



# Peru in Brief: Political and Economic Conditions and Relations with the United States

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## Summary

This report provides an overview of Peru's government and economy and a discussion of issues in relations between the United States and Peru.

Peru and the United States have a strong and cooperative relationship. Several issues in U.S.-Peru relations are likely to be considered in decisions by Congress and the Administration on future aid to and cooperation with Peru. The United States supports the strengthening of Peru's democratic institutions, its respect for human rights, environmental protection, and counternarcotics efforts. A dominant theme in bilateral relations is the effort to stem the flow of illegal drugs, mostly cocaine, between the two countries. In the economic realm, the United States supports bilateral trade relations and Peru's further integration into the world economy. The United States is Peru's top trading partner. The U.S.-Peru Trade Promotion Agreement (PTPA) went into effect February 1, 2009. The Obama Administration requested \$74 million in foreign assistance for Peru for FY2013 to advance these objectives.

Ollanta Humala, of the left-wing Gana Peru, was sworn in as Peru's president in July 2011 for a five-year term. Gana Peru won 47 seats out of the 130 seats in the unicameral Congress, requiring Humala to rely on political alliances with lesser parties in order to pass legislation. Deep social divides over how to pursue development continue to undercut political stability. The more radical elements of Humala's original support base and his party urge the pursuit of more leftist policies, such as nationalization of strategic industries, which Humala called for during the election campaign. Forces that resist more radical policies include a strong business sector; a conservative, wealthy elite; a centrist middle class; and a divided Congress. Social unrest, especially over exploitation of natural resources, is likely to remain a challenge for the Humala government.

Since 2001 Peru's economy has been stronger than all others in the region, with its growth due mostly to the export of natural resources. High economic growth, along with social programs, has helped to lower Peru's overall poverty rates. Nonetheless, in some jungle, mountain, and rural areas of the country, over 60% of the population continue to live in poverty. The income distribution gap remains quite large as well. This economic disparity has contributed to rising social unrest. President Humala submitted, and the legislature approved, a bill increasing royalties mining companies must pay. The government estimates the royalties will generate about US\$1 billion a year, which it will use to finance social development programs intended to narrow both the social divide and the economic distribution gap.

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## Background

Peru has had a turbulent political history, alternating between periods of democratic and authoritarian rule. Political turmoil dates back to Peru's traumatic experience during the Spanish conquest, which gave rise to the economic, ethnic, and geographic divisions that characterize Peruvian society today. Since its independence in 1821, Peru has had 13 constitutions, with only 9 of 19 elected governments completing their terms. Peru's most recent transition to democracy occurred in 1980 after 12 years of military rule. The decade that followed was characterized by a prolonged economic crisis and the government's unsuccessful struggle to quell a radical Maoist guerrilla insurgency known as the Shining Path (Sendero Luminoso).<sup>1</sup> President Alan García's first term (1985-1990) was characterized by many observers as disastrous. Of the leftist American Popular Revolutionary Alliance (APRA), García's antagonistic relationship with the international financial community and excessive spending on social programs led to hyperinflation (an annual rate above 7,600%) and a debt crisis.

By 1990, the Peruvian population was looking for a change and found it in the independent candidate Alberto Fujimori. Initially applauded for his aggressive economic reform program and stepped up counterinsurgency efforts, Fujimori became increasingly autocratic, dissolving the legislature in 1992, overseeing the writing of a new constitution in 1993—which allowed him to run again, and win, in 1995—and engaging in strong-handed military tactics to wipe out the Shining Path that resulted in serious human rights violations. Reelected in 2000, Fujimori's government collapsed with revelations of electoral fraud and high-level corruption, and he fled the country later that same year. In a landmark legal case, on April 7, 2009, former President Fujimori was convicted and sentenced to 25 years in prison for “crimes against humanity,” on charges of corruption and human rights abuses. Analysts regard the court's decision as a considerable accomplishment for Peru's judicial system, which has been considered weak and subject to political influence.

Peru then entered a period of relative political stability, economic growth, and poverty reduction, initiated by a capable interim government, headed by President Valentin Paniagua (November 2000-July 2001), and continued by Peru's first president of indigenous descent, Alejandro Toledo (2001-2006). Toledo pushed through several significant reforms that increased tax collection, reduced expenditures and the budget deficit, and negotiated a free trade agreement with the United States.

Softening his populist rhetoric, Alan García launched a political comeback and won the presidential race in 2006. Many observers cast him as “the lesser of two evils” compared to his opponent, Ollanta Humala, who espoused nationalist, anti-globalization policies. García (2006-2011) maintained orthodox macro-economic policies. Economic growth continued under García, and so, too, did popular protests over the failure of that growth to improve social conditions for Peru's poorest people, and over the exploitation of natural resources.

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<sup>1</sup> Between 1980 and 2000, armed conflicts between Peruvian government troops, the Shining Path, and others resulted in some 69,260 deaths and disappearances. See Commission on Truth and Reconciliation in Peru, Final Report, Annex 2, August 28, 2003. For more information, see David Scott Palmer, ed., *The Shining Path of Peru*, New York: St. Martin's Press, 1994.

