

PN-AN-153

80632-

FOOD PRICE POLICIES IN PERU

USAID/PERU

MAY 5, 1988
Lima, Perú

FOOD PRICE POLICIES IN PERU
EXECUTIVE SUMMARY

Food price policies in Peru traditionally have been biased in favor of consumers at the expense of producers. This bias has been reflected in suppressed and highly fluctuating producer prices of basic foodstuffs, combined with a long run trend (since the 1950's) of deteriorating domestic agricultural terms-of-trade vis-a-vis the rest of the economy.

These negative food price policies, combined with a poorly designed and implemented Agrarian Reform during 1970-75, created conditions in agricultural production and marketing of decapitalization, stagnation of productivity and depressed incomes. In early 1986, the Garcia Government, which was elected in mid-1985, responded to the severely depressed economic conditions of agriculture by approving an emergency Agricultural Reactivation Program (PRESA) that conceptualized and provided the framework for a radical departure from food price policies (FPP) of the previous three decades.

The essential purposes of PRESA were to shift terms-of-trade to make basic foodstuffs production profitable, and to increase their output and yields. Specific measures adopted were: For the short-run, a guaranteed producer price program and reduced input prices for basic foodstuffs production that would assure a profit to producers, for the longer run, a program to achieve producer foodstuffs price stabilization, food security, land tenure stability and an improved agricultural technology generation and transfer system. The Agricultural Reactivation and Food Security Fund (FRASA) was established in the State Food Marketing Enterprise (ENCI) to provide financial resources, first to implement short run measures, and, then, gradually to shift use of these resources toward accomplishment of longer run measures.

ENCI enjoys a monopoly for several basic foodstuffs. It receives import dollars for basic foodstuffs from the Central Reserve Bank at a highly subsidized exchange rate. FRASA financial resources have been generated, in part, from the difference in the Intis import price and the Intis price at which ENCI sells to wholesalers. The ENCI sales price includes a mark-up fee of 40% or more over the CIF price, plus transaction costs. On commercial imports/sales, ENCI profits generated approximately \$60 million for FRASA in 1987. In 1987, ENCI failed to deposit about 30% of the net sales proceeds from the 1986 PL-480 agreement in the Special Account, and used them for FRASA purchases. Neither the GOP Treasury nor the USAID have agreed to this use, and the Treasury, with AID support, is continuing to seek deposit of these funds in the Special Account. The balance of resources required to finance the program (approximately \$63 million in 1987) were provided from the public treasury.

In concept and framework, Peru's FPP is generally compatible with AID policy. Conceptually, it is intended 1) to avoid suppressing producer prices, 2) to provide incentives to producers consistent with comparative advantage, food demand and food security, and 3) to achieve producer price stability and income growth while increasing food production. It also has as its major long run objective improved agricultural resource use efficiency and increased food output. Peru's FPP also includes important complementary efforts to organize a more effective means of targeting food subsidy programs to poor populations.

Implementation of producer food price policy aspects of FRASA appears to be evolving in a manner consistent, in part, with AID policy. Support prices are moving closer to estimated long run international prices CIF at a parity exchange rate, and an attempt is being made to keep them stable in real terms in a highly inflationary situation. There is recognition that, in the longer run reliance must be placed on improved productivity to assure continuing producer profitability and farm capitalization. However, more needs to be done in setting relative prices for the guaranteed crops to reflect comparative advantage in the various regions, and in coordinating implied subsidies with other agricultural subsidies. how?

In contrast, consumer price subsidies for basic foodstuffs (especially rice) have become an unsustainable cost burden. As domestic inflation (and loss of value of the Inti against the US Dollar) has spiralled virtually out of control in recent months, the GOP appears to be politically incapable of making required consumer foodstuffs price and import exchange rate adjustments. Wheat is being sold at a price less than half that justified by the long run CIF import price at a parity exchange rate, and rice at only slightly more than half the reference price. This has resulted in continued heavy deficit financing by the GOP which further fuels inflation. Low consumer prices for wheat products and rice have a heavy unfavorable effect on demand for substitute products, such as potatoes and other tubers, through cross elasticity of demand effects. This leads to unnecessary use of scarce foreign exchange for imports and a loss of income to domestic producers of substitute products.

If significant (and politically difficult) consumer food price subsidy changes are not forthcoming quite soon, that subsidy will exceed \$100 million in 1988. Exchange losses to the Central Bank for wheat imports at the subsidized exchange rate will approach the same order of magnitude. Together these will total almost one percent of GDP. However, analyses and discussions in government quarters are focussed on this issue (e.g., Ministry of Agriculture, National Planning Institute, Ministry of Economy and Finance, and Central Reserve Bank). There are encouraging signs that the GOP is positioning itself to make at least some of the needed consumer price adjustments. However, for this to result in a coherent policy for consumer prices in the future, a better adjustment mechanism for price changes is required. ?

Given the current appropriate trends in producer price food policies, and signs of imminent corrective adjustments in consumer food price subsidy levels, it is quite important that USAID sustain, and do all possible to enhance, its policy dialogue position and possibilities with the GOP. Our past record in agricultural policy impact is good, especially through our Agricultural Planning and Institutional Development (APIID) Project. It would not be prudent to eliminate (or endanger or weaken) this positive role. Taking an a priori stand against any use of PL-480 resources for FRASA would be an unwise move, both technically and politically, and would not be consistent with USG policy of "constructive engagement".

USAID proposes that our negotiating position for the 1988 PL-480 self-help measures address critical current FPP issues through studies, development of programs responsive to FPP needs, and assistance in efforts to improve targeting of food subsidy programs to poor populations. Specific proposed self-help measures are detailed in the last section of this report.

FOOD PRICE POLICIES IN PERU
TABLE OF CONTENTS

	PAGE
A. Background	1
B. Evolution of García Administration Food Price Policy	2
C. How FRASA Operates	5
D. Complementary Programs	5
1. State Food Marketing Program	6
2. Agricultural Technology Generation and Transfer	6
E. Compatibility of Peru's FPP with AID Policy	6
1. Avoid suppressing producer prices and rely on market mechanisms for price formation	7
2. AID perspectives of desired objectives for FPP	7
3. Producer Price Policies	8
4. Other Aspects of Compatibility	8
F. Implementation of FPP and FRASA	11
G. <u>Estimates of the Economic Efficiency of Food Price Subsidies in Peru</u>	13
H. Impacts of FRASA	15
I. GOP Views of FRASA	16
J. Mission Conclusions about FRASA	17
1. Perspective	17
2. Policy Dialogue Agenda	17
3. Dialogue Difficulties	18
4. Negotiating Position Vis-a-Vis PL-480 and FRASA	18
5. Implications for Self-Help Measures	19

FOOD PRICE POLICIES IN PERU

A. BACKGROUND

Historically, consumer-oriented food price policies in Peru have resulted in suppression and instability of producer prices. This result has been reflected for many years in the unfavorable terms of trade of the agricultural sector with the rest of the economy.^{1/} From 1950 to 1985, terms of trade have shown an inexorable trend in favor of urban populations as compared to rural populations. In addition, especially since 1970, producer prices suffered wide fluctuations around the mean with cycles of 6 to 8 years.

Measured as a ratio of the domestic agricultural wholesale price index (DAPI) over the general wholesale price index (GWPI), terms of trade for agriculture have deteriorated to the point that in 1985, income from the sale of a kilogram of harvested agricultural product purchased for the farmer only 50% as much as it would have purchased in 1950.^{2/} This trend would not be of such serious concern if agricultural productivity had been increasing sufficiently during the period to offset the reduced income effects of less favorable terms of trade. Unfortunately, such has not been the case.

During the 1950's and 1960's, agricultural productivity increases, primarily in major export crops, were able to largely offset agricultural income losses caused by deteriorating terms of trade.^{3/} However, this improving productivity trend ceased abruptly beginning in the early 1970's.

During 1970-75, agriculture suffered a dramatic loss of technical and managerial capability, while agricultural investment plunged and large scale decapitalization took place. These phenomena were highly correlated to the massive agrarian reform carried out during that period by the Velasco Military Regime, combined with suppression of prices for domestically produced and consumed foodstuffs through far-reaching state intervention in food price formation and marketing. During this period, agricultural productivity gains of the 1950's and 1960's were lost. Furthermore, after 1975, prices for most of Peru's major agricultural exports dropped sharply, adding to agriculture's woes.

The net effect of these conditions halted productivity improvement, destroyed farm profitability and resulted in continued deterioration and decapitalization of commercial agriculture. During the last half of the decade of the 1970's, there was wide-spread abandonment (or conversion to subsistence agriculture) of agricultural lands previously in commercial production. Average annual agricultural Gross Domestic product (GDP) growth

^{1/} Ratio of prices received by farmers for what they sell over prices paid by farmers for what they buy. See Chart D in Appendix A.

^{2/} Webb, Richard, "Una Formula Poderosa", *Caretas*, Jan. 26, 1987, p.16.

^{3/} Small farm/subsistence agriculture, especially in the Sierra where much of domestically consumed foodstuffs are produced, shared little in these productivity increases.

in the 1970's was less than 1.0% 1/ while population grew at 2.7% annually. 2/

In 1978, the Morales Bermudez Military Government began to introduce more open foodstuffs pricing and marketing policies, and took measures to stabilize landownership. This trend toward more rational agricultural policies was continued and intensified by the Belaunde Government that took office in mid-1980. Both terms of trade and productivity in agriculture began to improve. Agricultural GDP jumped by 12% in 1981. This improved economic outlook for commercial agriculture was reflected in the fact that, by 1982, the amount of crop land in production had returned to the levels of the 1960's.

Unfortunately, inflationary pressures in 1982 caused the GOP to permit heavy foodstuffs imports at depressed international prices. This resulted in a new trend toward suppressed producer prices and a consequent downturn in agricultural terms of trade. The buoyancy of agricultural output growth was dampened (agricultural GDP grew by 2.9% in 1982). This reversal of the earlier favorable trend in agricultural terms of trade, combined with severely negative climatic conditions, caused agricultural GDP to drop more than 9% in 1983. Despite a continuing unfavorable trend in terms of trade in 1984, unusually good climatic conditions contributed to a rebound that increased agricultural GDP by 12.5% as compared to 1983 (a net increase of 2.5% from 1982). The overall 1981-84 average annual rate of growth in agricultural GDP was approximately 4.0% despite the severe climatic setback in 1983.

Policy paralysis during the last year of the Belaunde Government (mid-1984 to mid-1985) resulted in an accelerated rate of deterioration in agricultural terms of trade and sharply increased inflation. Thus, by 1985, negative economic conditions effectively halted the agricultural growth cycle that had been sustained since 1981.

B. EVOLUTION OF GARCIA ADMINISTRATION FOOD PRICE POLICY

When the García administration took office in July, 1985 it was faced with 1) a rapidly increasing rate of inflation (approaching 100% per year in June, 1985, compared with 80% a year earlier, 2) continuation of deterioration of agricultural terms of trade (the DAPI/GWPI ratio of .72 in 1985 was the lowest since 1950, and, 3) prospects for little or no agricultural growth in 1985/86.

Upon taking office, the Garcia administration applied an across-the-board price freeze "shock treatment" to counteract the inflationary spiral. The price freeze also froze in place the highly unfavorable terms of trade for agriculture. Thus, it was not surprising that 1985 third quarter agricultural GDP figures showed a continuing drop in output. In recognition of the problem, the government exempted most food perishables prices from the freeze

1/ Agricultural GDP growth rates are shown in Table II in the Appendix A.

2/ The deterioration of incentives to agriculture is confirmed by a study completed by the International Food Policy Research Institute in 1987 on Trade and Exchange Rate Policies in Peru and other Countries (Reported in their 1987 Annual Report, PP 54, 55).

and instituted various regulatory/controls regimes for most foodstuffs that permitted periodic adjustment to reflect supply conditions.

When end of year 1985 GDP estimates indicated a fourth quarter negative growth rate for agriculture, the Minister of Agriculture was changed. In taking stock of the agricultural situation and designing an emergency agricultural reactivation program, the new Minister (Remigio Morales Bermudez) relied on analytical work that had been carried out by GAPA 1/ during the previous two years.

