

CONFORMED COPY

LOAN NUMBER 7200 - PE

Loan Agreement

(Third Programmatic Social Reform Loan)

between

REPUBLIC OF PERU

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated November 17, 2003

LOAN AGREEMENT

AGREEMENT, dated November 17, 2003, between REPUBLIC OF PERU (the Borrower) and INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (the Bank).

WHEREAS (A) the Bank has received from the Borrower a letter, dated October 6, 2003 describing a program of actions, objectives and policies designed to achieve structural adjustment and social reform in the Borrower's economy (hereinafter called the Program), declaring the Borrower's commitment to the execution of the Program, and requesting assistance from the Bank in support of the Program during the execution thereof;

(B) the Borrower has carried out the measures and taken the actions described in Schedule 3 to this Agreement to the satisfaction of the Bank and has maintained a macroeconomic policy framework satisfactory to the Bank; and

(C) on the basis, *inter alia*, of the foregoing, the Bank has decided in support of the Program to provide such assistance to the Borrower by making a loan in one tranche (the Loan) as hereinafter provided;

NOW THEREFORE the parties hereto hereby agree as follows:

ARTICLE I

General Conditions; Definitions

Section 1.01. The "General Conditions Applicable to Loan and Guarantee Agreements for Fixed-Spread Loans" of the Bank dated September 1, 1999, with the modifications set forth below (the General Conditions) constitute an integral part of this Agreement:

(a) Section 2.01, paragraph 41, is modified to read:

“‘Project’ means the program, referred to in the Preamble to the Loan Agreement, in support of which the Loan is made.”;

- (b) Section 3.08 is modified to read:

“Each withdrawal of an amount of the Loan from the Loan Account shall be made in the Loan Currency of such amount. If the Loan Currency is not the currency of the deposit account specified in Section 2.02 of the Loan Agreement, the Bank, at the request and acting as an agent of the Borrower, shall purchase with the Loan Currency withdrawn from the Loan Account the currency of such deposit account as shall be required to deposit the withdrawn amount into such deposit account.”;

- (c) Section 5.01 is modified to read:

“The Borrower shall be entitled to withdraw the proceeds of the Loan from the Loan Account in accordance with the provisions of the Loan Agreement and of these General Conditions.”;

- (d) the last sentence of Section 5.03 is deleted;

- (e) Section 9.07 (c) is modified to read:

“(c) Not later than six months after the Closing Date or such later date as may be agreed for this purpose between the Borrower and the Bank, the Borrower shall prepare and furnish to the Bank a report, of such scope and in such detail as the Bank shall reasonably request, on the execution of the program referred to in the Preamble to the Loan Agreement, the performance by the Borrower and the Bank of their respective obligations under the Loan Agreement and the accomplishment of the purposes of the Loan.”; and

- (f) Section 9.05 is deleted and Sections 9.06, 9.07 (as modified above), 9.08 and 9.09 are renumbered, respectively, Sections 9.05, 9.06, 9.07 and 9.08.

Section 1.02. Unless the context otherwise requires, the several terms defined in the General Conditions and in the Preamble to this Agreement have the respective meanings therein set forth and the following additional terms have the following meanings:

- (a) “*A Trabajar*” means both of the Borrower’s programs “*A Trabajar Rural*” and “*A Trabajar Urbano*”;

- (b) “*A Trabajar Rural*” means the Borrower’s Rural Workfare Program;

(c) “*Cédula Viva*” means the pension system for civil service regulated by the Borrower’s Law No. 20530;

(d) “CGR” or “*Contraloría General de la República*” means the Borrower’s supreme audit institution;

(e) “CONSUCODE” or “*Consejo Superior de Contrataciones y Adquisiciones del Estado*” means the National Council for Contracts and Procurement;

(f) “Deposit Account” means the account referred to in Section 2.02 (b) of this Agreement;

(g) “DGAES” or “*Dirección General de Asuntos Económicos y Sociales*” means the Borrower’s General Directorate for Economic and Social Affairs;

(h) “PRONAA” or “*Programa Nacional de Asistencia Alimentaria*” means the Borrower’s National Food Assistance Program;

(i) “PSP” means each of the Borrower’s following six priority social programs: Initial Education, Primary Education, Secondary Education, Individual Health, Community Health and Social and Community Assistance;

(j) “SIAF” or “*Sistema Integrado de Administración Financiera*” means the Borrower’s Integrated Financial Administration System;

(k) “SIS” or “*Seguro Integral de Salud*” means the Borrower’s Integral Health Insurance for priority groups;

(l) “*Trabajar Urbano*” means the Borrower’s Urban Workfare Program.

ARTICLE II

The Loan

Section 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, an amount equal to One Hundred Fifty Million Dollars (\$150,000,000), as such amount may be converted from time to time through a Currency Conversion in accordance with the provisions of Section 2.09 of this Agreement.

