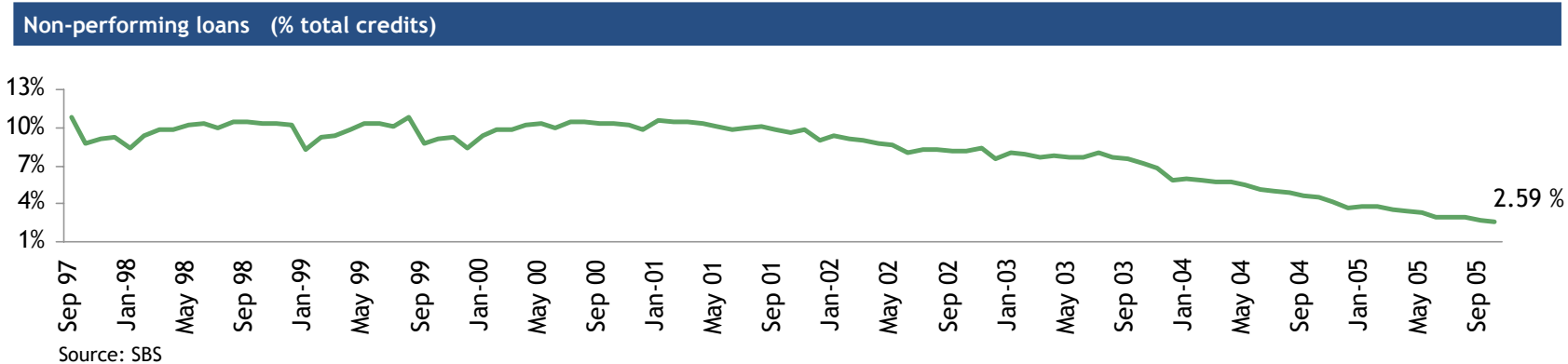


Source: Central Bank

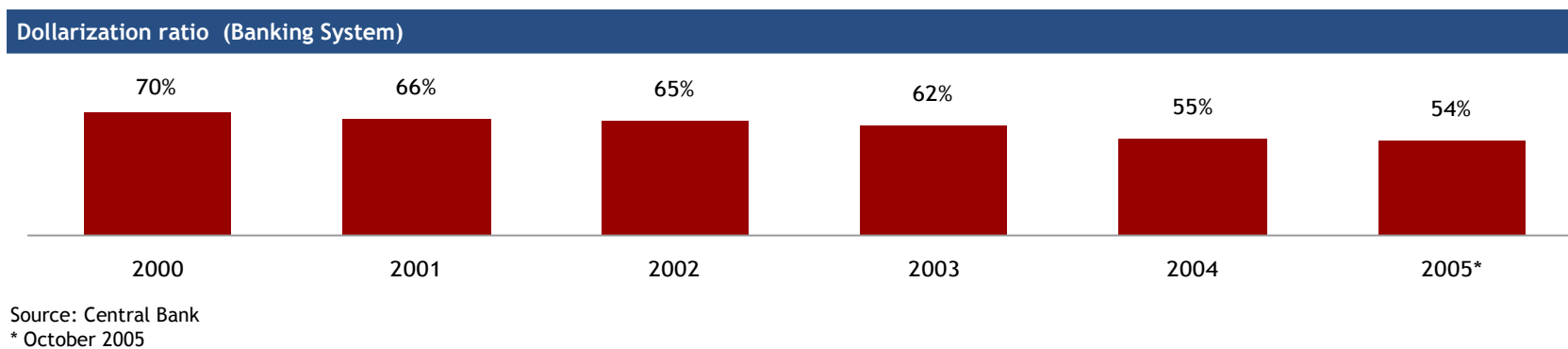


Healthy financial system and monetary stability underpin growing financial intermediation and declining dollarization

- Growth combined with a conservative monetary policy have contributed to strengthen the domestic financial system
- Non-performing loans have declined sharply

