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CONSOLIDATION OF TRADE LIBERALIZATION AND OTHER REFORMS UNDERPINNED ECONOMIC GROWTH AND WELFARE IMPROVEMENTS IN PERU

The consolidation since 1994 of earlier economic reforms has paid off in the form of significant growth in GDP, employment, trade, and foreign investment, as well as of improved social welfare indicators, says a new WTO report on the trade policies of Peru. However, the report highlights the need for Peru to achieve higher rates of growth to increase a still relatively modest GDP per capita (some US\$2,500 per person). In this regard, eliminating remaining impediments to greater economic efficiency would be of crucial importance both by enhancing the international competitiveness of Peruvian producers and exporters, and by making Peru more attractive as an investment destination.

The new WTO Secretariat report, along with a policy statement from the Peruvian Government, will serve as a basis for the second trade policy review of Peru which will take place in the Trade Policy Review Body of the WTO on 30 and 31 May 2000.

The report notes that Peru carried out major reforms in the 1990s, including the privatization of most state-owned enterprises, the establishment of a sound regulatory framework and the strengthening of the financial system. Reflecting Peru's generally open trade regime, total recorded merchandise trade grew at an average annual rate of 8.5% between 1994 and 1998, the report says. Trade in services also grew significantly driven by the economic liberalization process. The report also notes that the stock of foreign direct investment increased five-fold since 1993 thanks to the stabilization process and the establishment of a legal framework for the promotion and the protection of investment.

The report states that the United States remains Peru's principal trade partner both as an export destination and import source, followed by countries from the Latin American Integration Association, the European Union and Japan. Peru exports consist mostly of primary and semi-processed products, with fishing and mineral products together accounting for some 60% of total merchandise exports. As a consequence, Peruvian exports are exposed to important variability both in terms of volume and earnings.

The report says that there have been no significant changes to the general structure of Peru's trade policy since its last review in 1994. Peru still uses tariffs as its main instrument of border protection. The average applied MFN rate was 13.6% in 1999, down from some 16% in 1993. Some 330 agricultural items receive protection through a 5% or 10% tariff surcharge; of these, 23 are also subject to variable specific duties providing open-ended ad valorem protection. The report points out that the entire tariff is bound but that the wide margin between applied and bound rates (generally 30%) may undermine the predictability of the tariff regime.

The report indicates that non-tariff barriers to trade appear generally low. Anti-dumping has been used sparingly, and no countervailing or safeguard measures are in force. However, Peru still maintains certain local-content requirements and trade-related investment measures, while government procurement may favour domestic suppliers. The report notes that the scope and complexity of fiscal incentives raise concerns, with one scheme conditional on export performance. Refunds under Peru's drawback regime are not limited to the actual amount of import duties paid. A small number of Peruvian exports are subject to export restrictions, while others appear to face significant non-tariff barrier in foreign markets.

The report notes that agriculture is an important sector in the Peruvian economy, both in terms of output and employment. Difficult adjustments in this sector have resulted from the liberalization and reductions in state assistance initiated in the early 1990s which, nevertheless, have underpinned strong output expansion directed at both domestic and foreign markets. However, the concentration of various border and internal support measures in a limited range of favoured products (certain crops and dairy products) may well hinder further gains by misallocating labour, land, and capital resources at the expense of other activities. The report also notes that driven by international demand, production of coca leaf and derived products still appears sizeable albeit declining.

Peru's strategy to attract foreign private investment has been particularly successful in the mining industry, which has regained its leading role in the economy. The mining and energy sectors together attracted just over one third of total direct foreign investment during 1992-99, says the report. Peru also has a large fishing industry, which is, however, highly cyclical and suffers from apparently policy induced over-investment and over-fishing.

The report indicates that besides the processing of mineral, agricultural and fisheries products, manufacturing activities make only a small contribution to Peru's economy, having experienced extensive restructuring from increased import competition.