GAPA analyses showed that the relatively high 1981-84 agricultural growth trend had rapidly evaporated in 1985, provoked in large part by greatly deteriorated terms of trade and the continuing decapitalized state of the agricultural sector. GAPA predicted a 3.0% contraction in 1986 agricultural GDP in the absence of far-reaching measures to reactivate the sector. Based on these and other GAPA analyses and alternative options, the Minister proposed (and the Garcia Cabinet adopted in February, 1986) an emergency Agricultural Reactivation Program (PRESA) that represented a major departure from food price policies of the past three decades.

The major objectives of PRESA were 1) to shift terms of trade to favor agricultural producers and to assure a profit from farming in the short as well as long term, and 2) to increase basic foodstuffs output and yields in order to provide basic food security by assuring a constant supply of domestically produced foodstuffs to consumers at stable prices.

The major instrumentation for achieving these objectives in the short run was to guarantee to producers profitable prices for major basic foodstuffs production and to reduce the cost of key inputs for increasing yields (especially fertilizer, pesticides and machinery, as well as credit). Complementary areas of attention were land tenure stabilization and improvement of the agricultural technology generation and transfer (ATG&T) system.

The Agricultural Reactivation and Food Security Fund (FRASA) was established as the vehicle by which guaranteed producer prices and lower fertilizer prices would be implemented. FRASA was to be financed by a surcharge on depressed price food imports (primarily wheat and corn).

Reliance on FRASA to reactivate agriculture and provide food security was clearly put forward as an emergency measure. It was recognized that, in the longer run, currently depressed international prices of major foodstuffs imports would increase significantly, thereby reducing surcharge income to FRASA. It was further recognized that technological change which reduces unit costs of production would be the only sustainable source of profitability and capitalization of agriculture in the longer run, but that this could occur only in an environment of unsuppressed and stable producer prices.

1/ GAPA (Agricultural Policy Analysis Group) was established in late 1983 under the AID supported Agricultural Planning and Institutional Development (APID) Project.

The rationale for FRASA was:

In the short to medium term, FRASA would be used to provide higher output prices and cheaper inputs for foodstuffs production. This is expected to increase productivity and output. In the medium term, increased capitalization from profitable production (combined with tenure restructuring and ownership stabilization) are expected to result in continued increases in productivity and output. In the medium to long term, continued improvements in the ATG&T system, combined with improved water use policies, increased emphasis on Andean agriculture and on livestock development, improvements in the marketing system and improved production planning, will be the focus by the GOP to achieve continued increases in productivity and output, thereby eliminating the price support role of FRASA and converting its purpose to price stabilization and food security.

Guidelines for implementing food price policy (FPP) through FRASA were specified in the implementing Decree as follows:

1) Use to stimulate domestic agricultural production. Consumer food subsidies and cheap food imports should not be allowed to interfere with this stimulation.

2) Prices paid to producers must be sufficient to encourage farm enterprise capitalization, thus the need for adequate profitability and stabilization of prices. Landownership stabilization is a complementary policy area requiring action.

3) Producers must be participants in the agricultural policy-making and development program design process, including determination of costs-of-production upon which guaranteed prices would be based.

4) Food imports must be managed so as not to dampen domestic supply response where comparative advantage exists, i.e., imports should be used only to fill short-term supply gaps and assure food security in the short run.

5) Supply-demand relationships must be honored in setting guaranteed prices and in food import management.

6) The concepts of relative prices and comparative advantage will be applied in fixing guaranteed prices.

Guaranteed prices for selected major foodstuffs were to be pre-announced (prior to planting) and set at a level to permit profits to producers of average efficiency. Thus, guaranteed prices were to provide income from 20% to 40% above all costs-of-production. Products with guaranteed prices include: Rice, corn (yellow, white & amilaceo), wheat/barley, quinua/kiwicha, dry pulses (13 types), powdered whole milk, dry peas and selected dried/processed food products (banana chips, yuca chips and potatoes).

Wheat,
Corn
P. 480?
??

FRASA funds also were to be used to pay fertilizer subsidies and to subsidize wholesale and/or consumer prices.

C. HOW FRASA OPERATES

FRASA is a fund used to pay the costs of the PRESA program. ENCI, the State Marketing Company, administers FRASA. ENCI also is the exclusive importer of basic food and feed stuffs. FRASA receives net resources remaining from the sale of imported foodstuffs at wholesale, after paying FAS import costs (with foreign exchange acquired from the Central Bank at a highly favorable exchange rate), and other import and transaction costs.^{1/} These other import and transaction costs include ocean freight and insurance and, in 1986/87, were an estimated 11% of the FAS cost.

Guaranteed producer prices (as well as consumer prices for the same products) are set by an Interministerial Price Commission (IPC) based on cost-of-production estimates agreed to between the Ministry of Agriculture and producer groups. Except for rice, ENCI is the buyer and is charged with buying at the established price all of the guaranteed price products offered by producers. In practice, ENCI buys virtually all Selva produced yellow corn, but less than 10% of other guaranteed price crops, while ECASA buys all rice, using FRASA resources. In terms of magnitudes of financial producer subsidy, the only products of significance are rice, and yellow corn produced in the Selva.

In the case of powdered whole milk, ENCI purchases from national processors based on cost-of-production (which is above the imported price). ENCI also is the exclusive importer of powdered whole milk. ENCI then packages for retail use, and sells wholesale at a subsidized price (both national production and imports are subsidized). This subsidy is paid from FRASA.

FRASA funds also are used to cover any deficit that ENCI incurs in buying/importing fertilizer (primarily urea) and selling it at a discounted price.

D. COMPLEMENTARY PROGRAMS

In recognition of the emergency nature of the guaranteed producer price program under FRASA, the GOP is attempting to consolidate and improve the organization of its 1) state food marketing program, to better target poor

^{1/} A 40% (of CIF cost) fee (called "Tasa CIF") is deducted and paid into FRASA at the time of sale in Peru. The remaining "net proceeds" after paying all costs is profit on which ENCI normally would pay taxes (with the balance being turned over to its parent company - CONADE). These "net proceeds" are in fact also paid into FRASA through a sort of "forgiveness mechanism". The highest 1987 Dollar exchange rate for basic foodstuffs imports was I/.15.93, whereas the average parity exchange rate for the year was almost double that amount (I/.29.00).

populations as an alternative to generalized consumer subsidies, and 2) agricultural technology generation and transfer (ATG&T) program, to encourage output unit cost reductions thereby permitting food prices to fall in real terms without destroying producer profitability. Since these programs are critical to the GOP's longer run food price policy and food security strategy, they are briefly described below.

1. State Food Marketing Program:

Enabling legislation was approved in June, 1987 to establish a state - owned enterprise called CONAA (National Food Assistance Corporation). In January 1988, organization statutes were approved and CONAA began functioning. CONAA consolidates the following previously existing state-owned enterprises: The Central Wholesale Market Enterprise (EMMSA), the Livestock Products Marketing Enterprise (EMCOPESA), the Rice Marketing Enterprise (ECASA), and the assets of Pro-Compra, the latter having been organized into a state enterprise called "Peoples Markets, Inc" (Mercados Pueblos, S.A.). Pro-compra is a complex of rural assembly structures located through-out the country, a large wholesale warehouse facility in Lima, and a number of retail structures in Lima and other major cities. These were constructed under an US\$80 million Spanish financed project, initiated in the early 1980's and which utilized turn-key metal structures imported from Spain. These structures had not yet been made operational by 1986. The GOP intends to utilize these facilities and others, organized under Mercados Pueblos, S.A., as outlets for distributing key basic foodstuffs in poor areas. 18 outlets already are operating in the Lima area, 12 in other cities, and 100 are expected to be in operation by the end of 1988.

2. Agricultural Technology Generation and Transfer:

In September, 1987, the GOP signed a six year Grant Agreement (the Agricultural Technology Transformation - ATT - Project) with AID to assist in improving and expanding public and private sector capabilities in generating and transferring agricultural technology. The GOP is providing 52% of total resources to the ATT Project as counterpart, in addition to continuing to provide regular budget resources to public research and extension through INIAA and MinAg.

E. Compatibility of Peru's FPP with AID Policy. 1/

In many respects, the concepts and framework of Peru's FPP are compatible with AID guidelines for food price and subsidy policies. There are compatibility issues with regard to implementation, especially during 1987, of these policies, as discussed in the next section. This section highlights some of the more significant compatibilities between AID guidelines and Peru's FPP concepts and framework.

1/ References in this section are to the AID Policy Paper on "Pricing, Subsidies and Related Policies in Food and Agriculture", AID/PPC, Nov., 1982.

1. Avoid suppressing producer prices and rely on market mechanisms for price formation (P, i)

AID policy is to support food distribution programs that (among other things) do not rely on suppression of producer prices and do not regulate food prices or the bulk of the private food market, but instead use market mechanisms, so far as possible.

Current Peruvian FPP, for the first time in at least two decades, has established a food price stabilization program that does not rely on suppression of producer prices. Although current general price policies also regulate a number of foodstuffs prices in the private food market, this is done as part of an across-the-board mechanism to control inflation. Such price regulation applies to virtually all products at the wholesale and retail levels. In other words, foodstuffs are not singled out for regulation. In fact, a number of food products are not regulated (e.g., most perishables). Rice is marketed through a state monopoly, but rice has been subject to a state marketing monopoly for the past half century. Thus, current treatment of rice is not a "negative change" in FPP.

but we should negotiate positive change

The GOP incorporates market mechanisms into producer price formation by a process called "concertacion", i.e., participation by producers in determining producer prices and volume targets. The "concertacion" system works somewhat like a system of "marketing orders". Producers indicate an anticipated production response for selected products at a pre-agreed price. This process is carried out in "concertacion" between producers and the government, with the government representing interests of consumers and society as a whole. ENCI then is charged with purchasing any guaranteed price products offered at the pre-agreed level. All rice, as already indicated, is purchased by ECASA.

impact of off market grain price on domestic production

2. AID Perspective of desired Objectives for FPP (PP 3 and 4).

market determined

a. Provide incentives to domestic producers consistent with comparative advantage, food demand, and food security. As described in an earlier section, all of these factors are incorporated into the implementing principles of FRASA.

also - in operation this apparently doesn't happen.

b. Alleviate undernourishment, especially of vulnerable groups. The GOP specifically has targeted programs for school children, gestating and lactating mothers, as well as the more recent effort to provide "fair price" food outlets in poor areas. Although state owned "fair price" stores may not be the most efficient solution, it is an obvious effort to have in place a mechanism to protect the nutrition of poor populations when the inevitable happens (i.e., when the GOP no longer can pay current consumer subsidies). In the absence of USAID or other donor support for preferred alternatives, the "fair price" outlets likely will continue to be the GOP method of providing basic foodstuffs to poor populations.

c. Distribute food at minimum cost largely in conformity with supply and demand. Rice aside, the private food marketing system markets more than 90% of domestically produced foodstuffs. In the case of food imports, interestingly enough, even though state food import monopolies were removed in 1980, most imported food and feed grain users continued to use ENCI as their import agent. At least for wheat and yellow corn, the re-imposition of an import monopoly to ENCI simply made mandatory what previously had been happening in practice.

probably because ENCI was subsidized and private sector could not compete

3. Producer Price Policies (P.5)

Peruvian FPP seeks to stabilize prices and achieve food security in a way that results in sustained production and income growth in the sector. This is consistent with AID's basic goals of increased food production and increased farm income. By the same token, as previously stated, for the first time in two decades, Peruvian FPP does not put the burden of financing consumer subsidies on the farmer. Thus, in this aspect, Peruvian FPP appears to be consistent with AID's basic goals, if properly implemented.

4. Other Aspects of Compatibility

a. Consistency with AID's Basic Goals (P.6)

basic goals perhaps - in short term - but it won't do this in long term

Again, except for rice and Selva corn, the FRASA program is a system of limited government purchases at pre-announced support prices, designed 1) to confine price variations within a narrower range than would otherwise apply (as is the case for pulses, white and amilaceo corn and dry peas), and, 2) in some cases, to raise the average price in the short/medium term (e.g., Selva corn, quinoa and wheat). This is acceptable FPP within AID's basic goals, and may make economic sense especially where tradeable products are concerned.