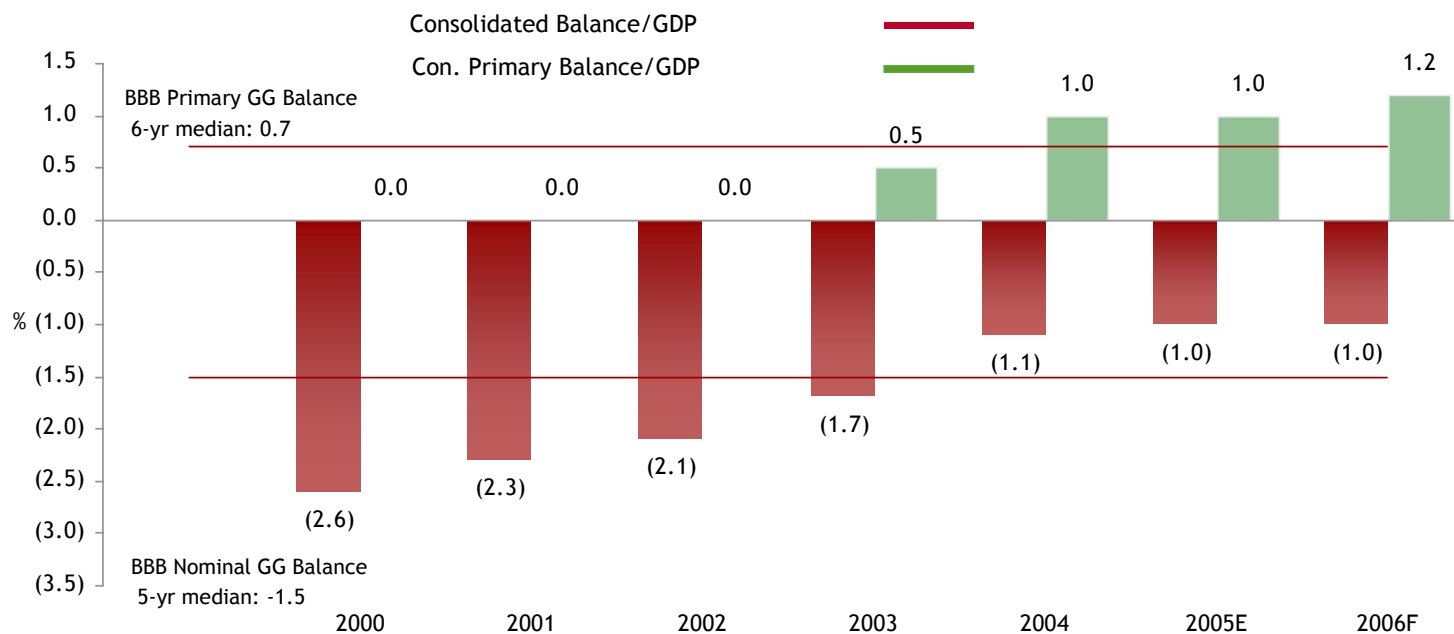


- Dollarization has declined, reflecting greater confidence in monetary policy and economic stability



Fiscal consolidation underway

Consolidated Total and Primary Balances as a % of GDP



Source: MEF & Central Bank

- Strong track-record of prudent fiscal management and growing primary surpluses underpin significantly greater fiscal flexibility
- Fiscal performance comparable to investment grade countries



Fiscal consolidation underway

Non financial Public Sector (% of GDP)

	2001	2002	2003	2004	2005E	2006F	2007F
Central Government	-0,6	-0,2	0,2	0,6	0,6	0,8	1,0
Current Income	14,4	14,4	14,9	15,1	15,7	15,6	15,4
Tax	12,5	12,1	13,0	13,3	13,7	13,6	13,4
Non-tax	1,9	2,3	2,0	1,8	2,0	2,0	2,0
Capital Income	0,2	0,2	0,2	0,1	0,1	0,1	0,1
Non-financial Expenditures	15,2	14,7	14,9	14,6	15,2	14,9	14,5
Primary Balance of Other Entities	0,4	0,0	0,2	0,4	0,4	0,3	0,3
Primary balance	-0,2	-0,1	0,4	1,0	1,0	1,2	1,3
Interest	2,2	2,0	2,2	2,1	2,0	2,2	2,1
Overall Balance	-2,5	-2,3	-1,7	-1,1	-1,0	-1,0	-0,8

