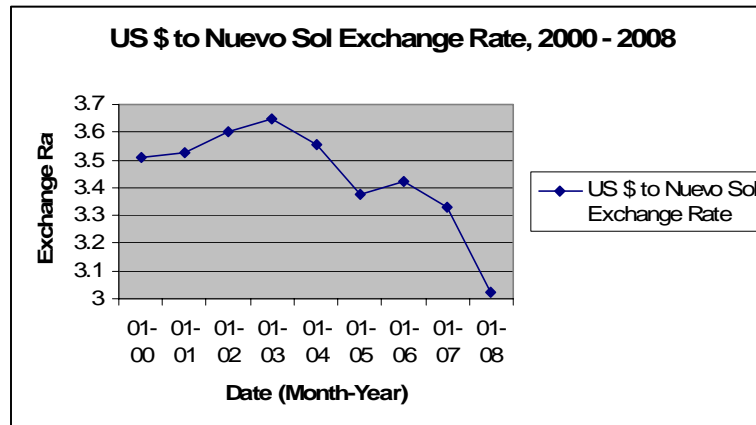


# Peru: Economic Analysis



SAMPLE

## Section 1: Introduction



Source: The World Factbook, CIA.com

The country of Peru, situated on the western coast of South America has experienced many economic changes over the last century. The official language is Spanish, ascended from the Spanish conquest of its Incan populated area in 1513. The currency is the Nuevo sol and it has appreciated against the U.S. dollar in the last five



Source: Google Maps

years (Peru Explorer). In an attempt to tame high inflation, the Nuevo sol replaced the inti, the previous currency; in 1991 (1 nuevo sol equaled 1 million inti). The inti had replaced the sol in 1985 at a rate of 1,000 to 1, showing the extremely high inflation that occurred between the years 1985 and 1991 (MSN.com). Peru did not endure recent currencies devaluation like other Latin American countries such as Brazil and Argentina and the IMF forecasts a growth rate of 6% in 2008. The diverse geography as seen in on the left, helps

shape Peru's economic structure. The mountainous areas provide Peru with a gamut of

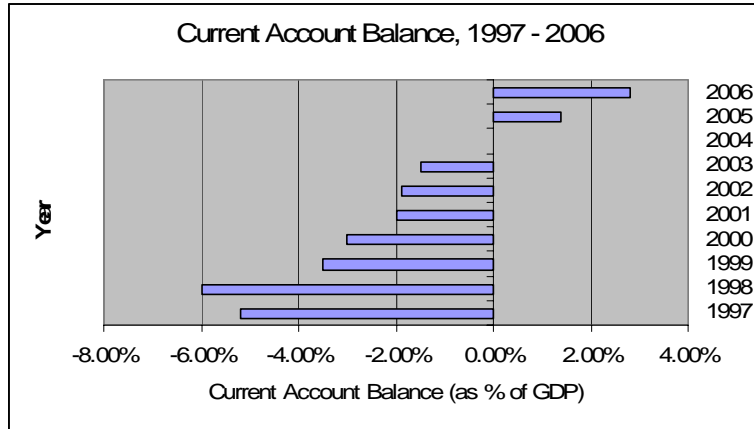
metal resources such as copper, gold, and zinc. The tropical areas are used for growing coffee and coca leaves while the coastal areas allow for superior fishing grounds (Peru History). In fact, prior to 1996, Peru was the largest producer of coca leaves in the world, and now stands as the second largest after Columbia. The past ten years have shown inconsistent economic performance. However, the Peruvian economy grew by over 4% per year between 2002 and 2006, with a relatively stable exchange rate and low inflation (CIA: World). Although the macroeconomic performance has been thriving in the past few years, underemployment and poverty have remained persistently high. The percentage of the population living below the poverty line reached an astounding 44.5% in 2006 and malnutrition has been an ever growing issue that the current president Alan García has promised to resolve (Commerce, The Economist).