A recent GAPA review found that the FRASA program actually resulted in reduced direct food subsidies (both in gross and net terms 1/) in 1986 as compared to the five year period of 1979-1983. During the 1979-83 period, average annual net subsidy cost was \$188 million, whereas no net food price subsidies were paid in 1986. Instead, purchases and sales operations for major foodstuffs by ENCI/ECASA provided net returns in excess of \$16.0 million. This excess was used to finance fertilizer subsidies and guaranteed price purchases by ENCI of minor food crops. In contrast, net subsidies in 1984 and 1985 were \$36 million and \$26.5 million, respectively. Nevertheless, the indirect subsidy (through a lower than market exchange rate provided by the Central Bank to ENCI to make these purchases) in 1986 more than cancels out the \$16.0 million FRASA surplus. Furthermore, the level of both direct

1987?

right

1/"Gross" refers to the total cost to ENCI of the subsidy, "net" refers to the difference between the total subsidy cost and the offset available from profitable commercial sales of imported foodstuffs by ENCI.

what did you lose from

subsidies

and indirect subsidies increased substantially in 1987 as the result of failure of the GOP to adjust consumer prices (especially for rice) to keep pace with inflation. It should be noted, however, that these are consumer and not producer subsidies, as explained in the next section.

b. Impact on Export Crop Production (P.6)

but have the effect of providing disincentives to domestic tuber production

It does not appear that FRASA has resulted in increased food production at the expense of export crops. Although there was substitution of cotton acreage by corn in 1986, it appears that the reasons were not primarily corn price motivated. Rather, increased costs of production and reduced yields of cotton caused by the recent arrival in Peru of the "Pink India Cotton Worm", combined with low internal and export prices appear to have caused the shift. Additionally, there are indications that some coastal farmers are beginning to use their profits from guaranteed price crops to invest in intensive production for export of fruits and vegetables.

c. Impact on efficiency/productivity (P.1)

Guaranteed producer prices are required by the implementing Decree to be fixed considering comparative advantage, although implementation does not appear to have considered this adequately. Also, the guaranteed price program is complemented by productivity enhancing programs. Thus, FRASA is not expected to result in decreased efficiency or productivity. On the contrary, as the use of FRASA shifts toward price stabilization objectives, it will provide incentives for improving resource use efficiency. Furthermore, the FRASA program does not appear to have caused significant production shifts (except temporarily as in the case of cotton in 1986, which suffered from unusually low prices and high production costs), but rather seems to have encouraged temporarily idle land to be brought back into production.

but you said it is?

this may exactly be the problem... govt do not do a good job of balancing all factors

d. FRASA in the Context of Overall Policy Dialogue and Project Assistance (P.1)

We re-emphasize that the original concept of the FRASA Guaranteed Producer Price Program is that it is a short/medium term stimulus being provided as one element of an overall strategy to achieve sustained price stability, rational agricultural development and food security. Mission efforts to influence changes in relative emphasis on the FRASA mechanism is taking place within the framework of our overall dialogue with the Peruvian GOP on both macro and agricultural policy matters.

There is a high degree of harmony between AID and the GOP on agricultural goals and objectives. To stonewall on the use of some PL-480 resources for FRASA would shift discussions on this matter from the technical to the political arena. It makes both technical and political sense to deal with our reservations about FRASA in the context of our overall policy dialogue.

USAID also is providing under our APID and our REE projects technical assistance and training to strengthen capacities of both the public and private sectors to analyze effects of existing and alternative policies regarding pricing and distribution related to food and agriculture. Through these efforts and our policy dialogue, we are encouraging the GOP to modify and reduce government intervention in price formation and distribution systems. However, the feasible degree of policy change along these lines at this particular point in time is constrained by a combination of severe inflationary pressures, political instability and the relative strength of the political left. These all are extremely important factors to be orchestrated in a way that preserves and strengthens the fragile democracy that currently exists.

*results
of AID
are not
encouraging*

*short
it has
increased*

AID should be especially understanding and circumspect about certain aberrations in what otherwise is, by and large a rational economic and agricultural development strategy and accompanying policies. Aberrations that are the result of a need to accommodate the political left in order to preserve the democratic process, and those that are the result of naive thinking but that can be sustained only temporarily, hopefully can be corrected in time so as not to destroy prospects for fairly rapid economic recuperation.

resources are being wasted on an uncooperative system - Would AID prolong that again?

Pushing too hard and inflexibly at this time of questionable individual elements of food price policy most likely would jeopardize AID's ability to continue to engage in meaningful policy dialogue. Downward adjustments in the relative levels of guaranteed producer prices already are taking place, leading us to be cautiously optimistic that the government fully intends for producer subsidies to be temporary. In the near future, we expect that the objective of FRASA in terms of producer prices will settle on price stabilization and food security. At the same time, we recognize the continuing food price policy issue of high general consumer food subsidies and the more general policy issue of administered pricing. Nevertheless, it is encouraging that there is considerable concern and debate about these issues in a number of government quarters (GAPA in MinAg., National Planning Institute, and the Office of Economic Affairs in Ministry of Economics and Finance).

Our approach should be to encourage intensification of analyses and discussions that lead to interim policy actions tending to achieve longer term goals of more competitive price formation and markets, and targeted food programs to alleviate the nutritional impact on poor populations of necessary consumer price adjustments. Before taking a drastic course of action, AID must consider whether cutting off the use of PL-480 related resources to FRASA will seriously damage our ability to influence, or eliminate entirely our ability to dialogue about FPP.

GAPA is an especially important influence in achieving a change to more rational consumer subsidy policies. The GAPA approach is analytical and the orientation clearly is producer price stabilization, food security and minimizing general consumer subsidies while targeting food assistance to poor populations, based on domestic production.

A recent evaluation of the APID Project identified an impressive number of specific instances where GAPA analysis and advice have positively influenced policy decisions. One of the most effective ways for us to influence appropriate food price policy decisions (as well as others) is to continue and strengthen our support to GAPA.

USAID had included in its last CDSS, and had hoped to include in the recently completed CDSS, a project of assistance to domestic food marketing in order to gain additional leverage and rationale for FPP dialogue in this area. However, severe budget cuts in our development assistance program have forced the Mission to drop domestic marketing improvement from its strategy and program.

e. Nutrition Improvement Programs (P.2)

Mission assistance to nutrition programs supports private voluntary organizations and government programs designed to reduce severe undernourishment in young children and gestating/lactating mothers. With additional appropriate resources, Mission would consider providing assistance to encourage a re-orientation of the new initiative of the GOP in the "Mercados Pueblos" fair price outlets toward targeting food distribution to poor people through the private distribution system.

F. Implementation of FPP and FRASA

Peru continues to rely on virtually across-the-board administered pricing as the principal inflation-fighting strategy. Except for food perishables, consumer prices of foodstuffs are subject to this administered pricing mechanism. However, Peru's FPP as such and the role of FRASA appear to be conceptually sound in many aspects.

Peru's record in implementation of FPP and FRASA is spotty. This appears to be largely the result of inability to resolve differing views within the governing (APRISTA) party, the perceived need by the President to retain popular support at all costs economically, because in his view the alternative is to permit intolerable political gains by leftist groups, and the overall lack of governing experience and technical capability of GOP leadership.

Major weaknesses, becoming especially pronounced in 1987, have been 1) failure to make upward adjustments in domestic wholesale (and retail) prices, especially of rice and wheat, in order to keep pace with inflation, and 2) failure to increase the basic food import exchange rate to keep pace with changes in the parity exchange rate, thereby creating an unsustainable drain on foreign exchange while increasing inorganic emissions of Intis to purchase foreign exchange. To illustrate the above, the wholesale price of rice changed from I/. 3.20/kg. in February, 1986, to I/. 8.20/kg. in March, 1988, a

change of 156%, whereas inflation increased by 170%. By the same token, the basic foodstuffs import exchange rate was I/.13.98 in February, 1986, and was I/. 15.93 in March, 1988, a change of 14%, whereas the parity exchange rate for the same period changed from I/. 14.92 to I/. 67.00 (a change of 349%).

There are positive features to the GOP implementation record for FPP and FRASA. For the producer price guarantee program, there is a clear trend toward a focus on price stabilization and food security, in contrast to price support, per se.

For example, in the case of rice (see Table I and Chart A in Appendix A), international rice prices (FOB Bangkok) were higher than domestic producer prices at the parity exchange rate in every year since 1970, except for 1970-72 and for 1986 and 1987. Chart A also shows the median international price for rice as a suggested "reference price" for domestic rice prices paid to producers. As can be seen, domestic producer rice prices consistently have remained considerably below the reference price except for 1986 and 1987. In other words, producer prices were suppressed below the international price through consumer-oriented price policies for 13 years out of 18 from 1970 through 1987. Further, of the 18 years of data shown, only in two years (1986 and 1987) did domestic producer prices exceed the reference price.

Charts B and C (and Table I) in Appendix A show similar plots of data for yellow corn and wheat. As can be seen, yellow corn prices rose substantially above the reference price as well as the international price beginning in 1986, after 7 years of being below the international price. The corn price for May, 1988 brings the guaranteed producer price back much closer to the reference price. In defense of the decision to set a high guaranteed producer price in 1986 and 1987, it was intended to offset the depressing effects of the extremely low producer prices received from 1979 to 1985 as compared to international prices (or to reference prices from 1981 to 1985).

In the case of wheat, prices during 1985, 1986 and 1987, were set at levels significantly above international as well as reference prices, although the May, 1988 price comes much closer to the reference price. Again, higher prices in 1986 and 1987 were intended to partially offset the negative effects of low producer prices from 1981 through 1984. It also was intended as a special stimulus in the short run to take advantage of successful wheat breeding work carried out during the past ten years. This work has made available considerably improved seed for the Sierra, the traditional area of wheat production, as well as for introduction into coastal and high jungle areas. This year, wheat has been seeded in significant amounts for the first time in the high jungle area of Jaen-Bagua, and prospects for expanded wheat production in the Central Sierra resulted in the recent construction of a privately owned flour mill in the Mantaro Valley.

Beginning in 1987, FRASA gradually has been converted from a producer price support fund to a producer price stabilization fund and to a consumer price subsidy fund. The latter role absorbs the majority of FRASA resources.

In 1987, total price subsidies for domestic production of the three major basic foodstuffs (rice, corn and wheat) were approximately \$95 million (before offsetting with earnings from foodstuffs import operations), of which an estimated 42% (\$40 million) were producer subsidies and 58% (\$55 million) consumer subsidies. Projections for 1988 indicate that rice producers will receive no price subsidies but rather will be subject to an implied tax of \$13 million, and corn and wheat producers will receive \$3.2 million and \$0.7 million, respectively. In contrast, without major consumer price adjustments, consumer subsidies will exceed \$107 million (See Tables IV, V and VI in Appendix A).

G. Estimates of the Economic Efficiency of Food Price Subsidies in Peru

The economic efficiency of a commodity's price system can be estimated by comparing the levels of existing producer and wholesale prices against its "social price". For purposes of this estimate, the social price has been defined as the domestic price equivalent of the long run international price (CIF) ^{1/} of the commodity converted to local currency using the "shadow" or "parity" exchange rate. Thus, the social price is based on an estimate of the average price that would prevail internally in the absence of restrictions on international trade and the exchange rate, i.e., free trade conditions. Deviations from the social price provide a measurement of subsidies/taxes imposed on the production and/or consumption of the commodity.

Producer price deviations from the social price may be justified to achieve national policy objectives such as food security, producer price stabilization, and, in the long run, foreign exchange savings. Consumer price deviations from this social price also may be justified as a means of achieving other policy objectives (e.g., lower food prices to consumers, improved nutrition among poor populations). How much deviation is justified and how the subsidy is targeted in each case (producer price subsidy/tax, consumer price subsidy/tax), are, in part, judgment calls related to questions of socially acceptable losses in economic efficiency and how much cost burden the economy can "afford" in social terms.

Table VII (in Appendix A) shows the principal features of the Peruvian price structure for rice, corn, and wheat--the principal food crops subsidized by FRASA. The combined annualized value of producer price subsidies for the three crops is about \$51 million, the corresponding value for consumer subsidies is about \$71 million. Individually, wheat is the least costly of the producer subsidies (\$1 million), but the most costly of the consumer subsidies (about \$93 million). Rice subsidies also heavily favor consumers (about \$51 million), as compared to producers (about \$8 million). Corn prices provide a substantial subsidy to producers (\$42 million) and a significant tax on consumers (\$95 million), mostly in the form of higher poultry and pork prices.

^{1/} This price may reflect longer run exporting countries' subsidies, and thus is not a pure "free trade" price, but can serve as a proxy.