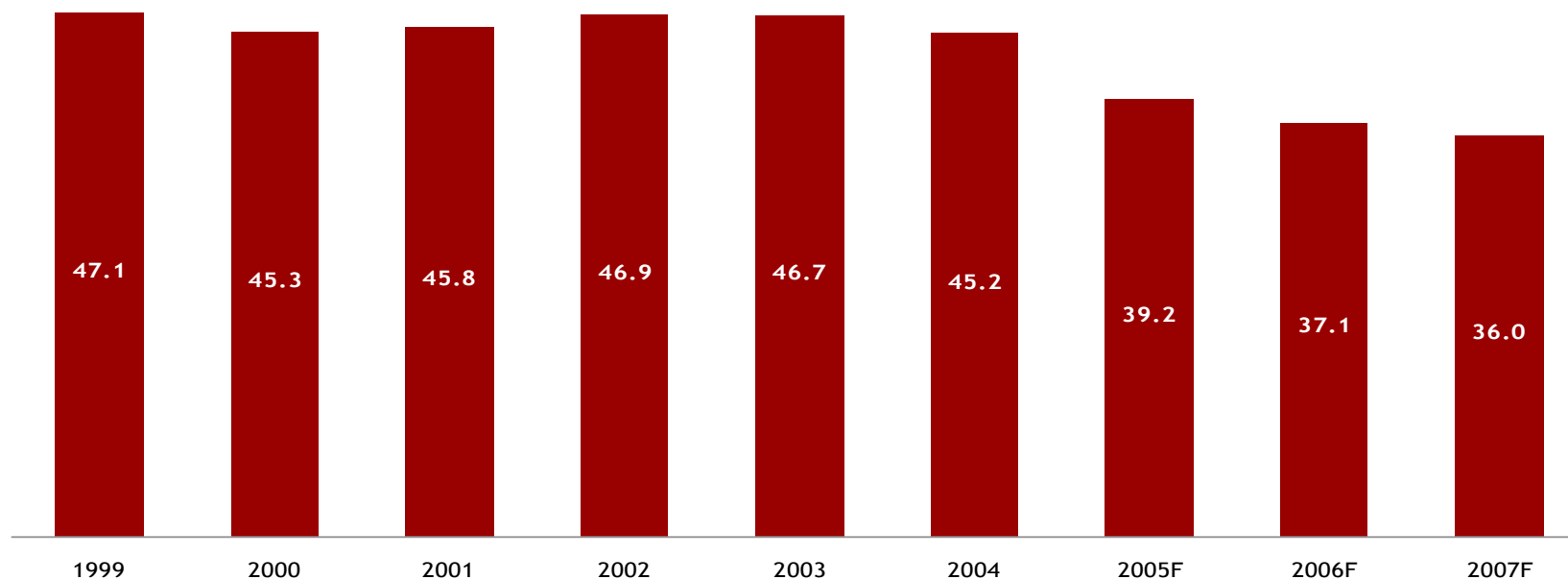
Source: MEF & Central Bank

- Further consolidation of public accounts is expected in 2005 and 2006
- Increasing revenues as % of GDP through 2005 and 2006



Positive public debt dynamics

Public debt % of GDP



Source: MEF & Central Bank

- Due to euro and yen appreciation, the Debt to GDP ratio increased 1.6%, 1.8% and 0.7% in 2002, 2003 and 2004, respectively
- 2005 pre-financing (€ 650 MM) represented a 1.2% increase in 2004 Debt to GDP ratio



Agenda

Robust economic performance

✓ **Public debt reprofiling**

Structural underpinnings for continued growth



Public debt reprofiling

The main objective of reprofiling is to support fiscal policy sustainability, reducing the different risks faced by the public debt.

- Reducing refinancing risk through market based operations that allow us to increase the average life and duration of the debt portfolio.
- Reducing the debt exposure to market risks.
- Reducing, if possible, the present value and/or the nominal value of the public debt.

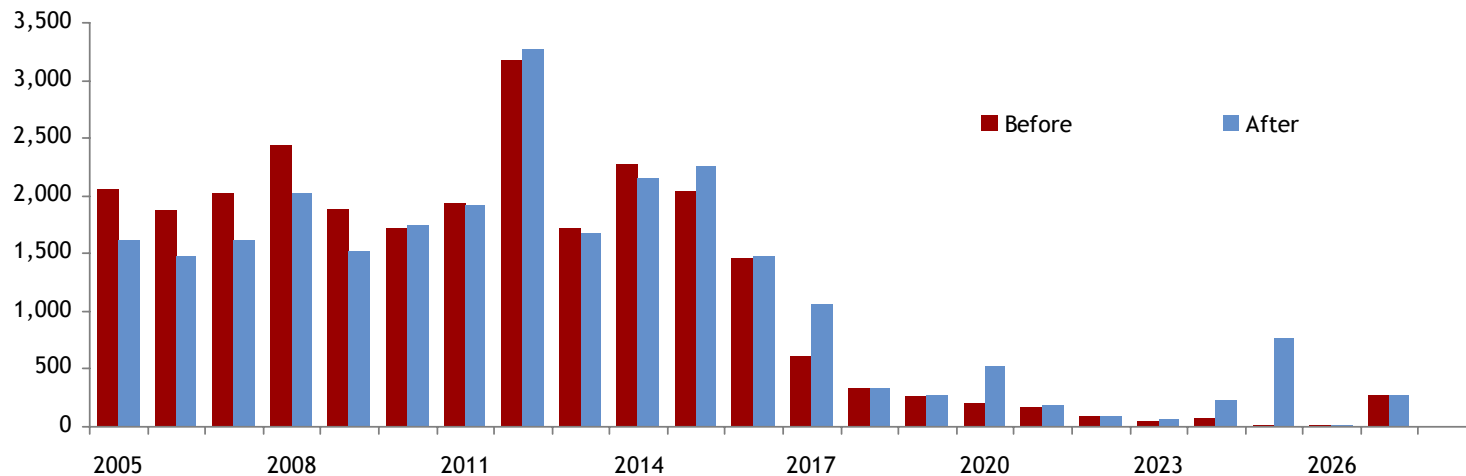
Reprofiling is implemented through:

- Bonds Exchange (external and domestic)
- Swaps Operations (interest rates and currency)
- Prepayments



Effect of reprofiling transactions...

Amortization payments (US\$ MM)
Before and after Paris Club prepayment and local exchanges*



Source: MEF
* Preliminary

- Through proactive, market-based, debt management strategies, we have reprofiled amortization payments due in the coming years.
- US\$ 1.55 billion Paris Club prepayment was financed with 20-year dollar global bonds (US\$ 750 million) as well as 11-, 12- and 15-year fixed-rate sol-denominated bonds (US\$ 800 million).
- Local dollar-denominated bonds for US\$ 381 million maturing by year-end were exchanged for 2010 and 2015 fixed-rate sol-denominated bonds and 2024 inflation-linked sol-denominated bonds.