## **Section 2: International Trade and Finance**

### *2-1 Current Trends*



Source: KITCO Base Metals 2003 – 2008



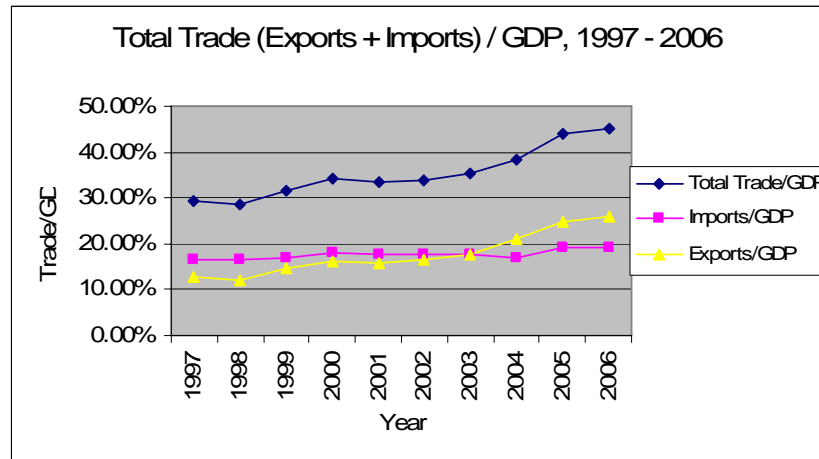
Source: Author's Calculations, IMF

Peru's heavy reliance on the export of metals like copper, gold and zinc could possibly be a cause for concern. With the fluctuations in the world prices of metals, their economy has fallen subject to these variations because of their overdependence on these materials. Recently, this has favored their economy as the price of copper has increased from less than \$1 in 2003 to \$3.73 as of March 2008 ("KITCO Base Metals"). This has likely assisted in the shift of the current account from a deficit to a surplus since 2003 when copper gained value. There was a 7.5% increase in GDP in 2007, as a result of increased world prices for metals and minerals. Interest rates on Peruvian bonds were relatively low, showing growing competence in fiscal policies and trade agreements ("KITCO Base Metals").

Along with the increasing prices of metals affecting the Peruvian economy, the weakening dollar may also cause an impact. As The United States is Peru's largest trading partner, see Appendix A, the price of imports and exports will be affected. They will be able to import from the U.S. for cheaper, while the exports may decrease, thus potentially shifting the trade balance. Lastly, the U.S-Peru Promotion Agreement (PTPA) that was signed over a year ago is close to ratification. This agreement will make

80% of U.S exports of consumer and industrial goods to Peru duty free, thus potentially increasing trade between the two countries (Commerce, The Economist).

## 2.2 – International Trade

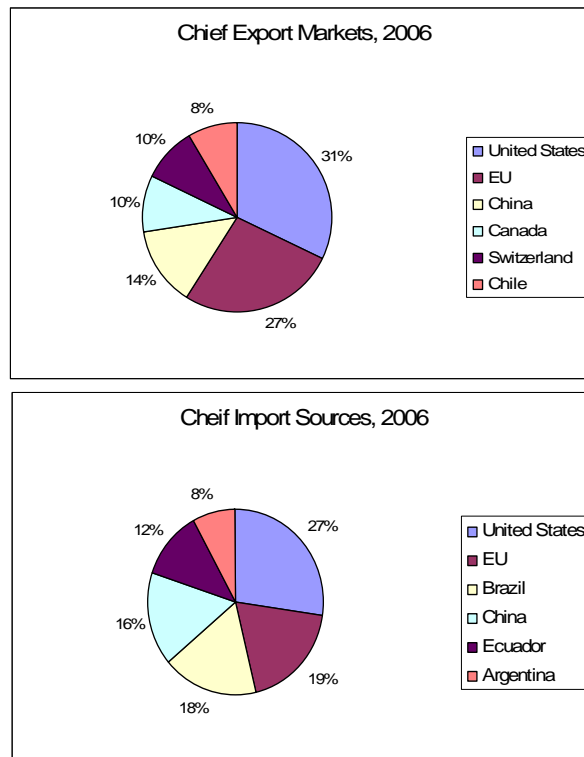


Source: Author's Calculations, IMF

International trade is largely important to the economy of Peru as it constituted 45.20% of GDP in 2006. This figure has steadily increased over the last ten years from 29.40% in 1997, reflecting an increasing dependence on trade to produce revenue. The trade balance has also shifted across the same time frame from a trade deficit of 5.20% of GDP in 1997 to a surplus of 2.8% of GDP in 2006. This has been a result of the reduction of trade barriers from chief trading partners such as the U.S, the increased value of the exportation of metals such as copper and gold, and president García's focus on decreasing trade barriers. If one was to look back at Peru's economic trade policy over 20 years ago when the same president García ruled, they would encounter a much different situation. When García served in the 1980's he believed in complete protectionism. He effectively banned the importation on many goods such as foreign cars and Chilean wine (Commerce, The Economist). However, since coming to office again in 2006 he found a new passion for free trade. In a meeting with the World Trade

Organization in Lima he stated “More trade and more investment [means] less migration, less poverty and less environmental destruction” (Commerce, The Economist). This view could potentially mean an even greater increase in volume of trade in the years to come.