An overall review and analysis of the magnitudes of subsidies involved raises several questions about the efficiency of the current price structure. Whereas rice producer price subsidies neither represent a gross distortion in relation to its social price (only 4% higher), nor a heavy cost to society (\$7.6 million), the corresponding consumer subsidy does not appear to be justified, especially since it is distributed almost indiscriminately among consumers of different income classes. Further, consumer price differentials according to quality are relatively small. This (and the low absolute consumer price) also encourages the substitution of traditional crops, e.g., potatoes, cassava, sweet potatoes and even pulses, for inexpensive rice.

In the case of wheat, although the producer price is relatively high in relation to its social price (35% higher), its overall cost to society is relatively quite small (\$1.0 million), since so little domestic wheat finds its way into commercial channels (for flour milling). As in the case of rice, the consumer subsidy on wheat appears to be excessive since its distribution also is essentially indiscriminate among the entire population. As in the case of rice, inexpensive imported wheat may encourage greater consumption of wheat at the expense of traditional crops. The consumer tax on corn, on the other hand, appears to be more justified because corn is primarily used as poultry and hog feed, an important but not necessarily an essential component of the Peruvian diet. The producer price subsidy, however, may be excessive in relation to the production response that it appears to elicit. Use of resources in technology improvement in corn production, as well as in more efficient use of water and land in corn production, appears to have the potential to achieve much greater output responses.

The brief analysis summarized above clearly provides only initial impressions about overall efficiency of current producer and consumer price structures. A complete assessment will require further and detailed analyses on each crop. Areas of analysis should include efficiency of mechanisms used to distribute price subsidies/taxes, the combined effect of price and other subsidies and taxes on producers and consumers, and the cross-substitution effects of consumer subsidies on other crops.

In 1987, about 63% of FRASA's funds (excluding working capital) were provided by the public treasury (including PL-480 resources). Thus, taxpayers are helping to support a substantial portion of consumer price subsidies. To the extent that taxpayers represent a relatively well-off segment of the population, this financing mechanism appears "fair".

The other 37% of FRASA costs are being financed through profits made by ENCI and ECASA on the import of commodities at lower than export exchange rates. On the surface it makes sense for these institutions to earn profits on such imports. However, the profit margins are made possible by an implicit Central Reserve Bank subsidy--the bank sells dollars low to ENCI but buys them at much higher prices from exporters or in the street market. This implicit subsidy is contributing to a monetary expansion that, in turn, contributes to the current high inflation rate. Of course, the impact of direct consumer subsidies (via price controls) may be partially offsetting the high inflation which some of FRASA's financing mechanism is inadvertently helping to foster.

Some decision-makers and key technical staff in the GOP are acutely aware of the consumer price subsidy problem and are looking for ways to ease out of it without jeopardizing either relative domestic price stability or FRASA's finances. The effort will require continuing analysis and a realization that some of the existing consumer price subsidies are not sustainable even in the short term.

The need for ongoing analysis is demonstrated by a preliminary analysis of the profitability of rice production in the Camana Valley in Arequipa. Using the Policy Analysis Matrix, the social and private profitabilities of rice production were compared. Input subsidies (fertilizers, interest rates, seeds, etc.) accounted for 58% of the difference between private and social profitability, while producer price subsidies accounted for the remaining 42%. These results are, of course, preliminary and cannot be regarded as representative of rice production as a whole. However, the results do represent only a "snapshot" of the situation at one point in time, they need to be placed in a dynamic context.

H. Impacts of FRASA

FRASA has been operating for only two years. Output data for those two years show mixed results for price-supported basic foodstuffs. However, increased profitability in agriculture and improved terms-of-trade are clear positive impacts. For example, the terms of trade ratio for agriculture jumped from .72 in 1985 to 1.01 in 1986 and 1.11 in 1987, and agricultural incomes increased by an estimated 19% in 1986 and an additional 9% in 1987. Output by volume for rice, yellow corn and wheat were as follows:

	<u>1985</u>	<u>1986</u>	<u>1987</u>
Rice (000 MT)	918.6	744.9	1,169.0
Yellow corn (000 MT)	698.3	864.4	625.8
Wheat (000 MT)	92.2	121.0	133.2
Totals (000 MT)	1,409.1	1,730.3	1,928.0

Since agricultural output changes generally lag the stimulus by three years or more, not enough time has yet elapsed to accurately determine a significant trend.

Additionally, a positive correlation exists between the FRASA financed reduced fertilizer prices and a large increase in fertilizer usage (173,283 MT in 1985, 376,491 MT in 1986 and 517,990 MT in 1987). There also are indications that the FRASA program resulted in incorporation of significant amounts of previously idle land into production from 1985 to 1986, with resultant increased output. For example, the number of hectares producing three major basic foodstuffs increased significantly from 1985 to 1986 and remained essentially stable in 1987, as shown below:

	<u>1985</u>	<u>1986</u>	<u>1987</u>
Rice (Ha.)	205,851	168,768	215,000
Yellow corn (Ha.)	175,074	217,247	164,680
Wheat (Ha.)	80,782	97,674	101,554
Totals (Ha.)	461,707	483,699	481,234

*CDSEJ
still
trend
had
been
reversed
again
in
decades
terms
of
land*

*is this
Jed*
↑
←
??

On the average, combined productivity for these three major basic foodstuffs crops have increased significantly (from 3.1 MT/Ha. in 1985 to 3.6 MT/Ha. in 1986, and to 4.0 MT/Ha. in 1987.

FRASA continues a program of incentive prices for rice and corn production in the Selva Area, paving the way to release coastal land for producing more high-value, non-traditional export crops. Coastal farmers are actively seeking export crop options. As an example, the Rice Producers Committee recently signed an agreement with INIAA to fund (among other things) research for testing and improving productivity of alternative crops to rice on the Coast. Ica region producers have been diversifying out of corn (and cotton) into tree crops, grapes and asparagus.

Although only two years have elapsed and not much supporting data are available, a reasonable hypothesis is that FRASA, through improved terms of trade, increased rural incomes and price stabilization, has increased on-farm capitalization and induced improved yields that, in turn, have increased rural employment, contributed to rural social stability and reduced the rural-urban migration rate. As farmers begin to respond to unsuppressed higher and more stable prices, they will adopt productivity improving technologies (e.g. increased fertilizer and greater improved seed use) that permit profitability at lower product prices, thereby permitting gradual reduction and/or elimination of guaranteed producer prices.

I. GOP Views of FRASA

FRASA is the emergency centerpiece of the current agriculture Minister's FPP. He is convinced that FRASA is demonstrating to farmers that the government is serious about giving high development priority to agriculture. This view is borne out by the results of a 1987 survey of farmers (by the MIAC technical assistance contractor for APID) to determine the impact of FRASA from the farmers' point of view. The survey indicated that farmers are in fact receiving prices very near to the guaranteed support prices

The GOP also is convinced that FRASA is a key factor to assist in maintaining social stability in rural areas, that it has had a significant impact on dampening the spread of coca to Selva Areas currently producing rice and corn, and that it has discouraged successes of "Sendero" efforts to expand its control over the Central Sierra Region.

Different GOP Ministries have different views regarding the use of PL-480 funds for FRASA. The MEF is concerned about high budget deficits and does not support the direct use of PL-480 sales proceeds for FRASA. On the other hand, they find it easier to permit the use of PL-480 net proceeds to fund FRASA than to put greater demands on scarce regular treasury funds. The Ministry of Agriculture sees no reason to treat PL-480 sales differently from other basic food import sales.

On balance, the GOP (including the President) sees FRASA as being a key element of its overall agricultural development policy and program strategy, at least for the next two years, until technology transfer and diversification begin to improve efficiency sufficiently to generate more broadly-based positive income impacts.

J. Mission Conclusions About FRASA

1. Perspective

Mission views FRASA within the overall context of the GOP FPP and agricultural development strategy. FRASA, as a short/medium term measure: a) has assisted in the short run to gain the confidence of farmers by assuring them that the GOP will protect profitability for agriculture, this is quite important after 20 years of producer price suppressing policies, and b) is beginning to encourage recapitalization of agriculture from farm profits, which can in turn be expected to create conditions that encourage more rapid adoption of unit cost reducing technologies, including diversification to more intensive crops.

There are indications that the GOP is beginning: a) to shift the guaranteed producer price aspects of FRASA from a focus on price support to one of price stabilization and food security, within the framework of equilibrium prices, and b) to shift its relative policy focus on means of increasing rural incomes, productivity and output from one of impacting on prices to one of encouraging technological improvements, diversification to intensive non-traditional export products, and application of regional comparative advantage to production choices. Complimenting these changes in focus, the Minister of Agriculture also has taken a bold stand on permitting more flexible land-ownership and tenure arrangements. This is politically quite sensitive in Peru.

2. Policy Dialogue Agenda

The Mission endorses FRASA within the above described context, but with the express recognition that there will be a tendency to dedicate professional talent and available resources to making FRASA a success, which in turn causes a tendency to put off dealing with medium/long term policy dimensions of the overall agricultural development strategy. Thus, Mission policy dialogue during 1988/89 will center on not only the temporary nature of the price support aspects of FRASA, but also on the medium/long term policy needs and on ways to convert FRASA into a price stabilization and food security mechanism. Timing now appears to be right for this type of dialogue since it is likely that Ministers of key Ministries soon will change, and, in addition, it is becoming more and more apparent to the government that they cannot continue to pay the high cost of current consumer subsidies on basic foodstuffs.

More specifically, our strategy will include support and dialogue for finding politically acceptable ways to increase the average retail price of rice

to equilibrium levels, while expanding capability to target subsidies to poor populations. Mission policy dialogue also will include treatment of specific medium/long term policy needs of agriculture, such as:

a) Expand the level and improve the quality of public and private sector agricultural technology generation and transfer.

b) Permit wider role of market forces in determining control and use of farm land and irrigation water.

c) Targeting of food programs to at-risk populations, more specifically, encouraging adoption of preferred options for making Mercados Pueblos more effective by operating through private sector outlets.

d) Permit increased role of market forces in price formation and reduce regulations on the private sector food trade,

e) Encourage producer regulation of supply during the crop year through crop staging (stagger times of planting) and storage.

3. Dialogue Difficulties

High consumer subsidies are a difficult subject for policy dialogue to deal with rationally in the context of high inflation and eroding popular support for the populist García government. Unfortunately, the GOP has delayed dangerously long in making needed upward adjustments in basic foodstuffs prices (especially rice and wheat, which absorb most of the consumer subsidy) to keep pace with inflation.

To recoup previous real consumer price levels for rice and wheat will require heavy price increases. A reasonable option for rice that will be examined by USAID is to design and apply a strategy to sharply increase rice prices for higher grades of rice, and to sell a subsidized "popular" grade of rice primarily through targeted food programs.

A recently completed study by the INP (with FAO support) provides a conceptual and some analytical basis for eliminating generalized consumer subsidies on mainly imported (wheat) and commercial farm (rice) crops, and to substitute such crops as potatoes, cassava, sweet potatoes, pulses, etc. This study can serve as a point of departure in our dialogue, and a more in-depth analysis can be supported.

Price spreads for other guaranteed price products, such as corn and pulses (i.e., the spread between actual and equilibrium consumer prices) are sufficiently small to permit approaching a free market price in a reasonable time.

4. Negotiating Position Vis-a-Vis PL-480 and FRASA

With regard to use of net proceeds from PL-480 sales to fund FRASA, the

Mission believes that the issue should be dealt with only within the context of our overall policy dialogue. We will encourage the GOP to raise wholesale/retail prices of basic foodstuffs to a level more nearly representing a free market price and to simultaneously increase the exchange rate for basic food imports to more closely reflect the parity exchange rate. Such moves should be complemented by efforts to improve and expand targeted food programs, and to resolve the subsidy problem in rice marketing.

5. Implications for Self-help Measures

Self-help measures should be appropriately targeted and focussed. They should address not only food price policy, as such, but also other key complementary policy and development program needs: agricultural technology generation and transfer system improvement, and improved targeting of food subsidy/assistance efforts.

We propose to negotiate for the following self-help measures in the 1988 PL-480 agreement as described below. We plan to drop some of the less important measures that were in the 1987 Memorandum of Understanding, so as to concentrate efforts on fewer and more important points. We will seek to make the measures on agricultural policy more specific this year, and move to implementation of policies where possible.