Effect of reprofiling transactions... Amortization payments relief

Amortization payments relief 2005 - 2009 (US\$ million)

Transactions / Year	2005	2006	2007	2008	2009
Bonds exchange January 2005	136	-	-	-	-
Bonds exchange D.U. 108-2000 (1st tranche)	262	-	-	-	-
Paris Club prepayment	106	345	359	367	378
Bonds exchange D.U. 108-2000 (2nd tranche)	119	-	-	-	-
Total relief	623	345	359	367	378

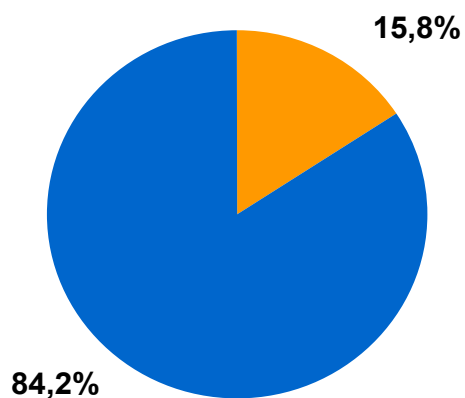
Source: MEF



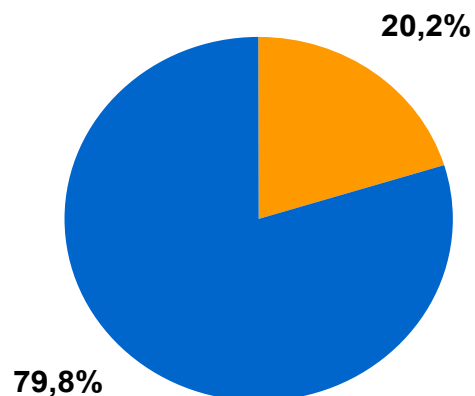
Expected changes in the public debt structure (I)

Public debt stock

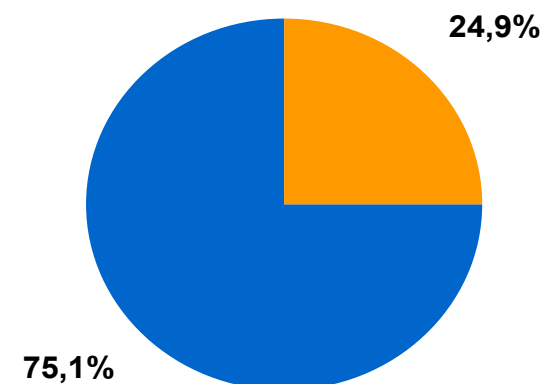
As of December 2004



As of September 2005



As of December 2008*



■ Domestic ■ External

Source: DNEP-MEF

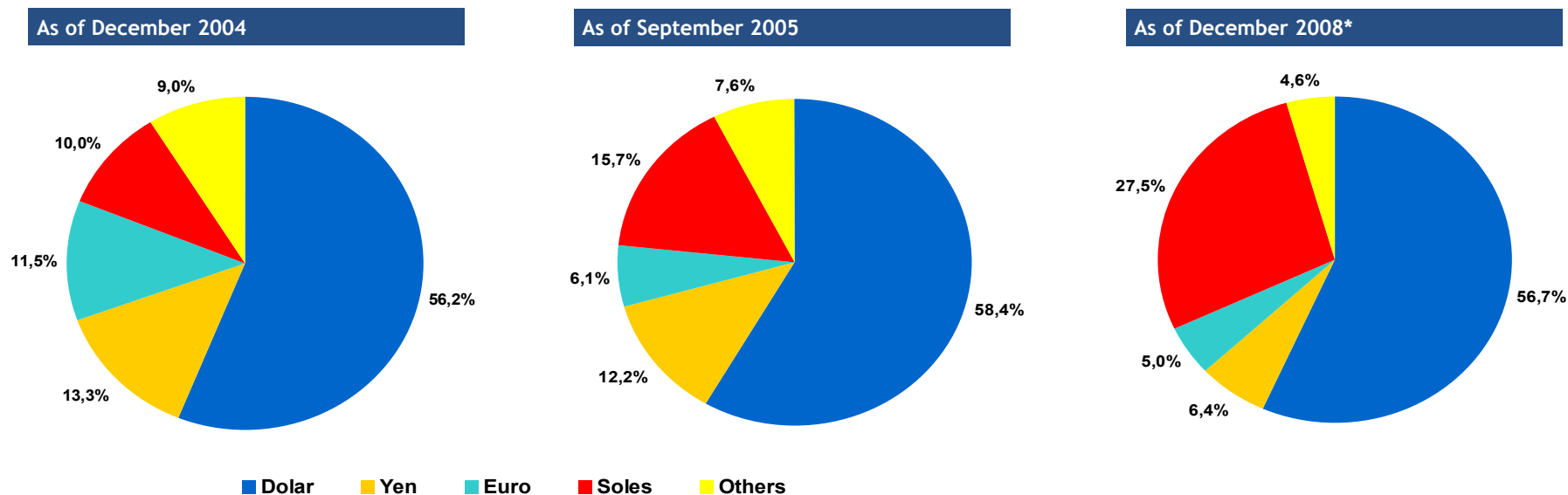
*Forecast. Previsional debt is not included