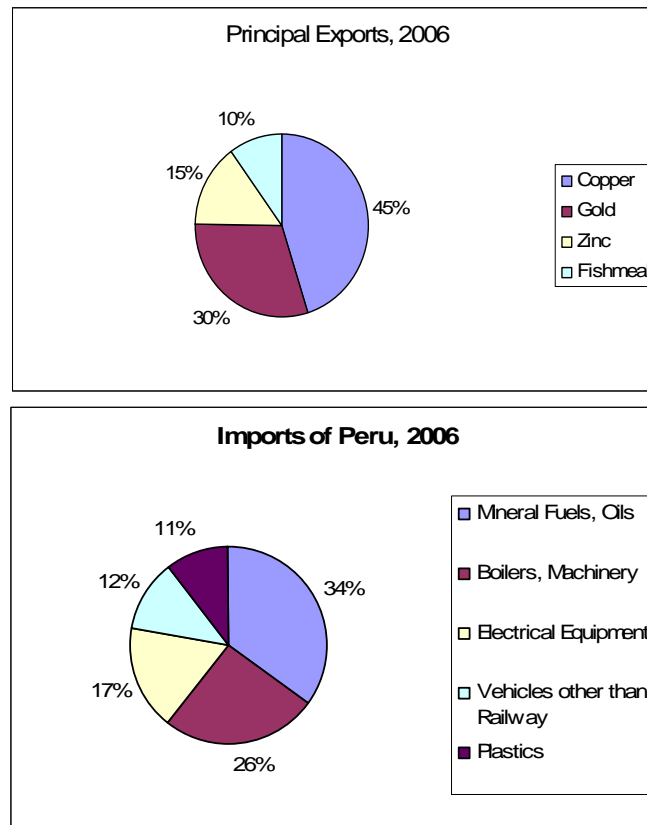
### 2.3 – Major Trading Partners



Source: Country Commerce, The Economist

International trade is critical to the Peruvian economy and it occurs among five prevalent countries. Peru’s chief export sources by volume of trade in 2006 were the U.S, E.U, China, Canada, Switzerland, and Chile respectively. The U.S showed a 2.5% increase from the previous year, while China increased by an astounding 21% (Country Commerce, EIU). With regard to imports, Peru’s major trading partners in 2006 were the U.S, E.U, Brazil, China, Ecuador, and Argentina. China experienced the largest increase of imports with an increase of 49.9% from the 2005 level (Country Commerce, EIU).

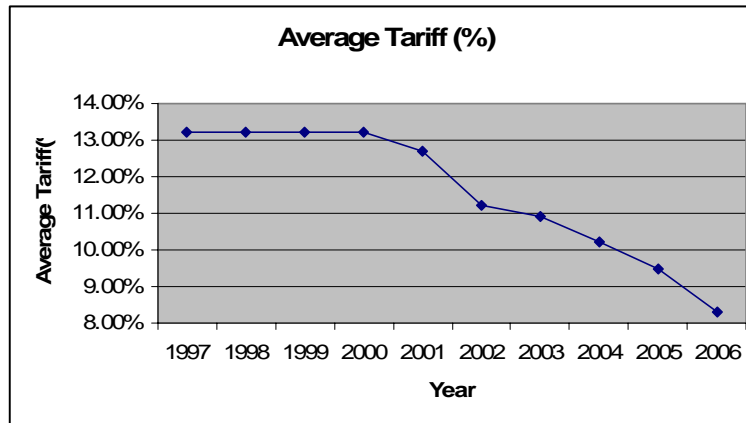
## 2.4 – Major Export and Import Commodities



Source: Autor's Calculations, UN Comtrade

A specific set of goods are the most often traded with the countries mentioned above. Copper, gold, zinc, and fishmeal are among the top four most exported commodities in Peru. In 2006, they exported over \$6 billion of Copper and more than \$4 billion of gold (see Appendix B). Intermediate goods are by far the largest group imported by Peru. Peru relies heavily on these goods in order to produce other goods to sell to the domestic market and abroad. The largest imported commodities are mineral fuels and oils (34%), boilers and machinery (26%), electrical equipment (17%), vehicles other than railway (12%), and plastics (11%).