Agricultural research and extension is the centerpiece of our agricultural strategy in Peru and, thus, our assistance initiative. As in the FY-87 Agreement self-help measures 1/, we again will seek a commitment by the Government of Peru to maintain real resource funding levels (through PL-480 and public treasury resources) to the National Agricultural and Agroindustrial Research Institute (INIAA) in support of the goal and purposes of the Agricultural Technology Transformation (ATT) Project, and to the MinAg to carry out its complementary extension strengthening program, emphasizing limited resource Trapecio Andino farmers. Likewise, we will seek assurances that the GOP will provide adequate counterpart resources to the Foundation for Agricultural Development/National Agrarian University (FDA/UNA) and the Agricultural Development Foundation (FUNDEAGRO) to support the collaborative technology generation and transfer activities of the ATT Project.

With regard to agricultural price and marketing policy, there are many indications that the GOP does not have a clear understanding of the combined effect of its price and input/output marketing policies on producers, and of their cost to society. Producer prices are not a sufficiently broad basis to determine whether the costs are acceptable to society in exchange for increased food price stability and food security.

1/ See Section (a). Appendix B provides the entire text of the FY-87 Title I Agreement self-help measures. Letters and numbers in this section refer to the corresponding letters and numbers of self-help measures in Appendix B.

There are other cost elements that need to be taken into account before a full picture can be developed. For example, input subsidies to farmers (which also carry costs), and the distribution of these costs, need to be known before the efficiency of a producer price policy can be gauged. In this context, FRASA likely is not the most efficient way to transfer resources to producers and consumers.

The consumer price structure currently supported by FRASA not only is distorted, it also carries high costs in terms of inflationary impact, via the implied subsidy of the Central Bank which finances the low exchange rate used to import foodstuffs, and the financial losses on sales of domestic rice. The disincentive effects from these subsidized consumer prices on domestic tuber producers and other substitute products also are serious.

In the Agricultural price and marketing policy area, we will drop 1987 measures (b) (3) and (4) from the 1988 self help measures. We will put relatively more emphasis on measures (b) (1) and (2). In (b) (1), emphasis will be added on agricultural input and output marketing and distribution systems costs and operations. We also will put more emphasis on the fiscal implications of subsidized producer and wholesale/consumer prices of cereals, and on the need for prices of cereals that do not have disincentive effects on substitute product prices, production and producer incomes. In (b) (2), we will seek agreement to establish specific systems to accomplish proper pricing of imported food commodities, and, in 1988, emphasize working on proper pricing of a few of the most important commodities, such as wheat and corn.

We will drop self-help measure (c) in 1988, since this subject now is to be covered in (b) (1). We also will drop the general language in measure (d) (1) and substitute much more specific language on rice marketing. We will attempt to ensure that the Ministry of Agriculture, with input from CONAA, ECASA and ENCI, analyzes producer, wholesale and retail rice marketing. The objective will be to seek ways to introduce more responsive price discrimination and product distribution, based on grades and quality standards for rice, with consumer rice subsidies concentrated on low quality rice distributed to the poorest areas. Other rice qualities would be priced without subsidies. We will drop the other two measures that were included under (D) in 1987.

Finally, we will seek a new commitment from the GOP to provide adequate funding and support through public treasury and PL 480 resources to carry out soil and water conservation activities in the Trapecio Andino. The purpose is to increase efforts in cost-effective soil/water conservation activities, thereby reducing erosion and increasing yields of Andean crops and providing more stable year to year crop production patterns. This alternative to land expansion through more intensive use has been shown to be more effective than bringing Virgin Selva land into production, or than building new coastal irrigation systems. This initiative forms part of the Andean Agricultural Strategy for Peru.

APPENDIX A :

STATISTICAL TABLES AND CHARTS

TABLE 1. PERU: PRICE POLICY RELATED DATA FOR RICE, CORN, AND WHEAT, 1970 - 1987

Definition	YEARS																		
	70	71	72	73	74	75	76	77	78	79	80	81	82	83	84	85	86	87	87
1/ Nominal International Commodity Prices (US\$/MT)																			
1/ Rice (milled rice, 5% broken, FOB Bangkok)	140	130	150	297	542	363	254	272	368	324	404	463	293	277	250	217	210	1392	274
1/ Corn (yellow No. 2, CIF Callao/Peru) 1/ & 13/	74	67	64	125	167	151	144	126	133	149	166	168	140	170	170	140	117	104	171
1/ Wheat (U.S. No. 1, Hard Red Winter, CIF Callao/Peru) 1/ & 13/	65	50	74	156	198	166	151	132	147	160	155	157	175	175	179	152	130	130	144
2/ Nominal Peruvian Producer Prices (US\$/MT)																			12/
4/ Rice (25% broken, equivalent milled rice)	161	161	168	173	207	254	169	201	181	241	255	226	219	181	158	221	324	318	218
4/ Corn (yellow)	74	81	81	116	143	182	123	127	115	117	129	112	98	66	66	121	197	201	155
4/ Wheat (Hard Winter)	94	99	113	131	152	233	156	182	159	158	168	146	153	114	156	174	257	310	191
5/ Exchange Rates (1/ per US \$)																7/	7/	7/	12/
5/ Official or Market	0.04	0.04	0.04	0.04	0.04	0.05	0.07	0.10	0.16	0.22	0.30	0.40	0.70	1.60	5.30	10.98	10.95	18.56	30.40
5/ Financial or IMF or BCR Mesa 5/	na	na	na	na	na	na	na	na	na	na	0.30	0.40	0.80	1.70	5.40	10.81	17.47	34.00	75.00
5/ Parity 6/	na	na	na	na	na	na	na	na	0.19	0.26	0.44	0.74	1.29	2.88	6.14	12.59	17.40	29.00	78.42
6/ Consumer Price Indexes (1979 = 100) 1/																			
6/ World	0.4	0.4	0.4	0.5	0.6	0.7	0.7	0.8	0.9	1.0	1.2	1.3	1.5	1.6	1.9	2.1	2.3	2.5	
6/ U.S.A.	0.5	0.6	0.6	0.6	0.7	0.7	0.8	0.8	0.9	1.0	1.1	1.3	1.3	1.4	1.4	1.5	1.5	1.6	
6/ Peru 7/	0.1	0.1	0.1	0.1	0.2	0.2	0.3	0.4	0.6	1.0	1.6	2.8	4.6	9.7	29.4	53.7	95.5	200.0	
8/ Annual Peruvian Producer Prices (1/ MT) 13/																10/	10/	10/	11/
8/ Rice (25% broken, equivalent milled rice) 4/	7.0	7.0	7.0	7.5	9.0	12.8	10.1	20.2	34.4	72.2	112.1	174.8	230.5	400.6	929.9	2760.0	5640.0	5010.0	100.0
8/ Corn (yellow) 4/	3.2	3.5	3.5	5.1	6.2	8.2	8.5	12.8	21.9	35.2	56.7	80.9	126.7	246.0	529.9	1505.5	3056.9	5800.0	100.0
8/ Wheat (Hard Winter) 4/	4.1	4.3	4.9	5.7	6.6	10.5	10.8	18.3	30.2	47.5	73.9	102.0	132.7	225.6	959.8	2179.5	4479.5	9000.0	100.0
9/ Production (1,000 MT) 3/																			
9/ Rice (25% broken, equivalent milled rice) 4/	411.0	413.8	337.6	336.5	345.9	375.8	399.3	415.8	327.5	392.3	284.3	502.3	542.9	558.3	809.1	643.0	521.4	818.3	
9/ Corn (yellow)	614.7	616.4	628.3	579.5	605.6	674.6	725.7	733.9	590.0	621.4	452.7	586.7	631.3	594.8	775.7	678.3	964.4	615.8	
9/ Wheat (Hard Winter)	125.4	122.2	126.1	123.6	127.4	126.3	127.5	115.5	104.4	102.1	77.1	116.5	100.8	75.8	83.5	92.2	120.0	130.2	
10/ Exports (1,000 MT) 3/																			
10/ Rice (5 to 15% broken)	15.4					78.2	70.6		26.4	150.4	225.8	136.8	56.9	95.4	47.6		183.1	211.4	
10/ Corn (yellow)	1.7	0.4	104.1	223.2	238.2	323.9	276.3	171.1	149.6	127.5	455.4	359.0	483.7	425.0	115.0	250.2	354.5	476.1	
10/ Wheat (Hard Winter)	521.8	675.8	853.3	763.4	713.3	620.3	743.7	766.8	720.4	816.7	823.7	941.7	940.7	967.0	964.0	805.4	1083.3	962.6	

1/ Annual Averages. Source: IMF International Financial Statistics

2/ Based on the average annual Parity Exchange Rate in relation to inflation differentials between Peru and its major trading partners using 1970 as base year.

3/ Annual Averages. Source: Centro de Investigaciones de la Universidad del Pacifico (CIUP), Organizaci6n Nacional Agraria Centro de Estadistica y Analisis Econ6mico (CEAE).

4/ Average price for unmilled coarse and superior grade rice. Equivalent milled rice computed using a factor of 1.70

5/ Annual Averages. Source: BCR, Instituto Nacional de Estadistica (INEI), and CIUP.

6/ Annual Averages based on inflation differential with Peru's major trading partners. Source: AID Peru Program Office.

7/ Parity Exchange Rate prevailing during the months of June, July, and August, which are the major harvest months for Peruvian rice producers.

8/ Estimates based on time series exponentially smoothed regression.

9/ From 1970 to 1976, the Ministry of Agriculture computed the average price for 'Pallaced' and Hard Yellow Corn.

10/ Prices paid to Rice Producers during the months of June, July, and August.

11/ Nominal Rice Prices in May, and nominal Corn and Wheat prices in March.

12/ In the case of Corn and Wheat, March Parity Exchange Rate of 1/. 53.15 was used, and in the case of Rice, May Parity Exchange Rate of 1/. 78.42 was used.

13/ Source: IMF and Ministry of Agriculture Policy Analysis Group (SARPA)

EXPLANATORY NOTES TO TABLE I

I. Nominal International Prices.

Prices quoted in current US\$ terms to reflect conformity with Parity Exchange Rates used in converting Peruvian Intis to US Dollars, thus representing the real value of current intis in relation to current dollars. Yearly prices are the average of monthly quotes for the year. For the years 1988 through 1990, prices were estimated using an exponentially smoothed time series regression with an alpha of .30.

Rice: Milled Rice, 5% Broken, FOB Bangkok Thailand, US\$/MT. Insurance and freight were not included thus allowing this price to serve as a proxy for the CIF price of .25% broken rice, which more closely resembles Peruvian rice.

Corn: Yellow No. 2, CIF Callao Peru, US\$/MT. In the case of corn, insurance and freight were included to reflect an opportunity price/cost for Peruvian producers/consumers. There are no major grade differentials between U.S. Yellow No. 2 corn and Peruvian corn.

Wheat: U.S. No. 1 Hard Red Winter, CIF Callao Peru, US\$/MT. As in the case of corn, insurance and freight were included for the same reasons.

II. Nominal Peruvian Producer Prices

Prices quoted in current US\$ equivalent using the average annual Parity Exchange rate for the year. Prices are in US\$/MT and were arrived at by dividing the Nominal or Current Inti/MT price by the average annual parity exchange rate. The US\$/MT price for 1988 was arrived at using the May Parity Exchange rate.

Rice: The unmilled producer price is adjusted to reflect the equivalent price for milled rice. This was done by dividing the average annual unmilled producer price by a factor of .70.

III. Exchange Rates

Official or Mercado Unico de Cambio (MUC). This is the official exchange rate published by the Central Bank of Peru (BCR).

The Financial or the Foreign Currency Bank Certificate (CBME) rates are the maximum allowable exchange rates used by commercial banks. In 1987, the CBME's were unified by the BCR and traded in the Negotiating Table of the BCR. Prior to 1980, the only exchange rates were the official and "black" market rates.

Parity Exchange rates are annual averages and are based on the inflation differential between Peru and its major trading partners, using 1978 as the base year. Parity exchange rates prevailing during the months of June, July, and August were used for the years 1985 through 1987, since these months are major harvest periods when farmers sell most of their crop. Due to lack of data, annual averages were used for the previous years. For 1988, the May Parity Exchange rate was used

IV. Consumer Price Indices.

Indices reflect average annual Consumer Price Indices published by the IMF using 1980 as the base year and later adjusted using 1979 as the base year in order to make it uniform with the CPI published by the GOP.