## Current Political Conditions

Following his unsuccessful bid for the presidency five years ago, Ollanta Humala moderated his stance from an extreme leftist, populist, nationalist approach allied with Venezuela's President Hugo Chavez, running again under a more center-leftist approach modeled after Brazil's former President Luiz Inacio Lula da Silva. Humala was sworn in as Peru's president in July 2011 for a five-year term. He defeated Keiko Fujimori, a conservative member of Congress and daughter of disgraced former President Alberto Fujimori. In his first address as president, Humala promised to maintain free-market policies while also working to narrow the wide economic distribution gap and eliminate the social exclusion of Peru's poor, mostly indigenous population. He reiterated that commitment in a speech to the Peruvian Congress as he completed his first year in office. Acknowledging that his government had not done all it pledged to do, Humala said his goal was to cut Peru's poverty by half, to 15% by the end of his term in 2016. Initially, Humala's cabinet encompassed a broad range of the political spectrum, from orthodox economists to former military officers and left wing radicals pursuing a consensus-based pragmatic approach. Humala has shuffled his Cabinet three times in a year, dismissing all of his top leftist advisers in a major cabinet re-shuffle in late 2011, and consolidating a more centrist approach since then.

**Figure 1. Map of Peru**



**Source:** Perry-Castaneda Library Map Collection.

After he was elected, Humala began negotiations with the mining sector, so that, once inaugurated, he was quickly able to propose an increase in mining royalties paid to the government. Mining companies accepted the increase as inevitable, since both presidential candidates had advocated it, and were willing to accept moderate increases in exchange for a stable set of royalty payment rules. The Peruvian Congress passed the bill, which became effective in January 2012. The increased royalties are expected to provide an additional

US\$1 billion annually to the national budget to fund Humala's proposed social inclusion programs and infrastructure projects.<sup>2</sup>

## **Addressing Social Conflicts**

President Humala also committed himself to reducing the social conflicts that have impeded government functions over the last couple of administrations. Peru's Ombudsman for Human Rights reported that there were over 200 civil conflicts across Peru as Humala came into office.<sup>3</sup> The first law Humala signed was a prior consultation law, requiring mining, energy, and logging companies to consult with indigenous and rural communities about projects planned in their communities, which had been the source of much social conflict. Former President Alan García had vetoed a similar law, and violent conflicts over land use continued throughout his term. The law brings Peru into compliance with the International Labor Organization's Convention on Indigenous Peoples, which Peru ratified in 1993. The convention requires that companies consult indigenous groups before entering their ancestral territories to exploit natural resources. Implementing regulations went into effect on April 4, 2012. As a complement to the new law, the Humala administration also created an office of conflict prevention.

Because the prior consultation law does not grant local communities veto power over investments in their area, however, and does not require consultation for government coca eradication efforts, tensions are likely to continue. Some businesses worry that the new consultation process could add bureaucratic impediments to their projects. And some conflicts have political or other roots besides land use issues. Although the government said it hoped to reduce the number of conflicts by increasing dialogue among communities, investors, and the state, major conflicts have continued, and some critics say not much has changed. The Humala government has declared two states of emergency in the northern Cajamarca region of Peru, but protests against mining efforts there have continued, often turning violent. Since Humala took office, at least 17 people have been killed in police confrontations.<sup>4</sup> In the southeastern region of Madre de Dios, the government is contending with illegal mining, which has also led to violence, pollution, and destruction of the Amazonian rainforest. Estimating there to be up to 50,000 small-scale miners in the area, the government decreed stricter penalties for illegal mining in February 2012, has removed thousands of miners, and plan to remove all illegal miners working near national parks.<sup>5</sup>

Deep social divides over how to pursue development continue to undercut political stability. The more radical elements of Humala's original support base and his party, Gana Peru, urge the pursuit of more leftist policies, such as nationalization of strategic industries, which Humala called for during the election campaign. Forces that resist more radical policies include a strong business sector; a conservative, wealthy elite; a centrist middle class; and a divided Congress.

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<sup>2</sup> "Peru's Humala signs bills to raise mining taxes," *Reuter News*, September 28, 2011.

<sup>3</sup> "Peru: Humala's Biggest Challenge," *LatinNews.com Weekly Report*, vol. WR-11-25, June 23, 2011.

<sup>4</sup> Mattia Cabitza, "Peru Mine Disputes mar President Humala's First Year," *BBC News*, June 27, 2012.

<sup>5</sup> Rob Walker, "Peru's Gold Rush Pits Illegal Miners Against Government," *BBC News*, July 11, 2012.

## **Humala and the Peruvian Congress**

As Humala alienates the leftist forces that helped him win the election, his position in the Congress becomes weaker. Humala's party does not have an outright majority; it has 47 seats to Fujimori's party's 37 seats in the 130-seat chamber. His weak alliance with former President Alejandro Toledo's centrist Peru Posible party, which gave him a two-seat majority, has dissolved, and some members of his own party have left in response to his shift away from the left and the crackdown on anti-mining protests.<sup>6</sup> Unable to agree on candidates, the Congress has left key positions, including two Constitutional Tribunal judges, the head of the human rights office, and three members of the central bank's board, vacant for over a year. Nonetheless, Toledo has been able to push through reforms in his first year, and in July 2012 his party was able to hold onto the leadership position in the Congress.