- Public debt structure has changed as a result of reprofiling transactions
- Domestic debt increased significantly its participation in the total public debt stock, from 15.8% to 20.2%
- Foreign currency denominated debt will continue to decrease significantly as a percentage of total public debt



Expected changes in the public debt structure (II)

Currency mix



Source: DNEP-MEF

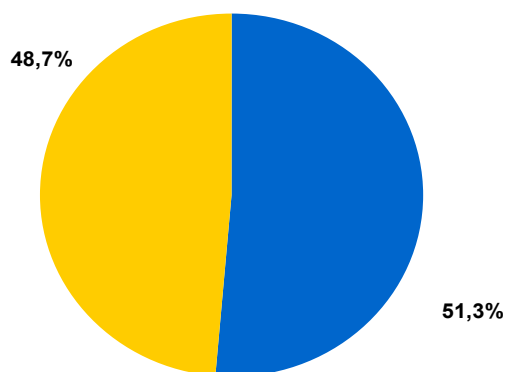
*Forecast. Previsional debt is not included

- Public debt denominated in euro and yen decreased its share in the public debt portfolio
- Nuevos soles increased its share in the public debt portfolio, from 10.0% to 15.7%
- Euro and yen denominated debt will continue to decrease its share in the public debt portfolio as the percentage of nuevos soles denominated debt increases



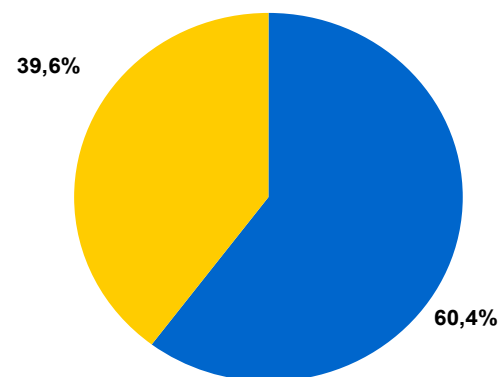
Expected changes in the public debt structure (III) Fixed vs. floating

As of December 2004



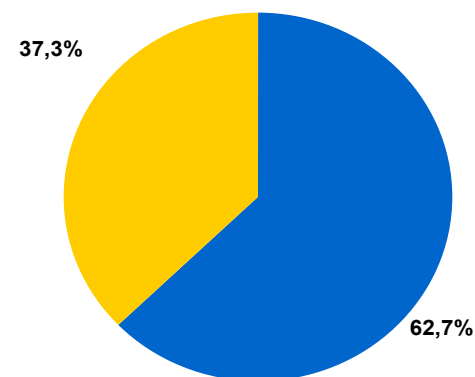
■ Fixed

As of September 2005



■ Floating

As of December 2008*



Source: DNEP-MEF

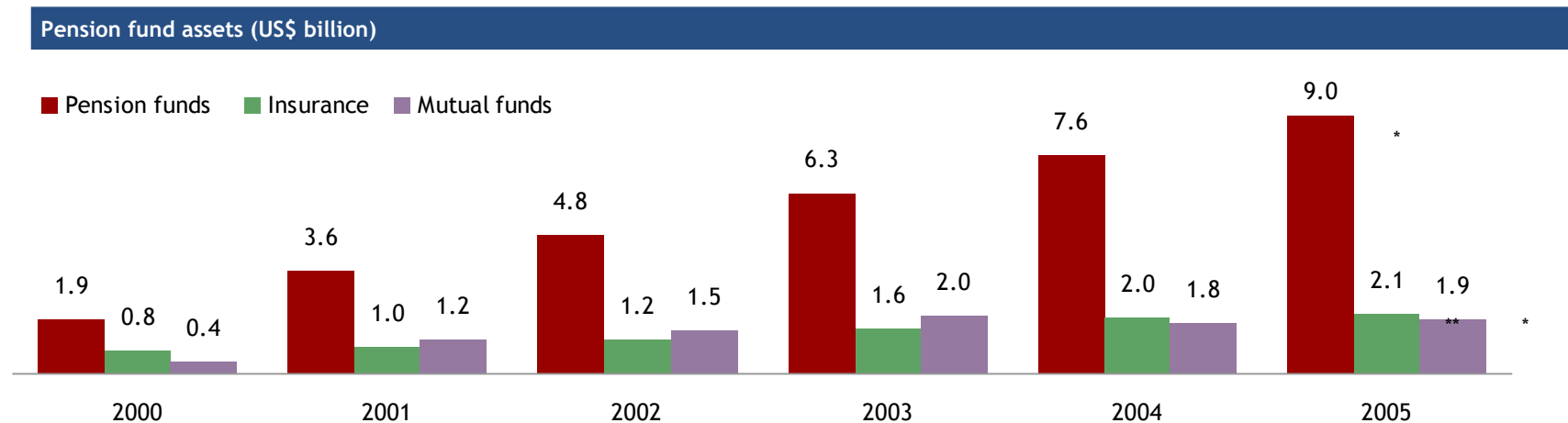
*Forecast. Previsional debt is not included