## 2.5 – Trade Restrictions



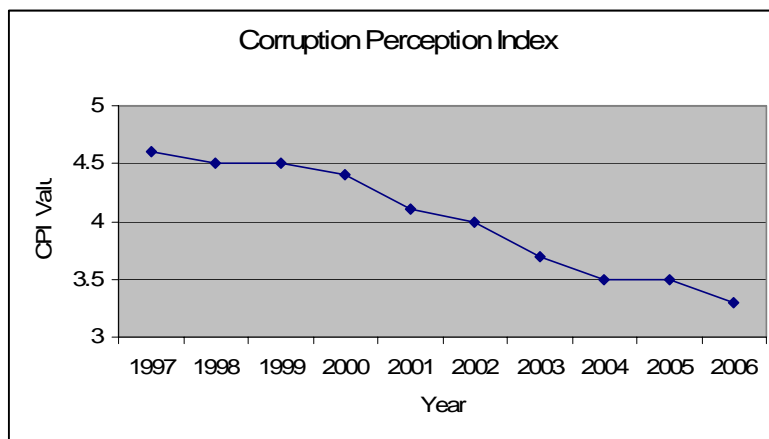
Source: Author's Calculations, UNCTAD

There is currently a number of trade restrictions imposed upon the goods discussed above. Peru is a member of the Andean Community of Nations (CAN) along with Bolivia, Columbia, and Ecuador, which guides most of their trade practices. Through the Supreme Decree 211–2006–EF on December 28th 2006, the Garcia administration eliminated tariffs on almost 3,000 capital goods and industrial inputs. This effectively lowered Peru's average tariff from 10.2% to 8.3%. The decree terms are as follows; 3,134 items can enter the country tariff free, seven are assigned a tariff at 4%, 2,730 at 12%, 48 at 17%, 759 at 20% and 316 at 25% (Country Commerce, EIU). Peru has been a member of the World Trade Organization since January 1, 1995 (Peru and the WTO, WTO). This entrance into the WTO marked numerous changes in trade policy. The trade weighted average tariff from 1995 to 1999 was 13.3% and reduced to 8.3%. (The World Bank). The percentage of duty free exports increased from 33.1% in 1995-1999 to 41.8% in 2005-2006. These changes reflect the policies imposed by the World Trade Organization in order to liberalize trade.

Peru has been the claimant in two trade disputes, both concerning their exports of fisheries. One dispute arose in 1995 because of the trade description of scallops in

France. The French government order that stated the official name and trade description of the product was thought to discourage competition on the French market. Peru's scallops could no longer be sold as "Coquille Saint-Jacques" even though there was no discernable difference between French and Peruvian scallops. The other dispute involved the trade description of sardines. In 2001, Peru complained to the EC about a trade regulation that did not allow Peruvian exports to use the name "sardines" for their products. The following year a panel concluded that the EC Regulation was inconsistent with Article 2.4 of the TBT Agreement (WTO, Trade Disputes).

### 2.6 – Institutional Development and Corruption



Source: Author's Calculations, Transparency International

Peru's level of institutional development is poor and has gotten worse over the last ten years. The Corruption Perception index gives a CPI score that relates to the perceptions of corruption as seen by business people and country analysts ranging from 10 (very clean) to 0 (highly corrupt) (Transparency International). The score given to Peru in 2006 was 3.3. Interestingly, over the past ten years it appears as though Peru has become more corrupt as their score has fallen from 4.6 since 1997. They were about in the middle of the pack in standing with the world in 2006, which leaves room for much improvement. The majority of Peru's democratic institutions motivate almost no public