## **Petition for Fujimori's Release from Prison**

Another potentially destabilizing element was thrown Humala's way when former President Fujimori's family petitioned the Justice Ministry for his release from prison on humanitarian grounds because he has mouth cancer. Fujimori was convicted for crimes against humanity, including for his role in the extrajudicial execution of 15 people, the forced disappearance and murder of nine students and a professor from a university, and two other abductions. The international organization Human Rights Watch opposes granting Fujimori amnesty, saying it "would be incompatible with Peru's obligations under international law," and that humanitarian pardons "should only be granted on the basis of an independent, thorough, and conclusive medical determination of the gravity of the prisoner's condition and the seriousness of the risk continued detention might pose."<sup>7</sup> Some opposed to his release warn it could lead to social unrest, and greater influence by Fujimori; he is said to have played a key role in the last elections, in which his daughter lost her bid for the presidency, but other supporters of his won seats in the Congress. President Humala, who once led a failed coup attempt against Fujimori, will decide whether to grant the pardon.

## **Socio-Economic Conditions**

Peru's economy has been stronger than virtually all other Latin American economies since 2001. Its gross domestic product (GDP) growth rate averaged 8.8% from 2001 to 2008.<sup>8</sup> During the 2008-2009 global financial crisis, Peru's economy slowed to 0.9%, but was one of the few in Latin America to maintain positive growth. Meeting with then-President García in Washington in early June 2010, President Barack Obama called Peru an "extraordinary economic success story."<sup>9</sup> In 2011, Peru's economy grew by 6.9%.<sup>10</sup> The Economist Intelligence Unit predicts 5.8%

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<sup>6</sup> "Peru: Country Outlook," *Economist Intelligence Unit*, October 1, 2011; and "Country Report: Peru," *Economist Intelligence Unit*, March 2012, p. 4.

<sup>7</sup> Diego Moya-Ocampos, "International Human Rights Organisation Opposes Eventual Amnesty to Former Peruvian President," *IHS Global Insight Daily Analysis*, October 12, 2012.

<sup>8</sup> The World Bank, *Peru: Brief*, September 16, 2011, at <http://web.worldbank.org>.

<sup>9</sup> Federal News Service, "Remarks by President Barack Obama and President Alan Garcia of Peru after their Meeting (as released by the White House)," June 8, 2010.

<sup>10</sup> "Country Report: Peru," *Economist Intelligence Unit*, March 2012, p. 3.

GDP growth in 2012 and continued strong growth in 2013.<sup>11</sup> Most of Peru's growth is due to the export of natural resources such as copper, gold, silver, zinc, lead, iron ore, fish, petroleum, natural gas, and lumber.

Peru has been integrating into the world economy, signing free trade agreements with the United States and other key trade partners such as Canada, Chile, China, Japan, Singapore, South Korea, and Thailand. Peru is completing agreements with the European Union and the European Free Trade Association<sup>12</sup> as well. Peru hosted the third South American-Arab Countries Summit in October 2012, during which 21 Middle Eastern and 11 South American countries agreed to create an investment bank to fund joint projects between the Union of South American Countries (UNASUR) and the Arab League, and Peru signed a commercial and technical agreement with the Gulf Cooperation Council (comprising Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates).<sup>13</sup>

## **Poverty Decreasing, Economic Disparity Still High**

García, during his second (non-consecutive) five-year term, largely continued the orthodox economic policies of his predecessor, Alejandro Toledo, concentrating on reducing the fiscal deficit. The U.S. State Department described Peru's economy as "well managed" under García, and maintained that better tax collection and growth were increasing revenues.<sup>14</sup> President Humala has followed suit, appointing a conservative economic team that is continuing existing free-market economic and trade policies. He also insists, however, that he will enact policies to eradicate poverty by spreading Peru's wealth to the country's poorest population. President Humala has maintained that "Economic growth and social inclusion will march together," and that he will expand social programs to reduce the number living in poverty.<sup>15</sup>

Peru's rapid and sustained economic growth has substantially reduced poverty and increased employment. Peru's poverty rates have been dropping since 2000. The percentage of Peruvians living in poverty fell from 54.3% in 2001 to 31.3% in 2010.<sup>16</sup> Peruvians living in extreme poverty, unable to purchase the most basic basket of necessities, fell from 24.1% to 9.8% during the same period. Social unrest has continued to rise in recent years, however, as Peru's poor have felt that the country's economic prosperity has not reached them. Indeed, the percentage of the population living in poverty in some mountain, jungle, and rural areas is over 60%. The disparity between rural and urban populations remains marked: as of 2010 over half (54.2%) of the rural

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<sup>11</sup> "Country Report: Peru," *Economist Intelligence Unit*, October 2012.