Concerning the services sector, the report mentions that the Peruvian State used to be a major supplier of services, including in financial, transport and telecommunications activities, but that such involvement has decreased dramatically since the mid 1990s. The report notes that, in parallel, foreign access to Peru's services market has improved markedly. Under the WTO's General Agreement on Trade in Services (GATS), Peru undertook horizontal commitments with respect to movement of natural persons and treatment of foreign investment. Peru's commitments in telecommunication services are particularly comprehensive.

The report states that Peru takes part in regional integration schemes within the Andean Community and the Latin American Integration Association, as well as in the Asia-Pacific Economic

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Cooperation forum and the negotiating groups of the Free-trade area of the Americas. The report notes, however, that despite Peru's long-standing participation in the regional integration processes within Latin America, the share of reciprocal preferential trade in total trade remains relatively modest.

In addition to the negotiated schemes, Peru benefits from increased market access to several countries under Generalized System of Preferences schemes, particularly under the special regimes granted by the European Union and the United States to promote alternatives to coca cultivation and production.

Notes to Editors

Trade Policy Reviews are an exercise, mandated in the WTO agreements, in which member countries' trade and related policies are examined and evaluated at regular intervals. Significant developments which may have an impact on the global trading system are also monitored. For each review, two documents are prepared: a policy statement by the government of the member under review, and a detailed report written independently by the WTO Secretariat. These two documents are then discussed by the WTO's full membership in the Trade Policy Review Body (TPRB). These documents and the proceedings of the TPRB's meetings are published shortly afterwards. Since 1995, when the WTO came into force, services and trade-related aspects of intellectual property rights have also been covered.

For this review, the WTO's Secretariat report, together with the policy statement prepared by Peru, will be discussed by the Trade Policy Review Body on 29 and 31 May 2000. The Secretariat report covers the development of all aspects of Peru's trade policies, including domestic laws and regulations, the institutional framework, trade policies by measure and by sector.

Attached to this press release is a summary of the observations in the Secretariat report and parts of the government's policy statement. The Secretariat report and the government's policy statement are available for the press in the newsroom of the WTO internet site (www.wto.org). These two documents and the minutes of the TPRB's discussion and the Chairman's summing up, will be published in hardback in due course and will be available from the Secretariat, Centre William Rappard, 154 rue de Lausanne, 1211 Geneva 21.

Since December 1989, the following reports have been completed: Argentina (1992 and 1999), Australia (1989, 1994 and 1998), Austria (1992), Bangladesh (1992 and 2000), Benin (1997), Bolivia (1993 and 1999), Botswana (1998), Brazil (1992 and 1996), Burkina Faso (1998), Cameroon (1995), Canada (1990, 1992, 1994, 1996 and 1998), Chile (1991 and 1997), Colombia (1990 and 1996), Costa Rica (1995), Côte d'Ivoire (1995), Cyprus (1997), the Czech Republic (1996), the Dominican Republic (1996), Egypt (1992 and 1999), El Salvador (1996), the European Communities (1991, 1993, 1995 and 1997), Fiji (1997), Finland (1992), Ghana (1992), Guinea (1999), Hong Kong (1990, 1994 and 1998), Hungary (1991 and 1998), Iceland (1994 and 2000), India (1993 and 1998), Indonesia (1991, 1994 and 1998), Israel (1994 and 1999), Jamaica (1998), Japan (1990, 1992, 1995 and 1998), Kenya (1993 and 2000), Korea, Rep. of (1992 and 1996), Lesotho (1998), Macau (1994), Malaysia (1993 and 1997), Mali (1998), Mauritius (1995), Mexico (1993 and 1997), Morocco (1989 and 1996), New Zealand (1990 and 1996), Namibia (1998), Nicaragua (1999), Nigeria (1991 and 1998), Norway (1991 and 1996), Pakistan (1995), Papua New Guinea (1999), Paraguay (1997), Peru (1994), the Philippines (1993), Poland (1993), Romania (1992 and 1999), Senegal (1994), Singapore (1992, 1996 and 2000), Slovak Republic (1995), the Solomon Islands (1998), South Africa (1993 and 1998), Sri Lanka (1995), Swaziland (1998), Sweden (1990 and 1994), Switzerland (1991 and 1996), Tanzania (2000), Thailand (1991, 1995 and 1999), Togo (1999), Trinidad and Tobago (1998), Tunisia (1994), Turkey (1994 and 1998), the United States (1989, 1992, 1994, 1996 and 1999), Uganda (1995), Uruguay (1992 and 1998), Venezuela (1996), Zambia (1996) and Zimbabwe (1994).