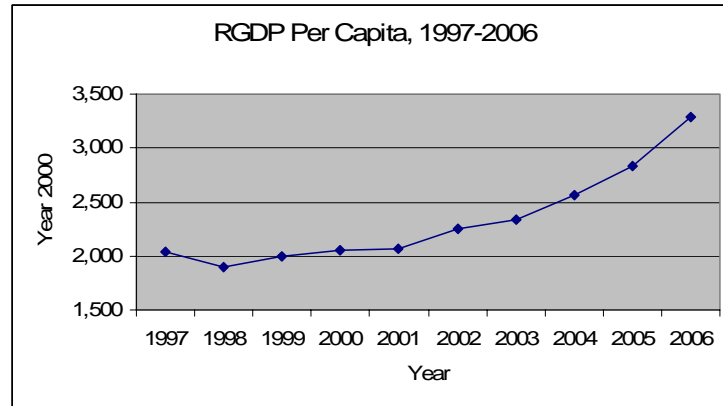
trust, and Congress and the judiciary are held in contempt by most Peruvians. High ranked officials, such as Intelligence Chief Vladimiro Montesinos, are imprisoned and faced with charges ranging from money-laundering to organizing death squads and may be sentenced to life imprisonment if convicted (BBC News). High rates of bribery among government officials contribute to Peru's poor level of institutional development. The government has been successful in past years in strengthening the Banco Central de Reserva del Peru (BCRP, the Central Bank), however, the poor reputation of other democratic institutions could potentially be a source of political instability. As the 2006 Congress inspires very little confidence, public disdain of the corrupt political class will likely remain vocal (CIA: The World).

### *2.7 – Suggestions on Improving Trade Policy*

Even though it is evident that Peru has prospered financially over the past few years, with a GDP that is 45% larger than in 2001, improvement can be made to their trading practices (“Suffer the Children”). The increase in GDP is not properly transferring to the improvement of social well-being. Health officials estimate that 30% of young Peruvian children suffer from chronic malnutrition. The number skyrockets to 90% in locations such as Apurímac, an area located in the Andes where poverty levels reached 74.8% in 2006 (“Transparency International”). The lack of efficient transport is the healthcare and education improvements are at a standstill. Therefore, it is important to not only increase spending for social programs, but to improve their effectiveness as well. This can be done by investment in infrastructure that will support the social efforts as well as improve trade. Through the improvement of roads and other infrastructure, goods and services would be able to move more freely throughout the country. This will

result in the potential decrease of the national poverty level as well as improve the overall structure for the trade of goods.

### **Section 3: Conclusion**



Source: WDI

Peru has been successful in their attempts to increase RGDP and reduce barriers to trade over the last ten years. In addition, the RGDP per capita has increased dramatically as well. The GDP growth has been accompanied by low inflation of 1.14% in 2006 and 0.80% for the first four months of 2007. It is expected that annual economic growth will average 5.7% in 2008-12, as a result of strong exports, investment and private consumption growth. The advancement of the Camisea natural-gas project and various additional major mining projects add to the positive forecast. It is projected that the current account will continue a surplus in 2008 however fall into a deficit in 2009, because of an increase in imports and the possible decrease of metal prices from their current high levels. As a result of the free-trade agreement with the US, exports of agricultural products and textiles will likely be strong in the US market (Peru, The Economist).

## Appendix A

### **Chief Export Markets (2006)<sup>1</sup>**

United States	\$5,400,000,000
EU	\$4,500,000,000
China	\$2,300,000,000
Canada	\$1,600,000,000
Switzerland	\$1,600,000,000
Chile	\$1,400,000,000

### **Chief Import Sources (2006)**

United States	\$2,500,000,000
EU	\$1,700,000,000
Brazil	\$1,600,000,000
China	\$1,500,000,000
Ecuador	\$1,100,000,000
Argentina	\$724,000,000

---

<sup>1</sup> "Country Commerce Peru." Economist Intelligence Unit. The Economist. Busref.Lib.Umn.Edu. 20 Mar. 2008. <[www.eiu.com](http://www.eiu.com)>.

## Appendix B

### **Principal Exports<sup>2</sup> 2006**

Copper	\$6,034,000,000
Gold	\$4,061,000,000
Zinc	\$1,991,000,000
Fishmeal	\$1,333,000,000

### **Principal Imports, 2006**

Mineral Fuels, Oils	2,959,729
Boilers, Machinery	2,172,418
Electrical Equipment	1,470,124
Vehicles other than Railway	993,069
Plastics	893,847

---

<sup>2</sup> "Country Briefings: Peru" The Economist, Mar.20 2008 <[www.economist.com](http://www.economist.com)>.