- Fixed rate debt grew from 51.3% to 60.4, helping to reduce market risks of our debt portfolio
- Fixed rate debt participation will continue to grow
- We continue to evaluate the execution of new interest swap operations



Structural increase in domestic demand for public and corporate debt

- Private pension funds, mutual funds and insurance assets have risen



Source: SBS

* August 2005

** June 2005



Financing plan

US\$ million				
	2005E	2006F	2007F	2008F
Uses	4 448	2 437	2 367	2 482
External amortization	2 908	1 171	1 252	1 750
Internal amortization	766	403	445	380
Fiscal deficit	774	863	670	352
General purpose loans	4 448	2 437	2 367	2 482
External	1 149	1 027	983	993
Policy based loans	546	499	483	493
Investment projects	500	500	500	500
Other	103	28	0	0
Internal	320	760	- 16	90
Bonds	2 979	650	1 400	1 400

Source: MEF

- Peru's international capital markets funding was completed with the US\$ 400 million reopening of the Peru 2033 bonds in January
- Peru's 2006 financing plan does not require that the Government tap international bond markets

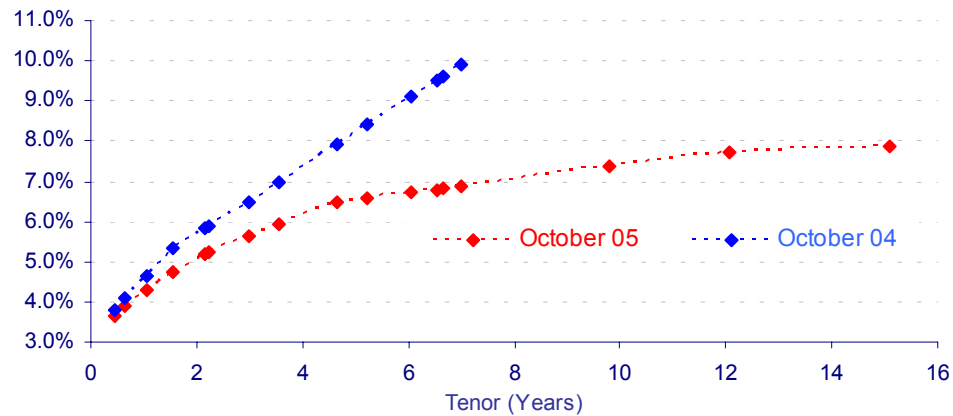


Domestic public debt market development (I)

- Fixed rate nuevo sol bonds tenure doubled in 2005.
- From October 2004 to October 2005 a 7-year bond yield decreased in 302 bps.

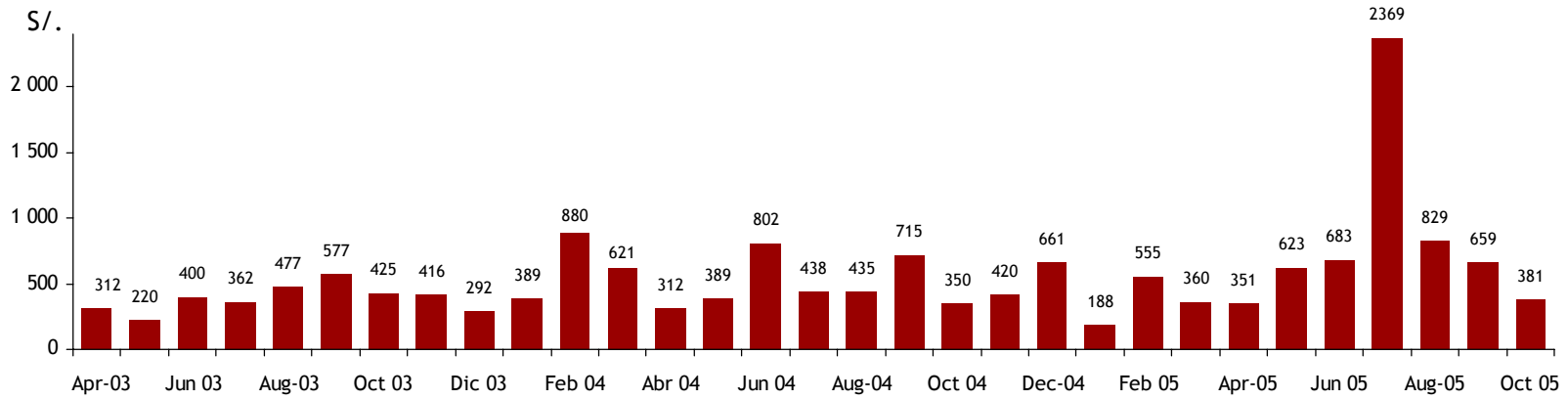
Concept	October-04	October-05	
Maximum tenor of fixed rate nuevo sol bonds	7 years	7 years	15 years
Yield	9.93%	6.91%	7.86%
Duration (Years)	2.14	5.47	