V. Nominal Peruvian Producer Prices (I./MT).

Producer prices are quoted in current Intis per Metric Ton, and reflect average annual prices. For the year 1988, May prices were used.

Rice: From 1985 through 1987, producer prices prevailing during the months of June, July, and August were used since these are the major harvest months when farmers sell most of their crop. These prices were then adjusted by a factor of .70 to reflect the equivalent milled rice price for unmilled rice.

VI. Production.

It should be noted that these figures relate to national production and do not necessarily reflect purchases from the State Run Marketing Enterprise (ENCI).

Rice: The volume of production reflects equivalent milled rice adjusted from unmilled rice. The majority of Peruvian milled rice is of 25% broken grade.

Table II PERU LEADING ECONOMIC INDICATORS, 1970-1986

YEARS	70	71	72	73	74	75	76	77	78	79	80	81	82	83	84	85	86	87	Source
I. INDICATORS																			
1. Growth Rate GDP (%)	5.4	5	1.6	4.3	7.5	4.5	2	-0.1	-0.5	4.1	3.8	3.9	0.4	-10.9	4.8	1.9	6.5	6.9	INE-SCR
Growth Rate AGR GDP (%)	7.8	2.1	-2.5	0.4	3.7	0	1.5	-0.1	-1.5	3.9	-5.8	112	2.9	-9.6	12.5	2.9	3.6	5.2	INE-SCR
Growth Rate IND GDP (%)	6.6	6.9	6.7	6	10.9	4.1	4	-4.3	-4	4.3	5.7	-0.2	-2.5	-16.0	3.9	3.9	14.0	11.9	INE-SCR
II. Prices																			
Wholesale Price Ind. (1970=100)	100	116.8	144.7	200.4	292.6	516.6	860.3	1347.6	2285.4	3541	7536.6	16610.6	45499.5	72934.7	119487.0				INE-SCR
Ind. Price Cons. (1970=100)	5	6.8	7.2	9.5	16.9	44.8	22.4	73.7	73.5	66.8	60.8	72.7	72.9	125.1	111.5	159.3	62.9	114.5	INE-SCR
Consumer Price Index (1970=100)	11.02	12.09	12.95	14.19	16.58	20.50	27.07	37.78	55.65	100.00	159.20	279.20	459.20	969.5	2078.0	5078.2	7551.1	17750.4	INE-SCR
Annual Inflation (%)	0	0	0	0	0	13.2	52.7	61.2	55.5	28.1	35.9	47.7	90.7	105.5	102.7	118.1	0.0	95.6	SCR
Exchange Rate (S/ vs US\$)	38.7	38.7	38.7	38.7	38.7	40.8	55.8	84.2	156.4	224.2	288.9	442.3	497.6	1478.6	3466.9	10960.00	12960.0	27400.0	SCR
III. Employment-Income																			
Unempl. & Underempl. (%)	50.6	48.6	48.4	45.5	45.8	47.3	49.5	54.0	58.5	56.5	53.2	52.8	56.9	62.5	65.1	65.9	62.5	59.6	M.Trep.
Real Wage Ind. (1970=100)	111.9	122.0	132.3	144.9	142.6	128.4	131.6	111.0	100.0	100.0	112.6	110.6	113.0	94.1	72.0	65.0	62.4	62.2	INE-SCR
IV. External Sector																			
Exports (US\$ Million)	1074	689	945	1112	1533	1330	1048	1726	1972	3676	3916	3249	3293	3015.0	3147.0	10966.0	2497.0	2175.6	SCR
Imports (US\$ Million)	700	720	812	1022	1708	2427	2896	2141	1160	1954	3090	3282	3721	2702.0	2140.0	10069.0	2519.0	2702.0	SCR
Net Incl. Favr. (US\$ Mill.)	402	330	397	411	693	116	-752	-1111	-1925	554	1276	772	578	65.0	1107.0	11421.0	982.0	470.0	SCR
Current Acc. Deficit (% GDP)	-1.2	-2.7	-3.3	-3.6	-2.8	-4.9	-6.3	-9.7	-8.1	-1.1	-4.7	-8.4	-9.3	-10.1	-7.6	-5.0	-6.0	-5.0	SCR

* PRELIMAR
 CONCEPTS ECONOMIC-CIIP
 FILE: REPULEAD I
 DISK: 011

Table III AGRICULTURAL SECTOR LEADING INDICATORS, 1970-1986

YEARS	70	71	72	73	74	75	76	77	78	79	80	81	82	83	84	85	86	87	
I. PRODUCTION																			
Growth Rate Agr Prod (value)	.....	2.8	+3.7	1.1	3.3	-1.3	1.2	1.8	-2.6	2.7	-7.6	10.5	3.3	-9.0	11.0	2.2	3.8	5.0
Growth Rate Crops Value (C)	.....	1.7	-4.4	0.7	2.2	-3.4	0.7	2.2	-2.3	4.0	-11.4	11.2	3.0	-10.7	15.9	1.0	2.7	3.0
Growth Rate Livest Value (L)	.....	6.5	-1.4	2.2	5.6	5.1	2.3	0.6	-0.4	-1.0	3.3	9.0	4.0	2.7	-5.3	5.4	7.0	10.5
II. AREA																			
Total Harvested (Ha/Thous)	1249.4	1254.3	1277.3	1270.8	1284.1	1251.1	1258.7	1265.0	1193.6	1261.3	1009.6	1181.2	1200.2	1118.5	1128.7	958.4	1009.4	107.4	
III. PRICES																			
Food Price Index (Clima)	9.7	10.4	11.2	12.3	14.6	19.4	25.6	35.9	57.4	100.0	109.9	250.1	429.3	966.5	1990.8	4981.8	9000.9	10000.0	
Whole Agr Price Index (Local Products)	.....	.....	.....	100.0	104.0	140.9	195.1	274.3	395.8	695.5	1042.5	2016.9	3419.0	6079.5	14749.1	30047.6	75036.1	100000.0
Whole Agr Price Index (Exports)	.....	.....	.....	100.0	146.5	137.6	158.7	274.1	365.5	673.0	1076.3	1581.0	2371.7	6475.3	15116.2	40448.2	70477.4	100000.0
IV. INTERNATIONAL TRADE (KUS\$Mill)																			
Agr Prod & Input Imports	83.6	87.5	145.7	184.4	269.4	370.2	555.0	824.8	1244.7	1777.8	294.4	560.6	397.9	486.5	326.2	151.0	355.0	107.0	
Agr Crop Prod Imports	45.2	51.2	105.1	134.4	210.2	295.5	410.2	566.2	854.8	1237.1	200.2	459.5	281.1	290.7	243.6	105.0	220.0	72.0	
Agr Livestock Prod Imports	31.1	27.5	30.6	36.9	42.1	46.7	32.2	36.6	17.7	17.5	49.0	32.0	32.0	37.0	47.4	14.0	171.0	35.0	
Agr Input Imports	7.3	8.8	18.1	13.1	29.1	28.0	12.5	22.0	22.0	17.2	21.0	21.0	17.5	16.8	17.2	8.4	.....	.....
Capit Goods-Agr (KUS\$Thous)	6.6	10.2	19.9	19.9	14.7	20.2	16.7	10.4	16.6	121.4	51.5	45.0	68.2	24.7	.....	.....	.....	.....
Agr Trade Exports (KUS\$Thous)	161.5	151.8	166.6	220.3	336.6	390.0	287.2	347.7	276.7	1361.9	159.0	227.5	277.8	344.5	260.8	246.0	250.0	211.0	
Agr Non-Food Exports	5.5	5.6	17.7	9.9	10.3	10.4	12.2	19.9	19.5	25.0	20.8	15.7	13.7	16.1	13.6	.....	.....	.....

* PRELIMINARY

.. Not available

C/ Only 10 Principal Products

L/ Included Agr Ind

APAD 87

FILE: AGPSED

DISK: 601

TABLE IV - SELECTED BASIC FOODSTUFFS FINANCIAL PRICE SUBSIDIES/TAXES IN PERU (*) 1977 - 1986

(CURRENT U.S.\$ MILLIONS)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
A. Domestic Production	-	-	39.9	92.1	143.2	124.0	62.8	19.6	21.1
Rice	-	-	39.9	90.0	140.2	120.5	59.1	19.0	20.4
Corn	-	-	-	2.1	3.1	3.5	3.7	0.6	0.7
Wheat	-	-	-	-	-	-	-	-	-71
B. Imports	165.6	11.2	98.3	107.3	20.1	77.6	25.0	(5.4)	(2.9)
Rice	-	-	-	-	-	-	(0.8)	(5.4)	(2.9)
Corn	23.5	-	4.8	16.6	-	-	-	-	-
Wheat	<u>142.1</u>	<u>11.2</u>	<u>93.5</u>	<u>90.7</u>	<u>20.1</u>	<u>77.6</u>	<u>25.8</u>	-	-
EXCHANGE RATE:(I/.to \$	0.084	0.1565	0.2245	0.2889	0.4223	0.6976	1.6286	3.4665	10.98

SOURCES: Derived from information prepared by GAPA based on data from BCR(1984-86), and Manuel Lajo, "Precios, Subsidios y Monopolios", Fundacion Ebert, 1986.

(*) Difference between purchase and sales prices

TABLE V - PERU PRODUCER PRICE SUBSIDIES/ (taxes) 1985-1988

(US\$ MILLIONS)

	DOMESTIC PRODUCER PRICE 1/ (US\$/MT)	SOCIAL PRICE US/MT 2/	PRICE DIFFERENCE (US\$/MT)	VOLUME PURCHASED 4/ MT.	AMOUNT PRODUCER SUBSIDY (TAX) (US\$)
<u>MILLIONS)</u>					
<u>1 9 8 5</u>					(41.859)
Rice	226	285	(64)	643,000	(41.152)
Corn	121	142	(21)	33,707	(.707)
Wheat	174	154	20	—	—
<u>T O T A L</u>					
<u>1 9 8 6</u>					27.764
Rice	324	285	39	521,400	20.335
Corn	187	142	45	149,464	6.726
Wheat	257	154	103	6,818	.703
<u>T O T A L</u>					
<u>1 9 8 7</u>					40.322
Rice	318	285	33	818,300	27.00
Corn	201	142	59	172,920	10.202
Wheat	310	154	156	20,000	3.120
<u>T O T A L</u>					
<u>1 9 8 8 3/</u>					(9.105)
Rice	269	285	(16)	818,300	(13.09)
Corn	159	140	19	172,920	3.285
Wheat	192	157	35	20,000	.700

SOURCE : Derived by OARD from data supplied by GAPA

1/ Price in INTIS converted at parity Exchange Rate.

2/ Median FOB Value (1970-1987) plus Ocean Freight and Insurance (\$17.- for corn, \$19.- for wheat,), except rice is FOB Bangkok for 5% broken.