<sup>12</sup> The EFTA is composed of Iceland, Lichtenstein, Norway, and Sweden.

<sup>13</sup> Diego Moya-Ocampos, "Third South American-Arab Countries Summit Issues Declaration," *IHS Global Insight Daily Analysis*, October 3, 2012, and "Peruvian President Expects Arab Countries' Investments Following Summit," *IHS Global Insight Daily Analysis*, October 4, 2012.

<sup>14</sup> Bureau of Western Hemisphere Affairs, U.S. Department of State, *Background Note: Peru*, May 2009, <http://www.state.gov/r/pa/ei/bgn/35762.htm>.

<sup>15</sup> "Ollanta Humala is Sworn In As New Peru President," *BBC News*, July 28, 2011; "Peru's Humala Renews Poverty Vow after Year in Office," *BBC News*, July 28, 2012.

<sup>16</sup> Poverty figures in this section from: Organization of American States, *Peru's Foreign Minister Trusts in a Fair Electoral Process in his Country*, Press Release E-290/05 (citing UN Economic Commission for Latin America and Caribbean figures), December 14, 2005; World Bank, *Peru Country Brief*, May 18, 2009, pp. 1-3, <http://go.worldbank.org/AHUP42HWR0>; and The World Bank, *Peru: Brief*, September 19, 2011, April 4, 2012; and World dataBank at <http://databank.worldbank.org>, April 4, 2012.



population lives in poverty, while 19.1% of the urban population does so. The income distribution gap remains significant: the top 20% of the population garners 52.6% of the nation's income, while the lowest 20% garners only 3.9% of the income. According to the World Bank, "poverty rates are still high for a country with income levels like Peru's."

Similarly, the factors weighed in the World Bank Human Opportunity Index, which measures "how personal circumstances (birthplace, wealth, race or gender) impact a child's probability of accessing the services that are necessary to succeed in life" (timely education, running water, sanitation, electricity), have improved greatly in Peru since 1995, but remain significantly lower for Peru's poorer population as compared to the wealthier population.<sup>17</sup> Overall, for example, chronic malnutrition among children under the age of five declined from 28.5% in 2007 to 23.2% in 2010. But among the poorest 20% of the country's population, 47% of children displayed stunting from malnutrition, as opposed to only 5% of children among the wealthiest quintile. The infant mortality rate was 64 deaths per 1,000 live births among the poorest quintile, and 14 per 1,000 among the wealthiest quintile. On the 2010 World Bank Human Opportunity Index, Peru scores about 70 on a scale of 100 for universal access to services. It compares poorly to the rest of Latin America, however, ranking 14<sup>th</sup> out of 18 countries.

As mentioned above, President Humala and the Peruvian Congress have already approved an increase in mining royalties expected to generate US\$1.1 billion a year to fund social development programs aimed at closing that social and economic distribution gap. The President also announced an increase in the minimum wage and a minimum pension to poor people over age 65. His administration proposed, and in March 2012 the legislature passed, a law to expand natural gas use, especially for low-income sectors.

## **Challenges of Funding and Managing Social Development Programs**

According to the Economist Intelligence Unit, "several years' worth of large surpluses" provided ample finance for the García administration's social policies, but implementation of those policies was hampered by the limited capacity of Peru's institutions.<sup>18</sup> The same holds true for the Humala administration, which faces the challenge of making the government more effective in order to continue and expand the positive trends of the past decade.

A case in point where increased effectiveness is needed is that of the Camisea natural gas project. Peru began to decentralize government functions in earnest in 2002. Some analysts reported that provincial and local governments were therefore not prepared, only two years later, to absorb the \$1.13 billion in revenue generated by the Camisea project that the national government transferred to them between 2004 and 2009.<sup>19</sup> The nascent sub-national governments appear to have lacked the skills to manage the social and environmental risks, resulting in reported damage to many indigenous communities, their livelihoods, and their ecosystems. The governments also reportedly lacked the fiscal management skills to marshal the funds effectively, and poverty in

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<sup>17</sup> Socioeconomic information in this section drawn from The World Bank, *Peru: Brief*, September 16, 2011; and World Data Bank at <http://databank.worldbank.org>; quintile data is from 2000, Oct. 19, 2011 and April 4, 2012.

<sup>18</sup> Economist Intelligence Unit (EIU), *Country Report: Peru*, London, May 2009, pp. 3, 4, 15.

<sup>19</sup> World Resources Institute, Bank Information Center, Oxfam, "People, Power, and Pipelines: Lessons from Peru in the governance of gas production revenues," June 16, 2010.

those areas remained as high as 60%. U.S. assistance programs help provide training and technical assistance to sub-national (and national) institutions to plan and manage social services, improve citizen access to information, and prevent and mitigate conflict.

## **Debate over Exploitation of Natural Resources**

Social unrest and debate over exploitation of natural resources is likely to remain a challenge for the Humala government. Work at the Conga gold and copper mine in Cajamarca, in northern Peru, has been suspended since late November 2011 due to violent protests there. Opponents worry that the \$5 billion project—the country’s largest foreign investment project ever—will contaminate water resources that provide the region’s water for drinking and agriculture by draining lagoons and filling them with mining waste. Many residents of the dairy and agricultural region say they want sustainable development based on agriculture and eco-tourism instead.