Fixed rate yield curve

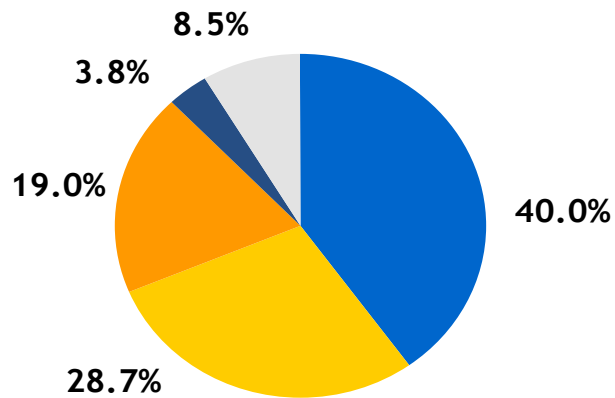


Domestic public debt market development (II)

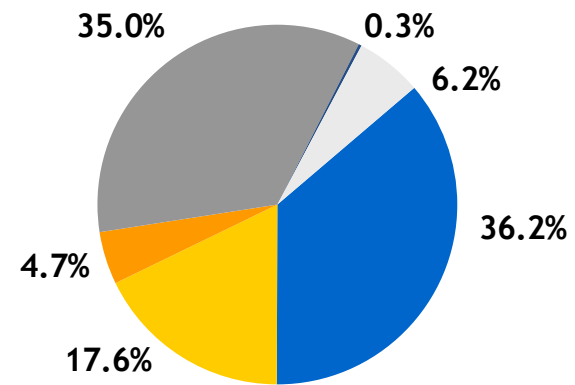
Fixed rate bonds trading (S/. Millions)



Fixed rate bondholders (2003)



Fixed rate bondholders (2005)



■ Pension funds ■ Banks ■ Private funds ■ Non residents ■ Insurance ■ Others

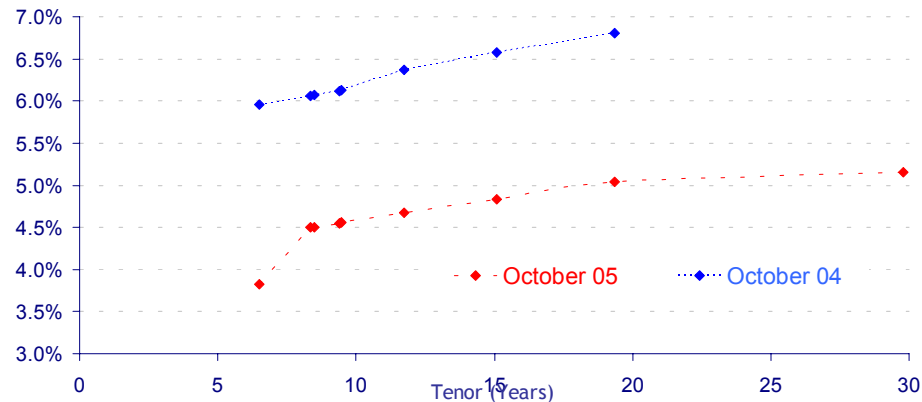


Domestic public debt market development (III)

- Inflation linked nuevo sol bonds tenure doubled in 2005.
- From October 2004 to October 2005 a 15-year bond yield decreased in 174 bps.

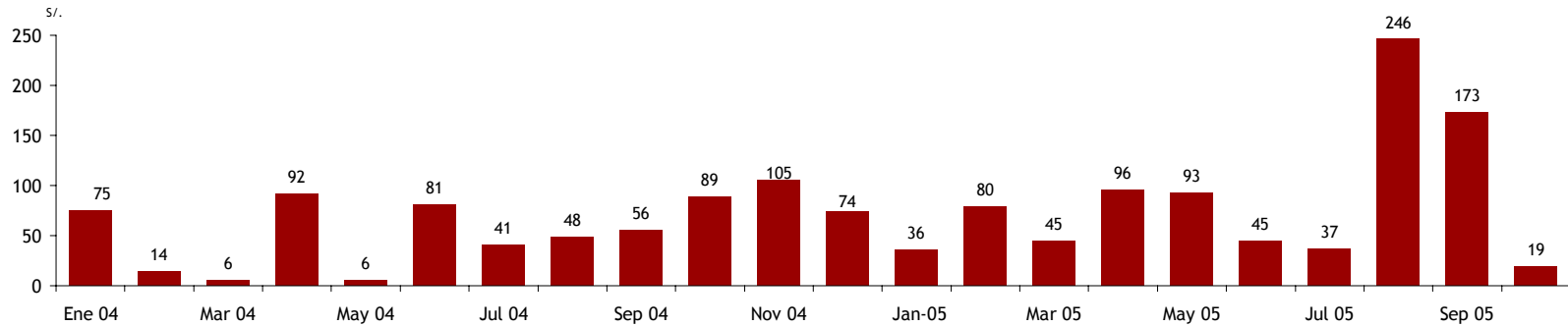
Concept	October-04	October-05	
Maximum tenor of inflation-linked nuevo sol bonds	15 years	15 years	30 years
Yield	6.57%	4.83%	5.15%
Duration (Years)	4.22	8.07	