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TRADE POLICY REVIEW BODY

PERU

Report by the Secretariat - Summary Observations

Introduction

Peru's generally open trade and investment regimes have remained relatively stable since its previous Trade Policy Review in 1994. The continued consolidation of earlier, far-reaching reforms has paid off during the last six years in the form of significant growth in GDP, employment, trade, and foreign investment, as well as in improved social welfare indicators. In the context of the Uruguay Round, Peru consolidated within the WTO many of its unilateral liberalization and economic reforms, and has subsequently enacted or amended domestic regulations to ensure implantation of its multilateral obligations. Peru's trading partners have thus benefited from growing market access for their merchandise exports and services suppliers.

A still relatively modest GDP per capita (some US\$2,500 per person), which in real terms is no higher than in the mid 1960s, highlights the need for Peru to achieve higher rates of growth. Eliminating remaining impediments to greater economic efficiency would be of crucial importance in this regard both by enhancing the international competitiveness of Peruvian producers and exporters, and by making Peru more attractive as an investment destination. A fresh round of reforms might include further customs simplification, more even and predictable tariff protection, the elimination of minor remaining local-content or export performance requirements, and greater transparency in support programmes. Current support for certain agricultural activities is out of line with the principle of sectoral neutrality. Pressing forward the privatization and concession programmes would create new opportunities for private investments and inject greater competition in the domestic market.

Economic and Institutional Environment

GDP grew at an average annual rate of 5.6% during 1993-99. Growth, however, has tended to oscillate, with 1998 in particular registering an important slowdown, due mainly to a series of exogenous shocks. Inflation has been brought down, and stronger external balances have allowed international reserves to rise to comfortable levels. Regaining investor confidence, through the normalization of relations with external creditors and debt restructuring, has also been an important ingredient of Peru's economic recovery.

In the wake of the economic reforms of the early 1990s, trade and investment flows have increased substantially. Between 1994 and 1998, total recorded merchandise trade grew at an average annual rate of 8.5%. Peru's export supply is concentrated in primary and semi-processed products, mainly from mining and fishing activities, and is exposed to sharp fluctuations both in terms of volume (output variations) and earnings (price variations). Trade in non-factor services has also grown substantially since Peru's previous Review, driven by the economic liberalization process and in parallel with rising merchandise trade. The stabilization process and the establishment of a legal framework for the promotion and the protection of investment has seen the stock of foreign direct investment increase five-fold since 1993.

There have been no significant changes to the general structure of trade policy formulation or implementation since Peru's last Review. The sectoral regulatory framework has also remained relatively stable, after earlier, wide-ranging reforms led to the comprehensive liberalization of sectoral investment rules and an ambitious privatization programme that saw the State withdraw from many production activities particularly during 1994-96. Investors are offered additional incentives through "law stability agreements", conditional on meeting minimum investment, job creation or export performance criteria.

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The competition policy framework continues to be developed with a view to ensuring that consumers benefit from the liberalization process. Aware of the interlinkages and the need for consistency between competition policy and protection of intellectual property rights and the use of contingency measures, responsibility for all three areas has been given to a single agency, INDECOPI.

Trade Policy Developments

The aim of Peru's trade policy is to liberalize the trade regime so as to provide non-distorting incentives that allow an efficient allocation of resources and foster the development of economic activities according to market signals. Consistent with this aim, Peru uses tariffs as its main instrument of border protection. The average applied MFN rate was 13.6% in 1999, down from some 16% in 1993. The tariff is based on a two-level ad valorem structure applied on the c.i.f. value of imports. In 1997, the two main rates were reduced to 12% and 20% (from 15% and 25%); simultaneously, tariffs on some 300 agricultural products were increased from 15% to 20%. Some 84% of all tariff lines are subject to the 12% duty rate. The entire tariff is bound but the wide margin between applied and bound rates (generally 30%) may undermine the predictability of the tariff regime.