The government hired a team of international experts to reassess the project’s environmental impact assessment, which the García administration had approved in 2010. After receiving the report on April 17, 2012, President Humala imposed additional conditions on the project, and Cajamarca’s regional president, Gregorio Santos Guerrero, continues to oppose it. A group of civil society groups announced that they would proceed with a mass strike unless the president declared the project “un-viable.”<sup>20</sup> The company involved, Yanacocha, whose U.S. parent company is Newmont Mining, is considering the new requirements. The mining consortium says that it will carry out its work in an environmentally sensitive way, and correct errors made in the past.<sup>21</sup> Investors see the outcome of the case as an important indicator of Peru’s business environment.<sup>22</sup> Four other regions are experiencing protests against mining and energy projects as well.

## **Peru’s Relations with its Neighbors**

Peru generally has friendly relations with its South American neighbors, although tensions with Chile arise occasionally. Peru’s Congress triggered renewed tensions in 2005 when it declared new maritime borders; Chile claims that the maritime borders had been agreed to in fishing pacts signed in the early 1950s. In 2008 the García administration asked the International Court in the Hague to arbitrate the dispute; the oral stage of the process is scheduled to begin in December 2012. Peru’s chancellor, Rafael Roncagliolo, says Peru wants “to maintain the most peaceful relations possible with Chile” during the process.<sup>23</sup>

Actions on both sides of the border led to tensions again in 2009. Chile conducted multinational military exercises that rankled Peru, and Peru arrested a member of its Air Force for allegedly

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<sup>20</sup> “Cool Response to Peru Government’s Conga Review,” *Latin News Daily Report, Daily Briefing*, April 24, 2012, Main Briefing.

<sup>21</sup> Ibid.

<sup>22</sup> “Resource Nationalism: Conga’s Outcome to Set Precedent for Future Mining Projects in Peru,” *American Metal Market*, March 25, 2012.

<sup>23</sup> EFE, “Perú Afirma Que Quiere ‘Relaciones Serenas Y Libres De Tensiones’ Con Chile,” <http://www.emol.com/noticias/internacional/2012/04/23/537105/peru-afirma-que-quiere-relaciones-serenas-y-libres-de-tensiones-con-chile.html>, April 23, 2012.

spying and providing classified defense information to Chile.<sup>24</sup> During the presidential campaign, Humala made inflammatory remarks regarding Chile, demanding Chile apologize to Peru for assaults during the War of the Pacific in 1879 and warning Chile not to discriminate against Peruvians residing in Chile, or Peru would do the same against Chileans within its borders.<sup>25</sup> Shortly after he was elected, however, Humala traveled to Chile, saying he wanted to get relations between the two countries off on a good foot.

Peru and Ecuador resolved their sometimes violent border disputes by signing a peace accord in 1998, of which the United States was one of four guarantor states. Peru and Ecuador coordinate a border integration project with U.S. and other international support.

Peru is a member of the Union of South American Nations (UNASUR), which seeks the “equitable, harmonious, integrated development of South America.”<sup>26</sup>

Peru joined the Asia-Pacific Economic Cooperation (APEC) in 1998, which promotes economic relations between Peru and Asian countries. Peru is an active member, hosting the APEC summit in 2008.

A member of the United Nations since 1949, Peru was a member of the Security Council in 2006 and 2007. Peruvian diplomat Javier Pérez de Cuellar served two terms as U.N. Secretary General from 1982 to 1991. About 200 Peruvian troops participate in peacekeeping operations as part of the U.N. Stabilization Mission in Haiti.<sup>27</sup>

## **Relations with the United States**

Peru and the United States have a strong and cooperative relationship. The United States supports the strengthening of Peru’s democratic institutions and its respect for human rights. The two countries also cooperate on environmental protection and counternarcotics efforts. In the economic realm, the United States supports bilateral trade relations and Peru’s further integration into the world economy. President-elect Humala met with Secretary of State Hillary Clinton and President Barack Obama in Washington in early July 2011. Humala said he wished to further strengthen ties between the two countries, and Clinton said that “the United States stands ready to be his partner.”<sup>28</sup> Presidents Obama and Humala met briefly at the Summit of the Americas on April 14, 2012, in Cartagena, Colombia.

U.S. Defense Secretary Leon Panetta met with President Humala and Defense Minister Pedro Cateriano in Peru on October 6, 2012. The officials said the two militaries cooperate in areas including humanitarian assistance, such as joint disaster response training; internal security; defense reform; U.N. peacekeeping; and regional security, and they discussed further collaboration. Panetta said the United States was prepared to work with Peru “on joint planning,

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<sup>24</sup> U.S. Dept. of State, *Background Note: Peru*, January 3, 2012, <http://www.state.gov/r/pa/ei/bgn/35762.htm>.