3/ Projected based on March price, May parity and 1987 purchases

4/ Purchased by State Run Marketing Enterprise (ENCI)

TABLE VI - SUMMARY OF PERU PRODUCER AND CONSUMER

PRICE SUBSIDIES, 1985 - 1988

	<u>1985</u>		<u>1986</u>		<u>1987</u>		<u>1988</u>	
	amount	%	amount	%	amount	%	projected amount	%
Total Subsidy	21.100	100	80.964	—	94.932	100	107.37	100
Producer Subsidy	(41.859)	0	27.764	41	40.332	42	(9.105)	0
Consumer Subsidy	21.100	100	53.200	66	54.600	58	107.37	100

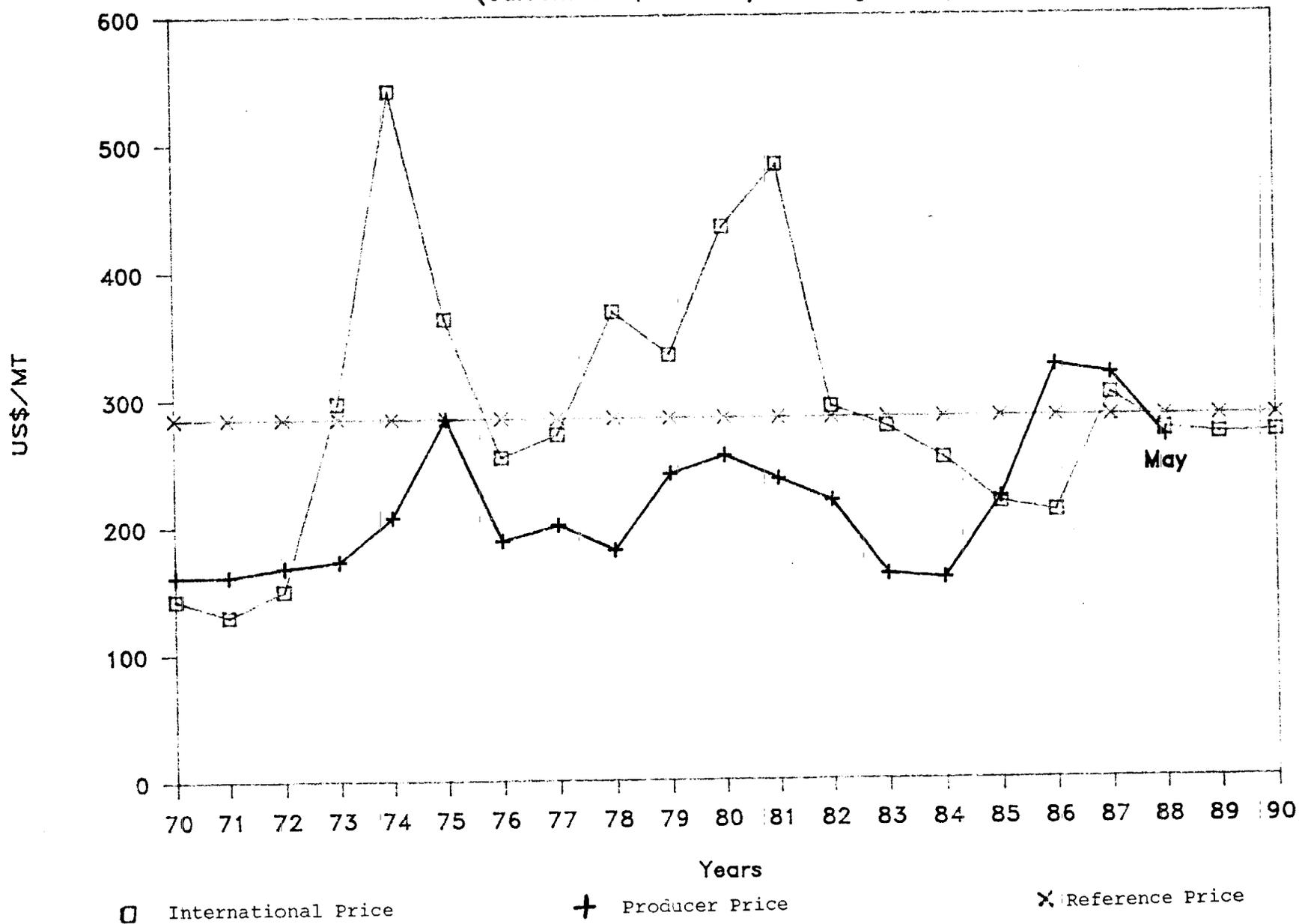
SOURCE: Derived by OARD from data supplied by GAPA.

TABLE VII
PERU: PRODUCER AND CONSUMER PRICE SUBSIDIES FOR
RICE, CORN AND WHEAT

	<u>Rice (c)</u>	<u>Wheat (d)</u>	<u>Corn (e)</u>
<u>US\$/Kg (a)</u>			
(1) Producer Price	0.26	0.19	0.16
(2) Wholesale Price	0.15	0.05	0.18
(3) Social Price (b)	0.25	0.14	0.10
<u>US\$/Kg</u>			
(4) Producer Subsidy/(Tax) (1) - (3)	0.01 (f)	0.05	0.06
(5) Consumer Subsidy/(Tax) (2) - (3)	0.10	0.09	(-0.08)
<u>1987 (1000 MT)</u>			
(6) Total Production	695.6	20.0 (h)	703.6
(7) Total Subsidized/ (Taxed) Consumption	740.2	1,038.6	1184.0
(8) Total Imports	211.3	1,018.6	500.0
<u>Annualized Value (\$1,000)</u>			
(9) Producer Subsidy/(Tax) (6) x 1,000 x (4)	7,584.0 (g)	1,000.0 (i)	42,216.0
(10) Consumer Subsidy/(Tax) (7) x 1,000 x (5)	72,254.9	93,474.0	(94,720.0)

- (a) At estimated May parity Exchange Rate I/.78.42/\$.
- (b) Long run international CIF price of similar quality product.
- (c) Average farmgate price of unmilled rice converted to milled rice based on .7 conversion factor, using producer and consumer prices expected to prevail in May, 1988.
- (d) Producer and average wholesale prices expected to prevail in May, 1988.
- (e) Average producer and consumer prices expected to prevail in May, 1988.
- (f) It should be noted that a "social price" could reasonably vary up or down from this estimate.
- (g) If the true social price were 4% higher than that estimated here, this producer subsidy would disappear altogether.
- (h) Actual domestic purchases by ENCI, the State Run Marketing Enterprise.
- (i) Most domestically produced wheat is sold locally and does not enter commercial channels, since it is not of milling quality. Thus, local silling prices do not appear to be significantly affected by the ENCI guaranteed price.

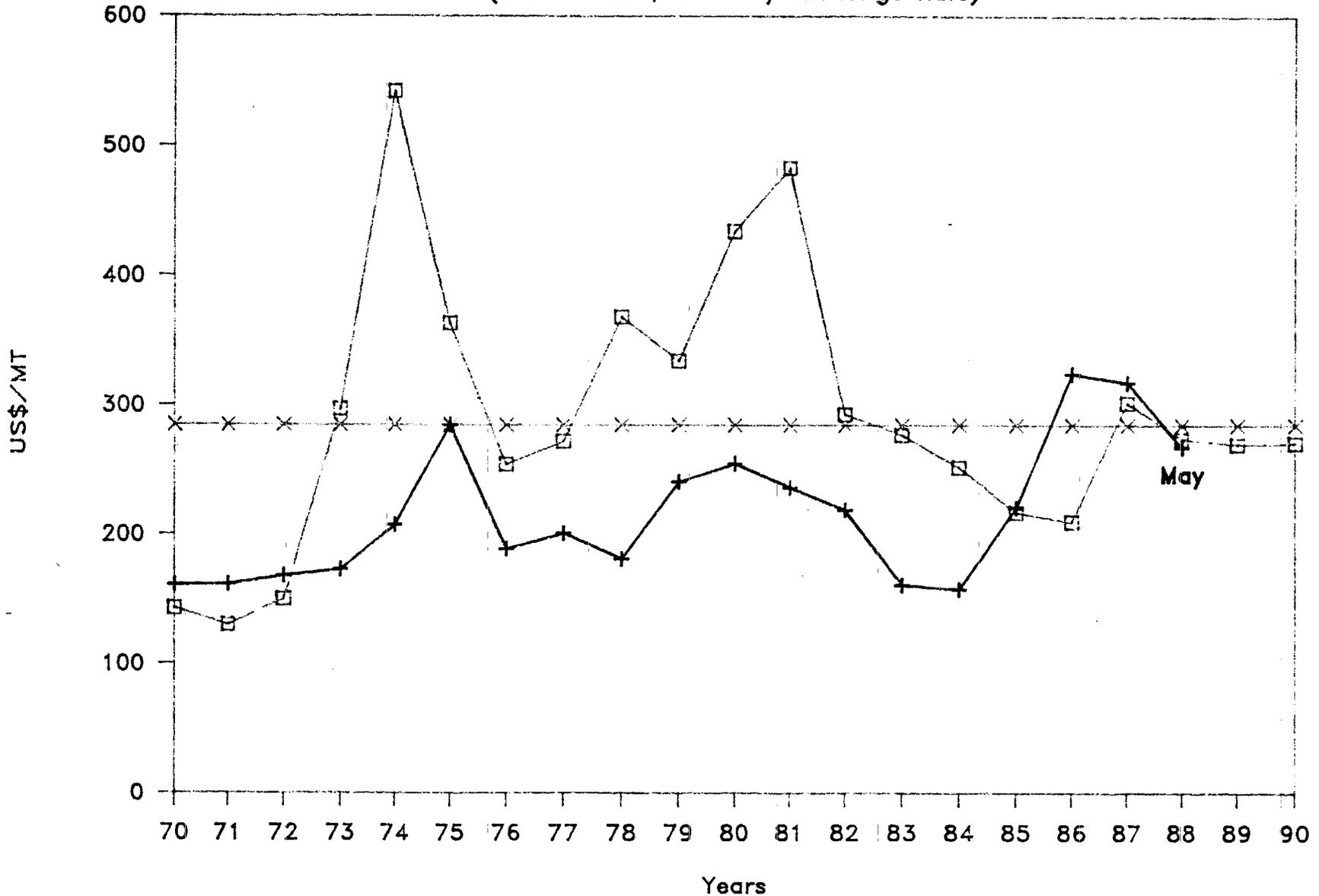
CHART A: Rice Prices : PERU AND FOB BANGKOK (5% broken), 1970-1990
 (Current US \$ at Parity Exchange Rate)



Note: Reference Data is shown in Table I

CHART A: Rice Prices : PERU AND FOB BANGKOK (5% broken), 1970-1990

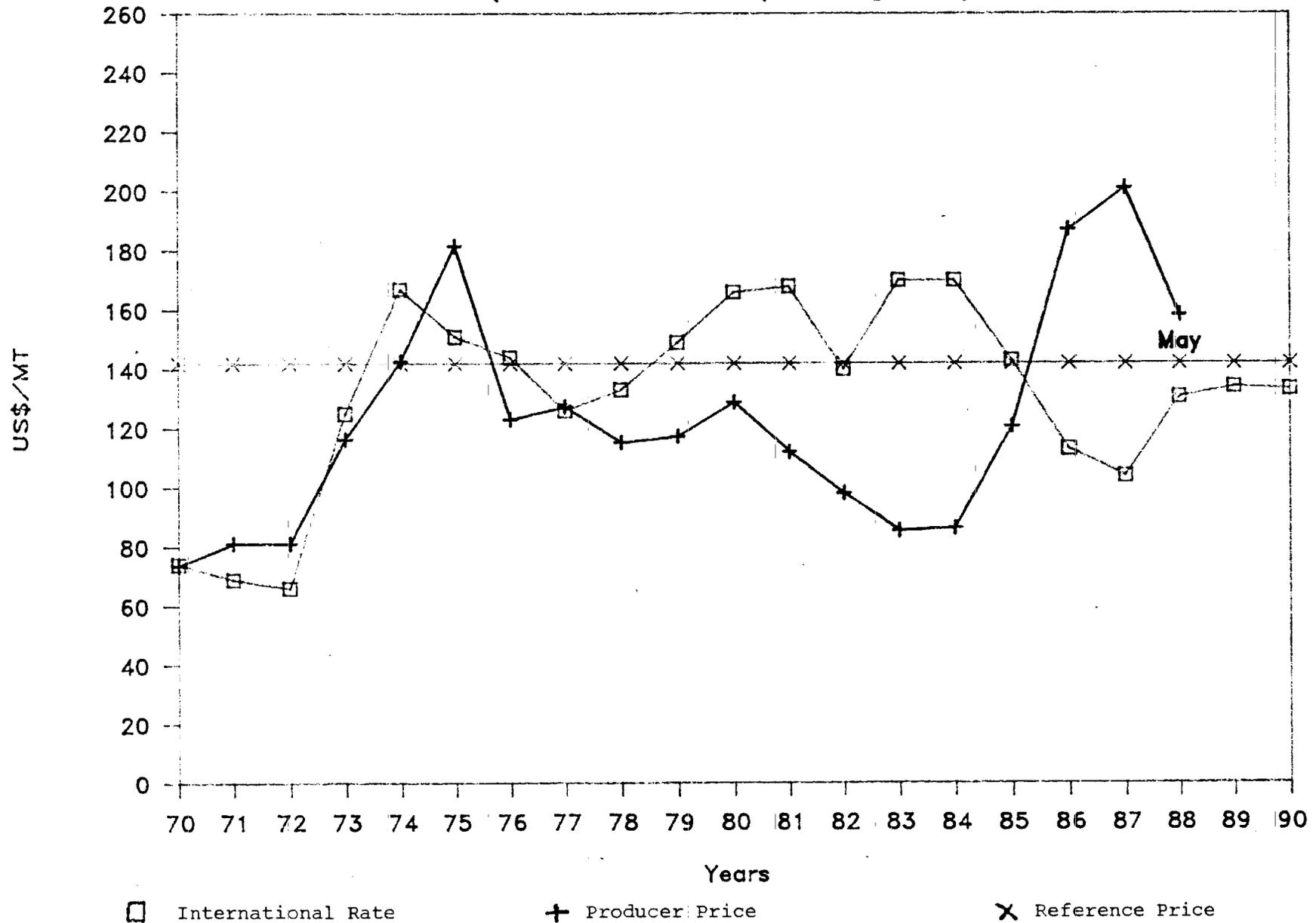
(Current US \$ at Parity Exchange Rate)