Some 330 tariff items involving agricultural products receive additional protection through a 5% or 10% tariff surcharge. Of these, 23 items are also subject to variable specific duties intended as a price stabilization and protection mechanism. In early 2000, these duties affected five product groups: milk, maize, sorghum, rice, and sugar (also wheat products until 1998). As, in effect, variable specific duties provide open-ended ad valorem protection, concerns arise about their use undermining predictability, distorting production and possibly leading to the breach of tariff bindings.

Peru's basic import formalities have remained essentially unchanged since its previous Review and in the main appear to be straightforward. Preshipment inspection, introduced in 1992 to prevent under-valuation, is still in use although the range of goods covered has been reduced. Peru receives technical assistance to implement the WTO Agreement on Customs Valuation, and was granted a waiver to delay full implementation until April 2000. Both preferential and non-preferential rules of origin are applied, the latter in relation to contingency measures.

Non-tariff barriers to trade appear generally low. Anti-dumping measures have been used sparingly, with only nine measures in force in early 2000, the majority affecting non-WTO exporters; there are no countervailing or safeguard measures in force. Peru maintains local-content requirements in relation to various government nutrition programmes, as well as a trade-related investment measure in dairy. A number of provisions favour domestic suppliers in government procurement, which is governed by a more transparent regulatory framework introduced in 1997. Peru is not a member of the WTO plurilateral Agreement on Government Procurement.

Regional, sectoral, and social policies make use of fiscal incentives whose scope and complexity raise some concern, although amounts involved are relatively small. Free zones and other special fiscal zones are largely used for regional development objectives but seem to have fallen short of their goals; fiscal exemptions provided under the CETICOS scheme established in late 1996 are conditional on export performance. Preferential credit to selected sectors is available from the national development bank, COFIDE.

Peruvian exports appear to receive limited direct government support. Peru's drawback regime refunds 5% of the f.o.b. value of the good exported regardless of the actual amount of duties paid on imported inputs. Export restrictions apply on guano, rough wood and certain animals. Visas are required for textile exports to the United States, with export restraints on cotton towels. Under the WTO Agreement on Textiles and Clothing, the European Union applies quotas to Peruvian exports of

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cotton yarns and fabrics. A number of non-tariff measures implemented in foreign markets (e.g. sanitary and phytosanitary measures) may also hinder certain other Peruvian exports.

Sectoral Policy Developments

Since its last Review, Peru has continued to pursue a sectoral policy approach that emphasizes neutrality of incentives across activities. Nevertheless, a small number of activities are still favoured through special fiscal incentives or tariffs.

In the agricultural sector, liberalization and reductions in state assistance initiated in the early 1990s have resulted in difficult adjustments which, nevertheless, underlie strong output expansion directed at both domestic and foreign markets. However, the concentration of various border and internal support measures in a limited range of favoured products (certain crops and dairy products) may well hinder further gains by misallocating labour, land, and capital resources at the expense of other activities. Driven by international demand, production of coca leaf and derived products still appears sizeable albeit declining.

Peru has a revealed comparative advantage in certain fishing and mineral products, which together typically account for some 60% of its total merchandise exports. Peru has a large fishing industry which is, however, highly cyclical and suffers from apparently policy-induced over-investment and over-fishing. Peru's strategy to attract local and foreign private investment has been particularly successful in the mining industry, which has regained its leading role in the economy. Mining and energy attracted just over one third of total direct foreign investment into Peru during 1992-99.

Besides the processing of mineral, agricultural and fisheries products, manufacturing activities make only a small contribution to Peru's economy; these activities have experienced extensive restructuring from increased import competition.

The Peruvian State used to be a major supplier of services, including in financial, transport, and telecommunications activities, but such involvement has decreased dramatically since the mid 1990s. In parallel, foreign access to Peru's services market has improved markedly. The ambitious privatization programme and the general policy of promoting private investment has induced important structural changes in most service areas. With respect to privatized public services, the Peruvian authorities are seeking to establish a strong regulatory framework in particular to prevent the abuse of dominant positions in service markets where competition is limited by technical constraints.