Section 2.02. (a) Subject to the provisions of paragraphs (b), and (c) of this Section, the Borrower shall be entitled to withdraw the amount of \$148,500,000 from the Loan Account in support of the Program.

(b) The Borrower shall open, prior to furnishing to the Bank the first request for withdrawal from the Loan Account, and thereafter maintain in its central bank, a deposit account in Dollars on terms and conditions satisfactory to the Bank. All withdrawals from the Loan Account shall be deposited by the Bank into the Deposit Account.

(c) The Borrower undertakes that the proceeds of the Loan shall not be used to finance expenditures excluded pursuant to the provisions of Schedule 1 to this Agreement. If the Bank shall have determined at any time that any proceeds of the Loan shall have been used to make a payment for an expenditure so excluded, the Borrower shall, promptly upon notice from the Bank, (i) deposit into the Deposit Account an amount equal to the amount of said payment, or (ii) if the Bank shall so request, refund such amount to the Bank. Amounts refunded to the Bank upon such request shall be credited to the Loan Account for cancellation.

Section 2.03. The Closing Date shall be December 31, 2004 or such later date as the Bank shall establish. The Bank shall promptly notify the Borrower of such later date.

Section 2.04. The Borrower shall pay to the Bank a fee in an amount equal to one percent (1%) of the amount of the Loan. On or promptly after the Effective Date, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amount of said fee.

Section 2.05. The Borrower shall pay to the Bank a commitment charge on the principal amount of the Loan not withdrawn from time to time, at a rate equal to: (a) eighty five one-hundredths of one per cent (0.85%) per annum from the date on which such charge commences to accrue in accordance with the provisions of Section 3.02 of the General Conditions to but not including the fourth anniversary of such date; and (b) seventy five one-hundredths of one per cent (0.75%) per annum thereafter.

Section 2.06. The Borrower shall pay interest on the principal amount of the Loan withdrawn and outstanding from time to time, in respect of each Interest Period at the Variable Rate; provided, that upon a Conversion of all or any portion of the principal amount of the Loan, the Borrower shall, during the Conversion Period, pay interest on such amount in accordance with the relevant provisions of Article IV of the General Conditions.

Section 2.07. Interest and commitment charges shall be payable semiannually in arrears on January 15 and July 15 in each year.

Section 2.08. The Borrower shall repay the principal amount of the Loan in accordance with the amortization schedule set forth in Schedule 2 to this Agreement.

Section 2.09. (a) The Borrower may at any time request any of the following Conversions of the terms of the Loan in order to facilitate prudent debt management:

- (i) a change of the Loan Currency of all or any portion of the principal amount of the Loan, withdrawn or unwithdrawn, to an Approved Currency;
- (ii) a change of the interest rate basis applicable to all or any portion of the principal amount of the Loan from a Variable Rate to a Fixed Rate, or vice versa; and
- (iii) the setting of limits on the Variable Rate applicable to all or any portion of the principal amount of the Loan withdrawn and outstanding by the establishment of an Interest Rate Cap or Interest Rate Collar on said Variable Rate.

(b) Any conversion requested pursuant to paragraph (a) of this Section that is accepted by the Bank shall be considered a "Conversion", as defined in Section 2.01(7) of the General Conditions, and shall be effected in accordance with the provisions of Article IV of the General Conditions and of the Conversion Guidelines.

(c) Promptly following the Execution Date for an Interest Rate Cap or Interest Rate Collar in respect of which the Borrower has made a request, the Borrower shall pay to the Bank any premium payable in accordance with Section 4.04 (c) of the General Conditions.

Section 2.10. The Director of Public Credit, and any person whom he or she shall designate in writing, is designated as representative of the Borrower for the purposes of taking any action required or permitted to be taken under the provisions of Section 2.02 of this Agreement and Article V of the General Conditions.

ARTICLE III

Particular Covenants

Section 3.01. (a) The Borrower and the Bank shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program.

(b) Prior to each such exchange of views, the Borrower shall furnish to the Bank for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Bank shall reasonably request.

(c) Without limitation upon the provisions of paragraph (a) of this Section, the Borrower shall exchange views with the Bank on any proposed action to be taken after the disbursement of the Loan which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program including any action specified in Schedule 3 to this Agreement.

Section 3.02. Upon the Bank's request, the Borrower shall:

(a) have the Deposit Account audited in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank;

(b) furnish to the Bank as soon as available, but in any case not later than [four] months after the date of the Bank's request for such audit, a certified copy of the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested; and

(c) furnish to the Bank such other information concerning the Deposit Account and the audit thereof as the Bank shall have reasonably requested.

ARTICLE IV

Additional Event of Suspension

Section 4.01. Pursuant to Section 6.02 (p) of the General Conditions, the following additional events are specified:

(a) A situation has arisen which shall make it improbable that the Program, or a significant part thereof, will be carried out.

