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May 25, 2021

**Statement by Ms. Senich and Mr. Westphal on Peru  
(Preliminary)  
Executive Board Meeting  
May 27, 2021**

**Peru's economic fundamentals and policy framework remain strong, and we agree that Peru continues to meet the FCL criteria.** The pandemic tested the authorities with the biggest economic contraction in 30 years, and the authorities responded with appropriate fiscal, monetary, and regulatory support. Against this backdrop, we continue to support the FCL as an appropriate precautionary tool for Peru. The authorities also face a difficult environment going forward, including elevated levels of unemployment, poverty, and financial market volatility ahead of the June 2021 election.

**The authorities' fiscal position has remained strong.** We agree that the authorities should increase domestic revenue mobilization in the medium term, particularly given Peru's low level of tax revenues relative to peers, but we caution against any increase in taxes that may dampen the pandemic recovery or impact vulnerable households in the near term. We are also concerned that given the authorities' recent approval of another round of early pension withdrawals from the private pension system, additional state support may be necessary to preserve its long-term viability. We would encourage the authorities to prioritize policy steps that could reduce the likelihood of the private pension system becoming a fiscal liability.

**Monetary policy remains appropriately expansionary given the large negative output gap and anchored inflation expectations.** As we noted in the Article IV discussion in March, the authorities should allow for greater exchange rate flexibility and decrease their interventions to smooth volatility, which should help the central bank to focus on its inflation targeting framework. The authorities should take advantage of the pandemic-induced reduction in dollarization to continue making progress in this area as it will enhance monetary policy transmission. We concur with staff that implementing Basel III risk weights to FX loans will also help with this goal. While we agree that the authorities should generally make progress on implementing Basel III and strengthening their supervisory and regulatory

framework, we caution against unwinding relief measures prematurely, including those that extended grace periods or allowed for lower capital buffers. Peru should only remove these measures after the recovery is on stronger footing.

**We consider staff's coverage of political risks surrounding the June 2021 presidential election to be cursory.** Staff suggest that both remaining candidates have expressed "broad commitment to maintaining very strong policies and institutional frameworks." One candidate, however, has expressed support for significant institutional changes, including restricting foreign investment, nationalizing key industries, and redrafting portions of the constitution, while the other was imprisoned as recently as 2020 on allegations of money laundering. *Could staff provide further information on the candidates' expected economic priorities?*