Trade Policy and Foreign Trading Partners

Through its participation in the WTO and regional initiatives, Peru has tried to enhance access to international markets so as to generate economies of scale and specialization. While welcoming the strengthening of the multilateral trading system and increased transparency and predictability that followed the conclusion of the Uruguay Round and the establishment of the WTO, the Peruvian authorities have noted that in some areas actual results have not met expectations. In their view, this is particularly the case in sectors such as agriculture, textiles, and clothing, and in respect to new disciplines for the adoption of anti-dumping measures.

Peru ratified the Marrakesh Agreement Establishing the WTO in December 1994, which is an integral part of the Peruvian legislation. Peru has enacted or amended various domestic regulations to harmonize them with its international obligations and thus facilitate their application, in particular in the area of intellectual property rights. As a result of the Uruguay Round, Peru bound its entire tariff, compared with previous bindings on only 460 lines. Peru grants at least MFN tariff to all partners.

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Under the WTO's General Agreement on Trade in Services (GATS), Peru undertook horizontal commitments with respect to movement of natural persons and treatment of foreign investment; although these commitments apply only to sectors included in its GATS Schedule, in practice Peru's legislation grants similar market access across most service activities. Sector-specific commitments cover 7 out of 12 broad categories of services. Reflecting Peru's legislation, market access and national treatment for services supplied through commercial presence (i.e. treatment granted to foreign investment) has been in general fully committed. Peru's commitments in telecommunication services are particularly comprehensive, with all services bound except for the granting of national treatment in relation to the presence of natural persons.

In parallel with its participation in the multilateral trading system, Peru takes part in regional integration schemes within the Andean Community and the Latin American Integration Association, as well as in the Asia-Pacific Economic Cooperation forum and the negotiating groups of the Free Trade Area of the Americas. Despite Peru's long-standing participation in the regional integration processes within Latin America, the share of reciprocal preferential trade in total trade remains relatively modest. In addition to the negotiated schemes, Peru benefits from increased market access to several countries under Generalized System of Preferences schemes, including under the special regimes granted by the European Union and the United States to promote alternatives to coca cultivation and production. According to the Peruvian authorities, these schemes have resulted in substantial export diversification.

TRADE POLICY REVIEW BODY**PERU****Report by the Government - Parts I and II****I. EXECUTIVE SUMMARY****A. RECENT DEVELOPMENTS**

1. Over the past six years, Peru has continued to intensify its economic reforms and trade liberalization with a view to strengthening its integration in the world economy. To that end, it has not only made the adjustments required to meet its multilateral commitments, but has also reinforced the liberalization of its external goods and services market through trade negotiations.

2. Peru became a Contracting Party to the GATT in 1951, participated in the Uruguay Round negotiations and was an original Member of the WTO. It adapted its domestic legislation to the Agreements adopted at the conclusion of the Uruguay Round, and has thus respected its multilateral commitments. Since 1 April 2000, Peru has applied the WTO Agreement on Customs Valuation to 100 per cent of its imported goods.

3. In the context of trade liberalization, tariff levels have been lowered and tariff spread reduced, while various restrictions on free trade have been eliminated. There are currently two tariff levels for imports (12 and 20 per cent) and temporary surcharges for certain agricultural products.

4. During this period, the Government's conduct of economic affairs has been marked by prudent management of fiscal and monetary policy, enabling it to balance the budget in 1997 and create suitable conditions for the promotion of investment.

- With respect to monetary policy, the sole objective is price stability, so there is an independent Central Bank which has opted for the monetary base as an intermediate target. From the outset, a floating exchange rate system was also adopted.
- With respect to fiscal policy, the Government continued the tax reform process, simplifying the tax regime in 1994 by retaining only four taxes: the general sales tax, income tax, the selective consumption tax, and the import tax. This reform was marked by stringent fiscal discipline and in 1997 resulted in the first surplus in the public sector accounts for 30 years.