## Works Cited

- "CIA: The World Factbook" Central Intelligence Agency. Mar.20 2008 <[www.cia.gov/library](http://www.cia.gov/library)>.
- "Commerce Between Friends and Foes." (2007). 15 Mar. 2008 <[www.economist.com](http://www.economist.com)>.
- "Country Briefings: Peru" The Economist. Mar.20 2008 <[www.economist.com](http://www.economist.com)>.
- "Country Commerce Peru." Economist Intelligence Unit. The Economist. Busref.Lib.Umn.Edu. 20 Mar. 2008. <[www.eiu.com](http://www.eiu.com) >.
- "Country Report." International Monetary Fund. 19 Mar. 2008 <<http://imf.org>>.
- Google Maps. 20 Mar. 2008 <[www.lib.utexas.edu/maps/thematic.html](http://www.lib.utexas.edu/maps/thematic.html)>.
- "KITCO Base Metals" 5 Year Copper Spot. Mar. 20 2008. <[kitcometals.com](http://kitcometals.com)>.
- "Long Haul for Peru Corruption Inquiry." BBC News (2002). 3 Apr. 2008 <<http://news.bbc.co.uk/2/hi/americas/1794129.stm>>.
- "Peru and the WTO." World Trade Organization. Mar.20 2008. <[www.wto.org](http://www.wto.org)>.
- "Peru: Country." MSN Encarta (2006). 18 Mar. 2008 <[http://encarta.msn.com/encyclopedia\\_761570790\\_6/Peru\\_\(country\).html](http://encarta.msn.com/encyclopedia_761570790_6/Peru_(country).html)>.
- "Peru History." Peru Explorer. Mar. 20 2008. <[www.peru-explorer.com](http://www.peru-explorer.com)>.
- "Suffer the Children." The Economist (2008). The Economist.Com. 20 Mar. 2008.<[www.economist.com](http://www.economist.com)>.
- The World Bank. WDI & GDF Online. 20 Mar. 2008 <<http://web.worldbank.org>>.
- Transparency International: The Global Coalition Against Corruption. Corruptions Percetion Index Peru (1997 – 2006). 20 Mar. 2008 <[www.transparency.org](http://www.transparency.org)>.
- UNCTAD, 1995-2006, <[http://www.unctad.org/en/docs/tdstat31ch4\\_enfr.pdf](http://www.unctad.org/en/docs/tdstat31ch4_enfr.pdf)>

## Appendix C

<b>Year</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
<b>RGDP Per Capita (2000 US \$)<sup>1</sup></b>	2,046	1,892	1,990	2,050.00	2,071	2,247	2,330	2,559	2,835.71	3,285.21
<b>Trade/GDP<sup>2</sup></b>	29.40%	28.70%	31.70%	34.20%	33.50%	33.90%	35.40%	38.30%	44.00%	45.20%
<b>Imports/GDP<sup>2</sup></b>	16.60%	16.70%	17.00%	18.20%	17.60%	17.50%	17.80%	17.10%	19.20%	19.10%
<b>Exports/GDP<sup>2</sup></b>	12.80%	12.00%	14.70%	16.00%	15.90%	16.40%	17.60%	21.20%	24.80%	26.10%
<b>Current Account Balance<sup>2</sup> (%GDP)</b>	-5.20%	-6.00%	-3.50%	-3.00%	-2.00%	-1.90%	-1.50%	0.00%	1.40%	2.80%
<b>Corruption Perception Index<sup>3</sup></b>	4.6	4.5	4.5	4.4	4.1	4	3.7	3.5	3.5	3.3
<b>CPI Country Rank</b>	40	41	40	41	44	45	59	67	65	70
<b>Average Tariff<sup>4</sup></b>	13.20%	13.20%	13.20%	13.20%	12.70%	11.20%	10.90%	10.20%	9.50%	8.30%

<sup>1</sup> The World Bank. WDI & GDF Online. 20 Mar. 2008 <<http://web.worldbank.org>>.

<sup>2</sup> "Country Report." International Monetary Fund. 19 Mar. 2008 <<http://imf.org>>.

<sup>3</sup> Transparency International: The Global Coalition Against Corruption. Corruptions Percetion Index Peru (1997 – 2006). 20 Mar. 2008 <[www.transparency.org](http://www.transparency.org)>

<sup>4</sup> UNCTAD, 1995-2006, <[http://www.unctad.org/en/docs/tdstat31ch4\\_enfr.pdf](http://www.unctad.org/en/docs/tdstat31ch4_enfr.pdf)>