<sup>25</sup> AP, “Canciller peruano: Victoria de Ollanta Humala no perjudicaría relaciones con Chile,” <http://www.emol.com/noticias/internacional/2011/04/06/474590/canciller-peruano-victoria-de-ollanta-humala-no-perjudicaria-relaciones-con-chile.html>, April 6, 2011.

<sup>26</sup> UNASUR, <http://www.comunidadandina.org/sudamerica.htm>.

<sup>27</sup> U.S. Dept. of State, *Background Note: Peru*, op. cit.

<sup>28</sup> Diego Urdaneta, “Peru President-Elect Meets Obama, Clinton,” *AFP*, July 6, 2011.

information sharing [and] trilateral cooperation with Colombia to address our shared security concerns in this area,” and on updating their Defense Cooperation Agreement, which dates from 1952, to improve cooperation.<sup>29</sup> The officials also reportedly discussed Peru’s desire to acquire 20 U.S. helicopters, and to use counternarcotics resources for counterinsurgency efforts as well.<sup>30</sup> (See “Counternarcotics Efforts” below.)

## **U.S. Assistance and Congressional Interests**

According to the Department of State, the goals of U.S. assistance to Peru are to help it consolidate democratic rule, invest in its people, combat narcotics trafficking and terrorism, and reform state institutions to improve public infrastructure and service delivery.<sup>31</sup> Congress has supported these goals through appropriated funding. Nonetheless, funding for Peru has been declining since at least FY2010, when the United States provided almost \$120 million in assistance to Peru. Funding decreased to \$97 million in FY2011. Total funding for FY2012 is estimated to be \$84 million, including \$45 million for Development Assistance; about \$2 million for Foreign Military Financing; \$5 million for USAID Global Health Programs; \$620,000 for International Military Education and Training; \$29 million for International Narcotics Control and Law Enforcement; and \$2 million for Nonproliferation, Antiterrorism, Demining and Related Programs.

Congress designated funding to Peru as part of several other regional programs. In the Consolidated Appropriations Act of 2012 (P.L. 112-74), Congress stipulated that “not less than” \$10 million of Development Assistance, and “not less than” \$10 million of Economic Support Funds shall be made available for Peru, Central American countries, and the Dominican Republic for labor and environmental capacity building activities relating to free trade agreements with the United States. In its Joint Explanatory Statement, Congress said that \$10 million should be made available for biodiversity conservation programs in the Andean Amazon region.<sup>32</sup>

The Obama Administration requested \$74 million for Peru for FY2013, a decrease of almost \$10 million from FY2012. The FY2013 request includes \$47 million for Development Assistance; about \$2 million for Foreign Military Financing; \$585,000 for International Military Education and Training; \$23 million for International Narcotics Control and Law Enforcement; and \$500,000 for Nonproliferation, Antiterrorism, Demining and Related Programs.

Peru and the United States signed a \$35.6 million Millennium Challenge Threshold program for 2008 to 2010 that supported Peru’s efforts to reduce corruption in public administration and improve child immunization coverage. The program, implemented by the U.S. Agency for International Development (USAID), was extended to July 2011. The nationwide immunization program is completed. To allow the completion of one remaining anti-corruption program, the Millennium Challenge Corporation (MCC) has extended the end date until September 2012. No

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<sup>29</sup> Department of Defense, *FDCH Regulatory Intelligence Database*, October 6, 2012.

<sup>30</sup> Diego Moya-Ocampos, “Peru Considers Satellite Monitoring for Coca Region,” *IHS Global Insight Daily Analysis*, October 15, 2012.

<sup>31</sup> U.S. Dept. of State, *Peru: Foreign Assistance Program Overview*, Congressional Budget Justification, Foreign Operations, Annex: Regional Perspectives, Fiscal Year 2012.

<sup>32</sup> Joint Explanatory Statement for Consolidated Appropriations Act of 2012, P.L. 112-74, [http://rules.house.gov/Media/file/PDF\\_112\\_1/legislativetext/HR2055crSOM/psConference%20Div%20I%20-%20SOM%20OCR.pdf](http://rules.house.gov/Media/file/PDF_112_1/legislativetext/HR2055crSOM/psConference%20Div%20I%20-%20SOM%20OCR.pdf)

FY2013 funding for MCC programs is expected. These activities will be incorporated into USAID programs for the remainder of FY2012 and probably into FY2013.

**Table 1. U.S. Assistance to Peru by Account and Fiscal Year**

(\$ in thousands)	Fiscal Year			FY2012-13 Increase / Decrease
	2011 Actual	2012 Estimate	2013 Request	
<b>TOTAL</b>	<b>96,581</b>	<b>83,550</b>	<b>73,665</b>	<b>-9,885</b>
Development Assistance	49,789	45,000	47,300	2,300
Foreign Military Financing	3,500	1,980	1,980	-
Global Health Programs - State	50	-	-	-
Global Health Programs - USAID	9,123	5,000	-	-5,000
International Military Education and Training	619	620	585	-35
International Narcotics Control and Law Enforcement	31,500	28,950	23,300	-5,650
Nonproliferation, Antiterrorism, Demining and Related Programs	2,000	2,000	500	-1,500