5. These reforms, coupled with a suitable legal framework and sound economic management, have enabled the country to be considered attractive for foreign investment. The share of investment in GDP terms rose from 15.6 per cent in 1990 to 24.4 per cent in 1997, dropping to 21.7 per cent by the end of 1999 owing to the 1998 and 1999 crises. As regards the foreign debt, the agreements signed with the Paris Club and the commercial banks between 1996 and 1997 led to the regularization of Peru's relations with its creditors.

6. As a result of this situation, the Peruvian economy grew at an average annual rate of 5.5 per cent during the period 1994-1999, while inflation fell to 3.7 per cent in 1999. Meanwhile, exports and imports increased by an average annual rate of around 9.7 and 8.4 per cent respectively.

7. In parallel with its domestic reforms, the Government consolidated its involvement in trade integration mechanisms at various levels.

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- Peru formally became a member of the Asia-Pacific Economic Cooperation forum (APEC) in November 1998.
- At the Americas level, Peru is taking an active part in the negotiations on the Free Trade Area of the Americas (FTAA).
- At the regional level, the integration process within the Latin American Integration Association (LAIA) is continuing.
- At the subregional level, Decision 414 of the Andean Community (CAN), which facilitates Peru's full reintegration into the Andean Free Trade Area and sets a timetable for progressive reductions in tariffs for its members, entered into force in July 1997. In 1998, Decision 439 approving a framework agreement for the liberalization of trade in services was adopted.

B. OUTLOOK

8. Over the next few years, Peru's economic policy will be aimed at promoting sustained growth in GDP with a view to achieving annual increases of over 6 per cent and lowering inflation to international levels so as to achieve economic and social progress in Peru. In order to do so, Peru considers it essential to maintain a balance in public finance and a cautious monetary policy, and to pursue the structural reform process.

9. Peru will maintain its commitment to a free trade regime, the free movement of capital and a floating exchange rate, and to further reforms in foreign trade and the customs regime.

10. Peru welcomes the initiative on a new round of multilateral trade negotiations provided that a consensus is reached on a broad and balanced agenda which reflects the interests of all Members and that transparent working methods are adopted so as to guarantee equitable participation by all Members concerned.

11. For Peru, it is particularly important to strengthen a stable, transparent and predictable trade environment that allows greater access to international markets for Peru's exports.

II. TRADE AND ECONOMIC POLICY ENVIRONMENT

A. TREND IN THE ECONOMIC ENVIRONMENT

12. The favourable trend in the Peruvian economy's major economic indicators since 1994 has to a large extent depended on prudent management of fiscal and monetary policy and the dynamic structural reform process initiated in the early 1990s. As a result of the new economic environment, inflation fell from 7,600 per cent at the beginning of the 1990s to one-digit levels of between 3 and 4 per cent by the end of the decade. In 1997, fiscal balance was achieved after a period of deficits exceeding 10 per cent of GDP at the end of the 1980s and the proper conditions were in place to encourage investment on a permanent basis and achieve sustained growth of economic activity. This process was stimulated by Peru's reintegration into the international financial system, the pacification process, a series of structural reforms and the adjustment programme which reduced the Peruvian economy's country risk and resulted in a substantial flow of foreign capital, mainly over the medium and the long term, which has financed a large part of the growth in production without endangering the viability of the external accounts.

13. During this period, the sole objective of monetary policy has been to stabilize prices, as established in the 1993 Constitution and the Organizational Law on the Central Bank. Since 1994, the Bank has announced target ranges of inflation for the year in order to reaffirm its commitment to lowering inflation and bringing it down to the level of the industrialized countries. In order to achieve this ultimate objective, the monetary authorities have opted for growth in the monetary base as an

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intermediate target. Another important element in this process has been the adoption of a floating exchange rate system which has allowed Peru to face crises such as the drop in the terms of trade without suffering traumatic effects. Interventions in the foreign exchange market are mainly to prevent unjustified fluctuations in the exchange rate. These interventions led to a strengthening of the Central Bank's foreign exchange position, which went from a negative situation in July 1990 to around US\$2,500 million at the end of 1999, amounting to 1.8 times the monetary base.