(b) The Borrower's macroeconomic policy framework has become inconsistent with the objectives of the Program.

(c) An action has been taken or a policy has been adopted to reverse any action or policy under the Program in a manner that would, in the opinion of the Bank, adversely affect the achievement of the objectives of the Program.

(d) An action has been taken or a policy has been adopted to reverse any action listed in Schedule 3 to this Agreement.

ARTICLE V

Termination

Section 5.01. The date February 16, 2004 is hereby specified for the purposes of Section 12.04 of the General Conditions.

ARTICLE VI

Representative of the Borrower; Addresses

Section 6.01. Except as provided in Section 2.10 of this Agreement, the Minister of the Borrower at the time responsible for finance is designated as representative of the Borrower for the purposes of Section 11.03 of the General Conditions.

Section 6.02. The following addresses are specified for the purposes of Section 11.01 of the General Conditions:

For the Borrower:

Ministry of Economy and Finance
Jr. Junín 319
Lima, Perú

Facsimile:

(511) 426-8500 or
(511) 426-9822

For the Bank:

International Bank for
Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable address:

Telex:

Facsimile:

INTBAFRAD
Washington, D.C.

248423 (MCI) or
64145 (MCI)

(202) 477-6391

IN WITNESS WHEREOF, the parties hereto, acting through their duly authorized representatives, have caused this Agreement to be signed in their respective names in Lima, Perú, as of the day and year first above written.

REPUBLIC OF PERU

By /s/Jaime Quijandría Salmón
Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By /s/Marcelo Giugale
Acting Regional Vice President
Latin America and the Caribbean

SCHEDULE 1

Excluded Expenditures

For purposes of Section 2.02 (c) of this Agreement, the proceeds of the Loan shall not be used to finance any of the following expenditures:

1. expenditures in the currency of the Borrower or for goods or services supplied from the territory of the Borrower;
2. expenditures for goods or services supplied under a contract which any national or international financing institution or agency other than the Bank or the Association shall have financed or agreed to finance, or which the Bank or the Association shall have financed or agreed to finance under another loan or a credit;
3. expenditures for goods included in the following groups or subgroups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or subgroups under future revisions to the SITC, as designated by the Bank by notice to the Borrower:

<u>Group</u>	<u>Subgroup</u>	<u>Description of Items</u>
112	-	Alcoholic beverages
121	-	Tobacco, unmanufactured, tobacco refuse
122	-	Tobacco, manufactured (whether or not containing tobacco substitutes)
525	-	Radioactive and associated materials
667	-	Pearls, precious and semiprecious stones, unworked or worked
718	718.7	Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors

<u>Group</u>	<u>Subgroup</u>	<u>Description of Items</u>
728	728.43	Tobacco processing machinery
897	897.3	Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971	-	Gold, non-monetary (excluding gold ores and concentrates)

4. expenditures for goods intended for a military or paramilitary purpose or for luxury consumption;

5. expenditures for environmentally hazardous goods (for purposes of this paragraph the term "environmentally hazardous goods" means goods, the manufacture, use or import of which is prohibited under the laws of the Borrower or international agreements to which the Borrower is a party;

6. expenditures (a) in the territories of any country which is not a member of the Bank or for goods procured in, or services supplied from, such territories or (b) on account of any payment to persons or entities, or any import of goods, if such payment or import is prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and

7. expenditures under a contract in respect of which the Bank determines that corrupt or fraudulent practices were engaged in by representatives of the Borrower or of a beneficiary of the Loan during the procurement or execution of such contract, without the Borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation.

SCHEDULE 2

Amortization Schedule

1. The following table sets forth the Principal Payment Dates of the Loan and the percentage of the total principal amount of the Loan payable on each Principal Payment Date (Installment Share). If the proceeds of the Loan shall have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined by the Bank by multiplying: (a) the total principal amount of the Loan withdrawn and outstanding as of the first Principal Payment Date; by (b) the Installment Share for each Principal Payment Date, such repayment amount to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

Payment Date	Installment Share (Expressed as a %)
On each January 15 and July 15 Beginning January 15, 2012 through January 15, 2017	8.33%
On July 15, 2017	8.37%

2. If the proceeds of the Loan shall not have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined as follows:

(a) To the extent that any proceeds of the Loan shall have been withdrawn as of the first Principal Payment Date, the Borrower shall repay the amount withdrawn and outstanding as of such date in accordance with paragraph 1 of this Schedule.