**Source:** Congressional Budget Justification, Foreign Operations, Fiscal Year 2013.

## Counternarcotics Efforts

A dominant theme in the relations between the two countries is the effort to stem the flow of illegal drugs, mostly cocaine, from Peru to the United States. Peru is one of the three Andean countries that produce virtually all of the world's coca. According to the State Department, Peru "has the world's highest potential production of pure cocaine."<sup>33</sup> Estimates of Peru's total area of coca production vary widely. According to the United Nations Office on Drugs and Crime, the area remained fairly stable in 2010, increasing by only 2% over the previous year, from almost 60,000 hectares in 2009 to just over 61,000 hectares in 2010. The U.S. government, using a different methodology, estimated that 40,000 hectares were under cultivation in Peru in 2009, and 53,000 hectares in 2010, constituting a 33% increase. Within the country, there have been significant changes in production. The upper Huallaga valley, formerly the country's largest producer of coca, experienced a strong drop in cultivation, due mostly to intensive eradication there. Producing almost a third of the country's coca, the valley of the Apurimac and Ene rivers, known as the VRAE region, is now Peru's largest coca cultivating region. Other areas, such as the Marañon, Putumayo, and parts of the Amazon basin increased their coca production by as much as 90%. According to the State Department, 93% of the coca grown in Peru is illegal and intended for cocaine production. The rest is for traditional domestic consumption. The State Department also reports that Peru is a major importer of precursor chemicals that are used to produce cocaine.

The cultivation of coca and production of cocaine has contributed to social problems in Peru. Coca eradication is highly controversial in Peru, with coca farmers violently resisting it. Some

<sup>33</sup> This and other figures in this section are from U.S. Dept. of State, Bureau for International Narcotics and Law Enforcement, *International Narcotics Control Strategy Report [INCSR], Peru*, vol. I, Drug and Chemical Control, March 2012, and March 2011, unless indicated otherwise.

coca farmers have become allied with remnants of the Shining Path terrorist organization. Now closely linked with narcotics trafficking, the Shining Path conducted 136 terrorist acts in 2010, killing civilians and members of the police and military.<sup>34</sup> Drug addiction has become a serious problem, with an estimated 150,000 addicts across the country, but an insufficient number of treatment and rehabilitation centers to treat them. Illicit coca cultivation and production has damaged the environment, contributing to the deforestation of 2.5 million hectares over 30 years, and the pollution of forests and streams from 118 million liters of precursor chemicals dumped in them over a period of 5 years.

U.S. counternarcotics programs in Peru focus on three areas: eradication, interdiction, and alternative development. The Obama Administration's request for FY2013 includes a total of \$47 million in counternarcotics funding, consisting of \$25 million in development assistance and \$22 million in International Narcotics Control and Law Enforcement (INCLE) funds.<sup>35</sup> According to the 2011 INCSR, from 2009 to 2010 alternative development programs led to a 24% increase in the legal incomes of participating families, and to a 25% decrease in their level of poverty.

The Peruvian government released a new national drug plan in November 2011. It focuses on combating organized crime, trafficking in narcotics and precursor chemicals, money laundering, and financial crimes; and on increasing or improving drug-use prevention, rehabilitation, eradication, and alternative development. When he took office, President Humala said he was reevaluating Peru's counternarcotics policy, and also that he saw the United States as a "strategic partner" in combating illegal drug production and trafficking.<sup>36</sup> The United States has required total eradication of coca before a farmer can enter into alternative development programs in Peru; critics say farmers should be allowed to make a gradual transition to alternative crops so that they maintain a source of income. When the Humala administration stopped eradication shortly after assuming office, many observers thought it indicated a major shift in policy, especially considering that Humala had support from coca growers in his campaign. But the Humala administration quickly resumed eradication in August 2011, and soon removed the officials he had initially placed in charge of counter-narcotics policy, some said out of concern their policies might antagonize the United States.<sup>37</sup>

In September 2011, President Humala declared a 60-day state of emergency in several coca-producing areas with a Shining Path presence. These areas were also the site of protests by coca farmers opposed to the government's forced eradication of their crops. Days after the state of emergency was declared, the defense minister announced that the military was going to "take total control of the VRAE."<sup>38</sup> According to the government, the military intervention to re-take control of the region was to be coupled with the development of infrastructure such as roads, communications, schools, and hospitals by army engineers. Nonetheless, the imposition of full military control of the area for the first time since the administration of former President Alberto Fujimori, now imprisoned for human rights violations and other crimes, raises concerns for many

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<sup>34</sup> U.S. Dept. of State, Office of the Coordinator for Counterterrorism, *Country Reports on Terrorism 2010, Peru*, Washington, DC, August 18, 2011, <http://www.state.gov/s/ct/rls/crt/2010/170259.htm>.

<sup>35</sup> U.S. Dept. of State, *Congressional Budget Justification, Foreign Operations, Fiscal Year 2012*, Annex: Regional Perspectives, Peru, Washington, DC, pp. 814-815, <http://www.state.gov/documents/organization/137937.pdf>.