14. In the area of fiscal policy, after the initial programme in 1990 eliminated the major sources of imbalance, particularly the financing of the Central Bank, in 1992 the Government adopted a series of measures to simplify the tax regime and restructure the tax administration. The result of this process was that in 1994 the tax regime only comprised four taxes: the general sales tax, income tax, the selective consumption tax, and the import tax. This policy, combined with careful management of fiscal spending, meant that in 1997, the public sector accounts showed a surplus after 30 years. In 1998 and 1999, the events which occurred due to external crises and the El Niño phenomenon had an impact on fiscal performance.

15. At the end of 1999, the Government adopted a Law on Fiscal Prudence and Transparency which *inter alia* provides that the fiscal deficit may not exceed one per cent (1%) of GDP as of 2002 and that the increase in the Government's non-financial spending should not exceed two per cent (2%) in real terms. It should be noted that between 1996 and 1997, the Government reached an agreement with the Paris Club and the commercial banks that regularized relations with its creditors. It should also be emphasized that the privatization process, which has been on a large scale since 1994, has contributed a sum of around US\$9,000 million through the sale of enterprises.

16. It is important to emphasize that the reforms undertaken such as the liberalization of foreign trade, the foreign exchange market, the capital account and the financial system, together with privatization and reforms in the labour market and legislation on foreign investment, have given economic activity an important boost, particularly investment. Investment's share of the GDP rose from 15.6 per cent in 1990 to 24.4 per cent in 1997. Following the crises in 1998 and 1999, however, the figure fell to 21.7 per cent at the end of 1999.

17. It should be emphasized that the larger amount of investment has had an important impact on foreign trade as it has not only made for a greater supply of goods for export but has also led to higher demand for imported goods. This situation meant that the deficit in the balance-of-payments current account rose from US\$2,648 million in 1994 to US\$3,790 million by the end of 1998, falling subsequently to US\$2,030 million in 1999. It is important to note, however, that during the period 1994-1999 over two-thirds of this deficit was financed by long-term private capital (excluding the revenue generated by privatization).

18. The preservation of the economic foundations and the legal framework for foreign investment have enabled Peru to be considered an attractive place for foreign investment over the past decade and have complemented the efforts made at the domestic level to restore sustained growth after the international crises.

19. Article 63 of the 1993 Constitution gives foreign and domestic investment equal treatment. Furthermore, current legislation gives total freedom to repatriate profits and dividends abroad, lease technology, pay trademark rights, and also allows for the possibility of private investment in public services. The Government has signed bilateral agreements which allow foreign investors to insure their investments against non-commercial risks with organizations such as the Multilateral Investment Guarantee Agency (MIGA) and the Overseas Private Investment Corporation (OPIC) and to sign tax stabilization agreements with the Government.

20. Foreign investment flows increased significantly throughout the decade. From a level of close to US\$13 million in 1990, they rose to around US\$1,600 million in 1994 and US\$2,200 million

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at the end of 1999, even though flows of investment to Peru fell in 1998, as they did in a large part of Latin America. During the period 1994-1999, the main sources of foreign direct investment were Spain, United States of America, United Kingdom, Canada and Chile. The sectors which received the major part of the accumulated flow of foreign direct investment during this period were communications, energy, mining, industry and finance.

21. As a result of this situation, during the period 1994-1999 Peru's economy grew at an average annual rate of 5.5 per cent, while inflation fell to around 3.7 per cent in 1999. In this new environment marked by greater economic stability foreign trade was boosted, partly as a result of the improvement in Peru's terms of trade. Consequently, exports and imports increased between 1995 and 1999 at average annual rates of around 9.7 per cent and 8.4 per cent respectively.

22. In 1998, as a result of the impact of El Niño and of the financial crises in Asia and Russia on Latin America's emerging economies, the fall in the price of exports of primary goods led to a decrease of 13 per cent in the terms of trade compared with the average for 1997, affecting consumption and private investment in particular due to the negative expectations regarding future income. The drop in domestic demand, 0.6 per cent in 1998, meant that Peru's economy showed only 0.3 per cent growth in GDP during that year. The value of exports and imports of goods fell by 16.1 and 4.1 per cent respectively in comparison with 1997 levels. Nevertheless, throughout the year, the Central Bank pursued its efforts to achieve price stability, so the inflation rate continued to fall and in December 1998 reached a cumulative rate of around 6 per cent.