Inflation-linked rate yield curve

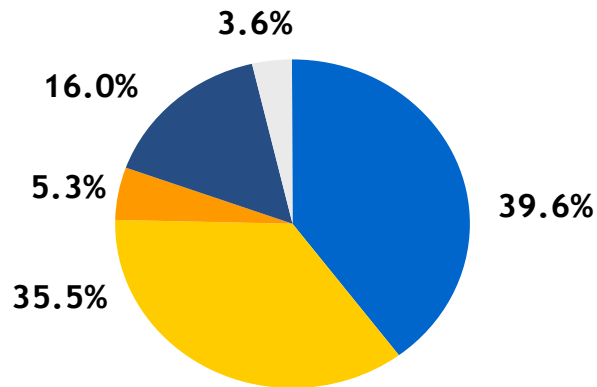


Domestic public debt market development (IV)

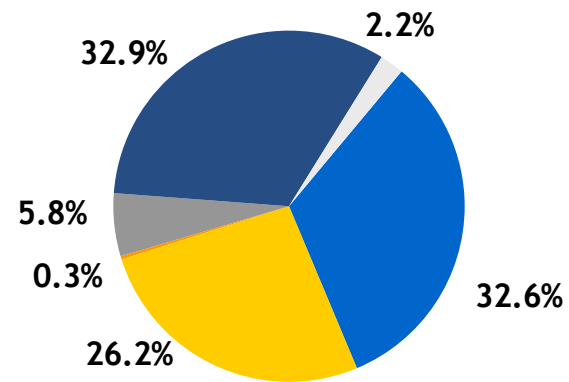
Trading of inflation-linked bonds (S/. Millions)



Inflation-linked rate bondholders (2003)



Inflation-linked rate bondholders (2005)



■ Pension funds
 ■ Banks
 ■ Private funds
 ■ Non residents
 ■ Insurance
 ■ Others



Agenda

Robust economic performance

Public debt reprofiling

✓ **Structural underpinnings for continued growth**



Institutional safeguards

- The Constitution does not discriminate between local and foreign investors
- Structural reforms to foster private investment:
 - Privatization of major public enterprises
 - Enhance the framework for private-public partnerships in infrastructure, in particular, for roads and sanitation in Peru's regions
 - Revive privatizations and concessions (ports, roads, airports)
- Pension Reforms:
 - Creation of Private Pension Funds in 1993
 - Reduction of pension costs approved by the Congress (Law 20530 was repealed)
- Sign FTA with the U.S. and start negotiations with EU and others
- The Transparency Law assures fiscal discipline
- Autonomy of Central Bank, who manages monetary policy with specific inflation target rules



Decentralization is accompanied by strong safeguards for fiscal responsibility

- Regions cannot borrow without the explicit guarantee of the central government.
- Transfer of functions (public health, education) being carried out according to pre-set conservative timetable, equivalent resources being deducted from central government budget.
- Ongoing discussions with various regions in order to substantially reduce tax exemptions and re-invest the proceeds in local roads and sanitation works.



Major projects to be carried out

	<u>Amount (US\$ Millions)</u>
■ <u>Gas export project</u> (Mexico, US, Chile) scheduled for 2008	2 700
■ <u>Alto Chicama</u> gold mine under construction	450
■ New <u>Southern Peru Copper</u> refinery due to begin construction this year	300
■ <u>Cerro Verde</u> copper mine expansion in 2005-2006	850
■ <u>Interoceanic road</u> Peru - Brazil	892
■ <u>IIRSA</u> North	219
■ Olmos project	112
■ New <u>terminal ports</u>	274
■ Regional airports	148
■ Road network 1 (Tumbes, Piura)	104
■ Road network 4 (Lima, Ancash, La Libertad)	100
■ Road network 6 (Lima, Ica)	191
■ <u>Costa Sierra</u> road	292
■ <u>Road network 6</u> . Pucusana bridge-Cerro Azul-Ica	191
■ Bidding La Granja	300
■ Bidding Michiquillay	300
■ Bayovar	<u>300</u>
	7 723



Risks

- Elections in April 2006 are prompting some leading politicians to make populist promises.
- Pent-up social demands need to be addressed in the short and medium-term. Despite four years of continued economic growth, about 50% of population continues to live in poverty.
- High international oil prices can affect global growth and therefore domestic growth.



In sum

- Medium term growth prospects are good:
 - Growing exports
 - Favorable international environment
 - Major new investment projects
 - FTA negotiations with U.S.
- Commitment to maintaining macro stability remains solid.
- Fiscal accounts are expected to continue strengthening despite political pressures.
- Decentralization is being carried out responsibly.
- Sound fiscal policies result in declining public debt as a share of GDP and in a manageable, flexible financing plan.



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