<sup>36</sup> "Ollanta Humala is Sworn in as New Peru President," *BBC News: Latin America and Caribbean*, July 28, 2011.

<sup>37</sup> "Humala Stops Rocking the Boat," *Latin American Weekly Report*, vol. WR-12-02 (January 12, 2012).

<sup>38</sup> "Peru: Security; Militarisation of the Vrae - Then and Now," *Latin American Weekly Report*, vol. WR-11-38, September 22, 2011, p. 4.

over human rights and development issues. Protests over coca eradication are expected to continue.

Securing the VRAE is complicated by the presence there of remnants of the Shining Path (Sendero Luminoso) insurgency movement, who reportedly operate alongside local drug traffickers. A Shining Path faction killed two police agents and injured two others on October 14, 2012. In response, the Humala Administration said it planned to monitor the Shining Path via satellite, and was in discussions with U.S. officials to allow helicopters provided by the U.S. for counter-narcotics operations to be used for counterinsurgency operations as well.<sup>39</sup>

## **Trade and Environment**

The United States is one of Peru's top trading partners. Of Peru's \$46 billion in exports in 2011, almost 12.76% went to the United States; Peru exported more to China (15%) and Switzerland (12.9%). Almost 20% of Peru's imports came from the United States.<sup>40</sup> Both the executive branch and Congress have promoted trade with Peru, and protection of its environment, often linking the two. The U.S.-Peru Trade Promotion Agreement (PTPA) went into effect February 1, 2009. Congress passed environmental amendments to the PTPA that commit Peru (and the United States) to enforce its domestic environmental laws, and adopt new laws to fulfill obligations under multilateral environmental agreements. Other amendments to the PTPA call for the two countries to take steps to enhance forest sector governance and promote legal trade in timber products.

On April 17, 2012, a conservation non-profit organization invoked those amendments in petitioning the U.S. Trade Representative to investigate and verify the legal origin of wood shipments from Peru.<sup>41</sup> An Environmental Investigation Agency (EIA) report indicated that millions of dollars worth of illegal wood from the Peruvian Amazon were exported to the United States between 2008 and 2010.<sup>42</sup> If the U.S. government finds evidence of illegality, it can take actions, including prohibiting the companies involved from exporting to the United States until Peru produces evidence that each company is complying with the law and regulations. EIA noted that Peruvian agencies are exercising greater oversight over the industry; to conduct its analysis, the group used data from a government agency it said was reformed and strengthened under provisions of the PTPA.

As mentioned above, Congress stipulated in the FY2012 appropriations law that both Development Assistance and Economic Support Funds shall be made available for Peru for labor and environmental capacity building activities relating to free trade agreements with the United States. In its Joint Explanatory Statement, Congress said that \$10 million should be made available for biodiversity conservation programs in the Andean Amazon region.

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<sup>39</sup> Diego Moya-Ocampos, "Peru Considers Satellite Monitoring for Coca Region," *IHS Global Insight Daily Analysis*, October 15, 2012.

<sup>40</sup> U.S. Dept. of Commerce, Bureau of Census, via Global Trade Atlas, April 25, 2012.

<sup>41</sup> Andrea Johnson and Fiona Mulligan, *US Government Requested to Use Free Trade Agreement to Take Action on Illegal Timber Exports from Peru; Environmental Organization Submits Formal Petition To US Trade Representative With Evidence On Dozens Of Shipments In Violation Of International Laws and US-Peru FTA*, Environmental Investigation Agency, press release, Washington, DC, April 19, 2012.

<sup>42</sup> "NGO Alleges Illegal Logging Shipments from Peru; Will urge USTR to Act," *Inside U.S. Trade*, vol. 30, no. 15 (April 13, 2012).

In 2009 the United States announced it would be entering into an Asia-Pacific trade agreement known as the Trans-Pacific Partnership (TPP). Peru is one of the negotiating partners. According to the USTR, the TPP will be “a means to advance U.S. economic interests with the fastest-growing economies in the world, and a tool to expand U.S. exports.”<sup>43</sup> Critics assert that any economic benefits deriving from the agreement “will be relatively small and the regulatory costs could be significantly high—especially for the emerging market and developing countries engaged in the negotiations.”<sup>44</sup>

Peru and the United States signed a debt-for-nature swap in 2008 that reduces Peru’s debt to the United States by more than \$25 million over seven years, until 2015. In exchange, Peru agreed to use those funds to support grants to protect its tropical forests.

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<sup>43</sup> U.S. Trade Representative, *2012 National Trade Estimate Report on Foreign Trade*, Peru, 2012, p. 307.

<sup>44</sup> Kevin Gallagher, *Bamboozled by the TPP: The Small Benefits and Real Costs of the Trans-Pacific Partnership Agreement*, Global Development and Environment Institute, Tufts University, Globalization Commentaries, Medford, MA, January 23, 2012. For further information on the TPP, see CRS Report R40502, *The Trans-Pacific Partnership Agreement*, by Ian F. Fergusson and Bruce Vaughn.