23. Peru's economy has been showing signs of recovery since the last quarter of 1999, recording growth in GDP of 3.8 per cent for the year, the highest rate in Latin America. Exports once again experienced vigorous growth and rose by 6.6 per cent, even though there was a 5.2 per cent reduction in the terms of trade, while the value of imports fell by 18.1 per cent. In terms of goods and services, the value of Peru's exports rose from US\$7,487 million in 1998 to US\$7,793 million in 1999 (an increase of 4.1 per cent), while imports of goods and services fell from US\$10,492 million to US\$8,857 million (15.6 per cent).

24. In addition, efforts to reduce inflation to international levels continued. In 1999, inflation was 3.7 per cent, the lowest rate recorded in Peru's economy over the past 40 years and the second lowest in the past 60 years.

B. TRADE POLICY OBJECTIVE

25. Peru's trade policy of openness and liberalization seeks to integrate Peru in the global economy so that it can take advantage of specialization in international markets. Peru therefore pays particular attention to strengthening a predictable international trade system based on fair competition, the development of comparative advantages and less protectionism.

26. The trade policy objective is to help lay down the bases for sustained growth and the modernization of the Peruvian economy, seeking to enhance its efficiency and productivity in order to guarantee internal and external competitiveness and greater participation in global trade flows.

C. REINFORCEMENT OF THE OPENING UP OF THE PERUVIAN ECONOMY

27. One of the foundations of the structural reforms was trade liberalization. In order to make international prices the catalyst for efficient production and ensure that the domestic market faced external competition, tariff levels and spread were drastically reduced and all quantitative restrictions on foreign trade were abolished. At the end of the past decade, there were 39 tariff rates (with an average of 70 per cent) and, if existing surcharges are included, the total was 56 effective tariff rates, which distorted the efficiency of domestic production and the development of export activities. As part of the process of reinforcing the opening up of trade, in April 1997 the two tariff levels were

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reduced from 25 to 20 per cent and 15 to 12 per cent respectively. At present, 85 per cent of tariff headings are subject to a rate of 12 per cent and the remainder to 20 per cent, so that the average weighted tariff for the whole of the NANDINA classification fell from 15.3 per cent in December 1996 to 13.1 per cent after the aforementioned tariff reductions. It should be added that there are temporary surcharges on some agricultural products. Certain restrictions which affected free trade have also been abolished.

D. RELATIONS WITH MAJOR TRADING PARTNERS

28. Peru's major trading partner during the period 1994-1999 was the United States of America, which accounted for 33 per cent of its trade in 1998. Exports and imports from the United States amounted in each case to 33 per cent of the relevant totals. Trade with the United States has been given renewed impetus by the Andean Trade Preferences Act since Peru was made eligible for this preferential scheme in 1993.

29. The second trading partner in terms of importance is the European Union, which accounted for 22 per cent of Peru's total volume of trade in 1998. The share of Peruvian exports to the European Union fell from 31 per cent in 1994 to 22 per cent in 1998. The share of imports from the Union rose from 16 per cent to 22 per cent in the same year.

30. The LAIA countries' share of total trade during this period remained steady and in 1998 represented 22 per cent. Countries belonging to the Andean Community play an important role and account for 8 per cent of trade, corresponding to 8 per cent and 7 per cent of exports and imports respectively; next come the MERCOSUR countries, which in 1998 accounted for 7 per cent of Peru's trade, corresponding to 4 per cent for exports and 9 per cent for imports.

31. Lastly, other important foreign trading partners are Asian nations such as Japan and the People's Republic of China. After a period of sustained growth (17.1 per cent) in the value of exports of goods to these countries during the period 1994-1997, in 1998 the volume fell sharply (53.4 per cent), while the rate of growth in imports of goods from these countries, which was 5.8 per cent over the period 1994-1997, fell to 3.2 per cent in 1998.

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