International Price
 Producer Price
 Reference Price

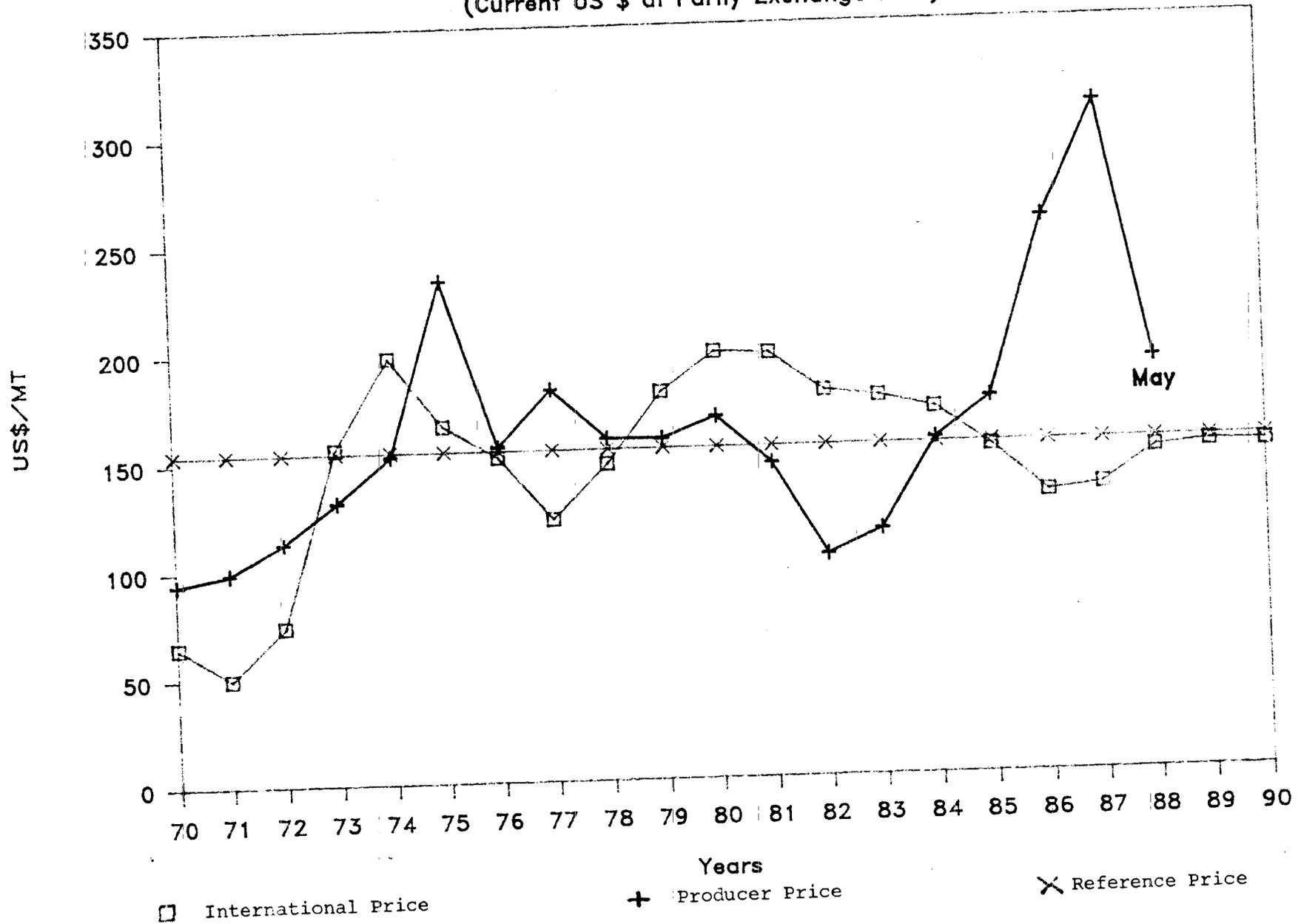
Note: Reference Data is shown in Table I

Chart B.: Corn Prices: Peru and CIF Callao, 1970-1990
 (Current US \$ at Parity Exchange Rate)



Note: Reference Data is shown in Table I

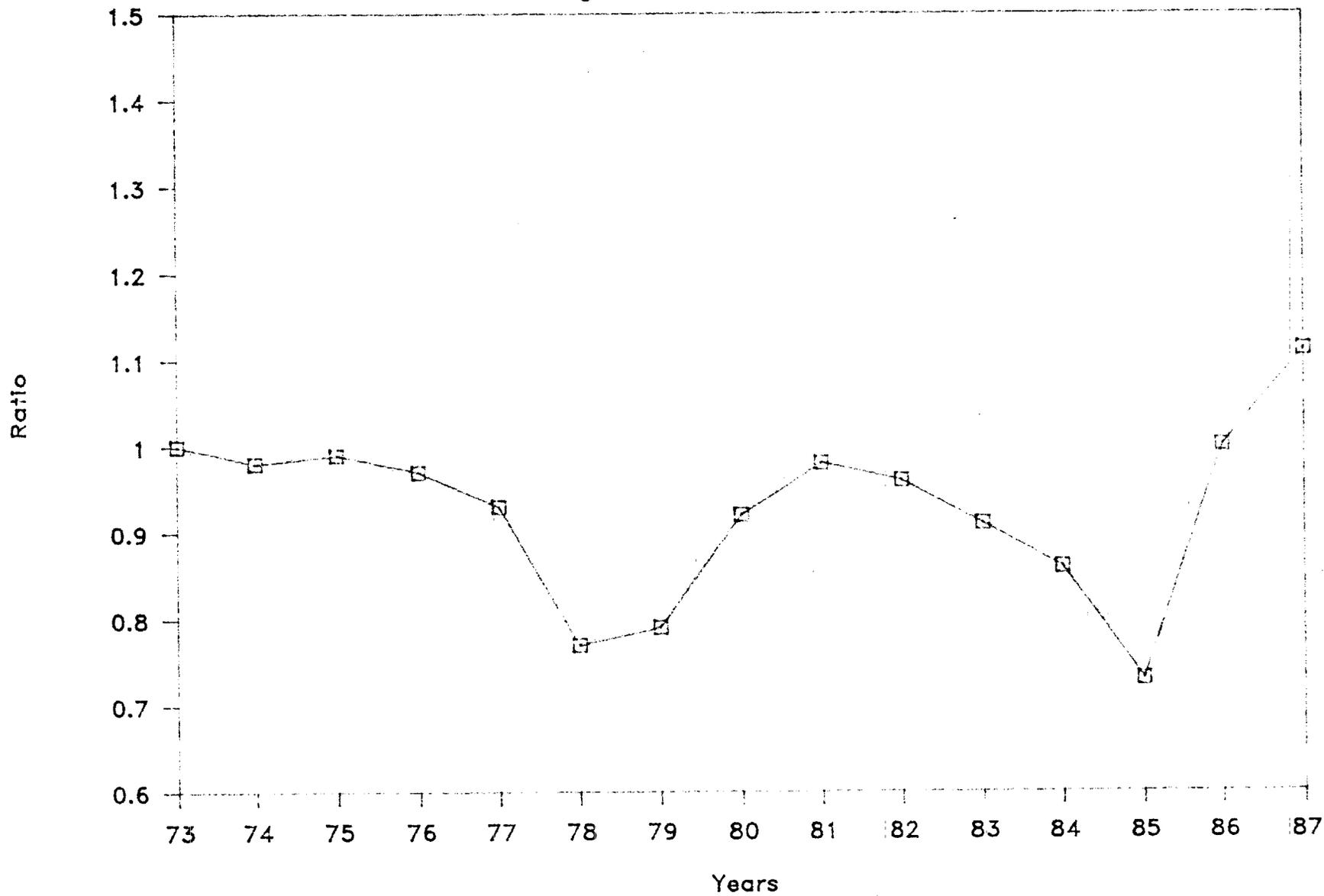
Chart C: Wheat Prices: Peru and CIF Callao, 1970-1990
 (Current US \$ at Parity Exchange Rate)



Note: Reference Data is shown in Table I

Chart D: Peru: Agricultural Terms of Trade - 1973-87

Domestic Agr.Index/Gen.Whisle. Index



APPENDIX B:

PERU FY-87 TITLE I AGREEMENT SELF-HELP MEASURES

C. SPECIFIC SELF-HELP MEASURES

1. In order that the self-help measures contained in Item V of the Sales Agreement be described, to the maximum extent feasible, in specific and measurable terms, the United States and Peru hereby agree that during 1987 and 1988:

(a) Agricultural Research and Extension

The Government of Peru will provide adequate funding and support in 1987 and 1988 to the National Institute for Agricultural Research and Extension (INIPA) or its successor agency to complete the program planned with AID in the Research, Extension and Education project and begin the new Agricultural Technology Transformation project. INIPA will propose and justify a new professional personnel system to make it possible to recruit and retain highly qualified professional employees.

(b) Agricultural Development Policies

(1) The Ministry of Agriculture, through its Agricultural Policy Analysis Group, in coordination with the Central Office of Prices of the Ministry of Finance, will analyze production costs, prices for agricultural inputs (including credit and water), and world market as well as Peruvian

prices of agricultural products in absolute and relative terms, to develop incentives for more efficient agricultural production and for development of support prices for key domestic agricultural products in line with comparative production advantages. These studies will be related to pricing policies for food sales to the public to increase domestic food production while minimizing the costs to the budget of the Government of Peru.

(2) The Ministry of Economy and Finance, with the Ministry of Agriculture, will carry out studies of food import policy, including sales prices, import tariffs, quantity limitations, etc., recommending actions to ensure that imported foods do not provide a disincentive to increased production and consumption of domestic agricultural products, and that revenues from imported food products assist in financing domestic agricultural production incentives.

(3) The Ministry of Agriculture will prepare a proposal to establish an institutional mechanism, with academic and private sector support that will guarantee continuity in the analytical studies of agricultural policies, with recommendations for measures to increase domestic food security.

(4) The Ministry of Agriculture, in collaboration with other agencies promoting trade expansion, will analyze and take steps to increase non-traditional agricultural exports and reduce existing constraints in the agricultural sector and in international markets which hinder this agricultural trade expansion.

(c) Agricultural Marketing

The Ministry of Agriculture will take actions to (1) reinforce the efficient marketing and distribution system particularly for perishable agricultural products, (2) analyze and recommend actions which will provide incentives for the private sector to expand its participation in the storage and marketing of agricultural products, and (3) analyze and recommend actions to assure coherence and uniform criteria for the efficient functioning of activities of government enterprises related to agricultural marketing and distribution.

(d) Food and Nutrition

(1) The Ministry of Agriculture will carry out studies and take actions tending to guarantee that agricultural subsidies are directed to the low income groups.

(2) The Ministry of Economy and Finance, in coordination with other agencies, will study the magnitude of adequate food subsidies minimizing unnecessary costs and the use of foreign exchange, with the goal of providing more adequate food supplies to the groups now suffering most seriously from malnutrition.

(3) The Government of Peru will establish the technical commission to implement the second National Food Consumption Survey (ENCA II) to provide the food consumption data needed to design more cost effective food security and targeted food subsidy programs.

2. The Government of Peru, through the Ministry of Economy and Finance, the National Planning Institute and the Ministry of Agriculture agrees to review progress on meeting the above self-help measures six months after signature of the Agreement. The Government of Peru agrees to present a report on its actions with regard to (a), (b), (c), and (d) above on or about August 1, 1988, approximately one year after signature of this Agreement.