(b) Any withdrawal made after the first Principal Payment Date shall be repaid on each Principal Payment Date falling after the date of such withdrawal in amounts determined by the Bank by multiplying the amount of each such withdrawal by a fraction, the numerator of which shall be the original Installment Share specified in the table in paragraph 1 of this Schedule for said Principal Payment Date (the Original Installment Share) and the denominator of which shall be the sum of all remaining Original Installment Shares for Principal Payment Dates falling on or after such date, such repayment amounts to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

3. (a) Withdrawals made within two calendar months prior to any Principal Payment Date shall, for the purposes solely of calculating the principal amounts payable on any Principal Payment Date, be treated as withdrawn and outstanding on the second Principal Payment Date following the date of withdrawal and shall be repayable on each Principal Payment Date commencing with the second Principal Payment Date following the date of withdrawal.

(b) Notwithstanding the provisions of sub-paragraph (a) of this paragraph 3, if at any time the Bank shall adopt a due date billing system under which invoices are issued on or after the respective Principal Payment Date, the provisions of such sub-paragraph shall no longer apply to any withdrawals made after the adoption of such billing system.

4. Notwithstanding the provisions of paragraphs 1 and 2 of this Schedule, upon a Currency Conversion of all or any portion of the withdrawn principal amount of the Loan to an Approved Currency, the amount so converted in said Approved Currency that shall be repayable on any Principal Payment Date occurring during the Conversion Period, shall be determined by the Bank by multiplying such amount in its currency of denomination immediately prior to said Conversion by either: (a) the exchange rate that reflects the amounts of principal in said Approved Currency payable by the Bank under the Currency Hedge Transaction relating to said Conversion; or (b) if the Bank so determines in accordance with the Conversion Guidelines, the exchange rate component of the Screen Rate.

5. If the principal amount of the Loan withdrawn and outstanding from time to time shall be denominated in more than one Loan Currency, the provisions of this Schedule shall apply separately to the amount denominated in each Loan Currency, so as to produce a separate amortization schedule for each such amount.

SCHEDULE 3

Actions Referred to in Recital (B) of the Preamble to this Agreement

- (1) With respect to the Borrower's 2002 budget approved by the Borrower's legislative branch and dated December 5, 2001 (Law No. 27573), at least 95% of amounts allocated to education, culture, health, sanitation and social assistance were executed and the allocations for said sector functions in the Borrower's 2003 budget approved by the Borrower's legislative branch and dated December 5, 2002 were established at levels higher than their 2002 executed amounts as adjusted in real terms.
- (2) With respect to the Borrower's 2002 budget approved by the Borrower's legislative branch and dated December 5, 2001, the total aggregate allocation for all PSPs was executed as planned and for each of said PSP, under performance did not exceed 50% of the initial allocation.
- (3) In the Borrower's 2004 budget submitted for approval to the Borrower's legislative branch on August 30, 2003, measures are proposed to prevent diversion of funds from the PSPs to civil service payrolls and benefits.
- (4) In 2002, *A Trabajar* was adequately targeted, an evaluation report on said program was carried out, publicly debated and published and a separate study on the impact of the wages paid under *A Trabajar Rural* was carried out.
- (5) The Borrower's law related to programmatic transfers of resources to sub-national governments establishing adequate rules for the decentralization of food programs was submitted to Borrower's legislative branch for its approval, and in the Borrower's 2004 budget submitted for approval to the Borrower's legislative branch on August 30, 2003 allocations are proposed to distribute the food-aid funding according to a pro-poor formula.
- (6) A Ministerial Resolution was approved and published in order to give DGAES responsibility over pension policy making.
- (7) The Borrower's legislative branch has approved and published two laws in order to create a pension assistance contribution and to improve the current *Cédula Viva* pension system.
- (8) During 2002, SIS exceeded target coverage agreed with the Bank and the Borrower's 2004 budget submitted for approval to the Borrower's legislative branch on August 30, 2003 prohibits the diversion of funds assigned to primary and secondary care in favor of higher complexity care.

- (9) The Borrower's administrative treatment of human resources in education has been substantially improved and covers 51% of teachers for the unified payroll system.
- (10) The Borrower is developing a hardship and merit incentives system through: (a) a pilot program currently under implementation with an agreed design structure and baseline in order to monitor and evaluate hardship and merit incentives for 1,000 rural teachers including detailed indicators; and (b) the first report of a study to design new merit incentives applicable to the education sector has been delivered.
- (11) The Borrower has carried out, presented and publicly discussed a report on a pilot system to assess users' satisfaction in relation to selected services of the PSPs and the Borrower's Law on transparency and access to public information, (*Ley* No 27806 dated April 24, 2003 as modified) and its related regulations were approved and published.
- (12) The Borrower has made SIAF available through an internet portal "*Consulta Amigable*" which provides information on the Borrower's budget for all public programs as well as data on actual spending and physical progress achieved for PRONAA, SIS and *A Trabajar Urbano*.
- (13) CGR and CONSUCODE issued oversight and supervision regulations concerning public procurement for mandatory use by all public agencies.