INFLATION REPORT

December 2013

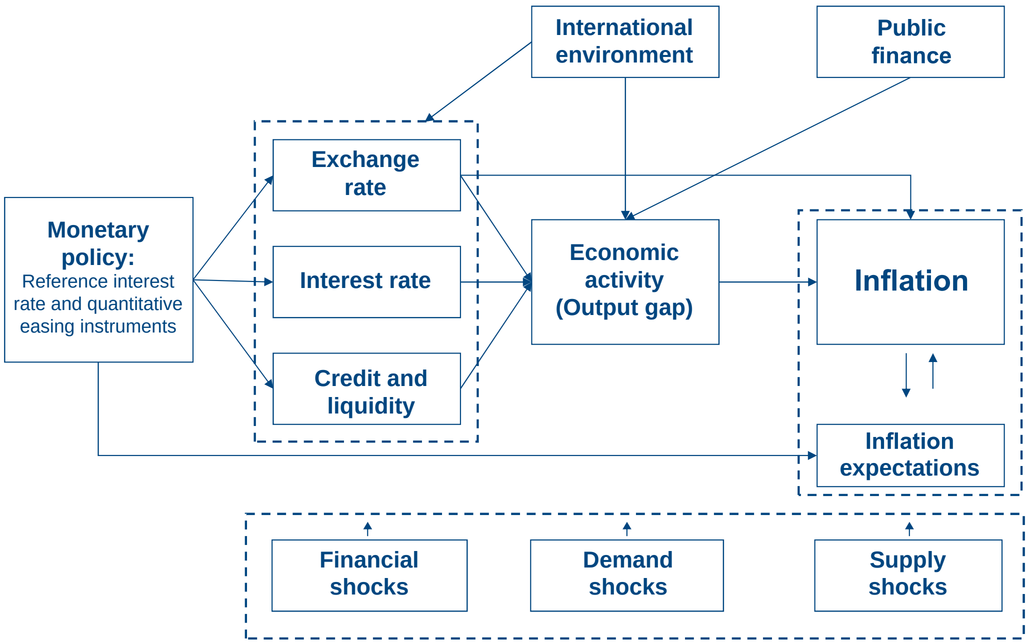
Recent trends and macroeconomic forecasts 2013-2015

CENTRAL RESERVE BANK OF PERU

INFLATION REPORT:

Recent trends
and macroeconomic forecasts 2013-2015

December 2013



Central Reserve Bank of Peru
441-445 Antonio Miro Quesada. Lima 1
Telephone: 613-2000 - Fax: 613-2525
Mail: webmaster@bcrp.gob.pe

INFLATION REPORT
Recent trends and macroeconomic forecasts

CENTRAL RESERVE BANK OF PERU

INFLATION REPORT:

Recent trends and macroeconomic forecasts 2013-2015

December 2013

CONTENT

	Pag.
Foreword	5
Summary	6
I. International environment	9
II. Economic activity	31
III. Balance of payments	52
IV. Public finances	66
V. Monetary policy	77
VI. Inflation	104
VII. Balance of risks	117
Conclusion	118

BOXES

1. The Fed's monetary stimulus	26
2. Competitiveness and business climate in Peru	49
3. Modification of the macro fiscal framework	75
4. The monetary policy interest rate and reserve requirements	100

This ***Inflation Report*** was drawn up using data on the balance of payments and the gross domestic product as of the third quarter of 2013, and data on the operations of the non-financial public sector, monetary accounts, inflation, financial markets, and the foreign exchange rate as of November 2013.

Foreword

- In accordance with the Peruvian Constitution, the Central Reserve Bank of Peru (BCRP) is a public autonomous entity whose role is to preserve monetary stability.

- In order to consolidate this goal, the Bank's monetary policy is based on an inflation targeting scheme, with an inflation target of 2.0 percent, plus or minus one percentage point (between 1.0 and 3.0 percent). The Central Bank's inflation target is aimed at anchoring inflation expectations at a similar level to the inflation rate observed in developed economies and reflects the BCRP's permanent commitment with monetary stability.

- The nature of monetary policy is preventive and therefore aimed at anticipating inflationary or deflationary pressures, taking into account that inflation may be influenced by factors beyond the control of the Central Bank, such as supply shocks or the prices of imported products, which may result in transitory deviations of inflation from the target. The BCRP considers the annual increase in the consumer price index recorded each month and not only at year end.

- Each month, and according to a previously announced schedule, the Board of the BCRP approves a reference rate for the interbank lending market. This interest rate, which is the monetary operational target, affects the rate of inflation through several channels in different timeframes and, therefore, it is determined on the basis of macroeconomic forecasts and simulations.

- Additionally, the Central Bank implements preventive measures to preserve financial stability and monetary policy transmission mechanisms. Through interventions in the foreign exchange market, the Central Bank reduces excessive volatility in the exchange rate and accumulates international reserves, thus developing strengths to face negative events in an economy with still high levels of financial dollarization. The Central Bank also uses other monetary policy tools that affect the volume of liquidity and credit in a more direct manner, such as reserve requirements in domestic currency and in foreign currency, in order to avoid excessive credit or credit constraints.

- The forecasts on which monetary policy decisions are based are disseminated through the Inflation Report to show the consistency of the decisions adopted with the aim that economic agents' expectations take these forecasts into account. The Central Bank also disseminates the studies analyzing the risk factors that may cause deviations in the forecasts of the economic variables considered. The world economy has maintained a moderate pace of growth so far this year and a more widespread recovery is estimated for 2014 and 2015. The world GDP would grow 2.9 percent in 2013, 3.6 percent in 2014, and 3.8 percent in 2015.

Summary

i. The **world economy** has maintained a moderate pace of growth so far this year and a more widespread recovery is estimated for 2014 and 2015. The world GDP would grow 2.9 percent in 2013, 3.6 percent in 2014, and 3.8 percent in 2015.

ii. Between January and October, Peru's **gross domestic product** grew 4.9 percent, less than in the same period of 2012. Domestic demand registered a growth rate of 6.0 percent, a higher rate than the GDP.

The GDP growth rate projected for 2013 has been revised down from 5.5 percent (September Report) to 5.1 percent. This is explained by the lower dynamism of domestic demand, associated mainly with the deterioration of investment expectations, and the downward revision of the forecast of global growth.

The GDP growth forecasts for 2014 and 2015 have been revised down from 6.2 to 6.0 percent and from 6.7 to 6.5 percent, respectively. A faster pace of growth would be observed in 2015 due to the onset of operations in some investment projects, mainly in the mining sector.

iii. In the period of January-September, the **balance in the current account** of the balance of payments showed a deficit equivalent to 5.4 percent of GDP, higher than the one observed in the same period of 2012, in a context in which investment grew at a higher rate than domestic savings and terms of trade declined. In this period the deficit was financed by long-term capital inflows (US$ 18.3 billion) –a higher flow than the one recorded in the first three quarters of 2012– associated with mining, energy and hydrocarbons projects.

The current account deficit is still estimated at 4.9 percent of GDP in 2013 and at 4.6 percent of GDP in 2014, and a deficit of 4.2 percent of GDP is projected for 2015 in a context of a slight decline in the terms of trade. The declining path foreseen in the deficit considers the onset of operations of several mining projects in 2014 and 2015 (Toromocho, Las Bambas, and Constancia).

iv. A declining path in the **surplus of the non-financial public sector** is still considered in the fiscal scenario. The surplus would decline from 2.1 percent of GDP in 2012 to a nil balance in 2015, with ratios of 0.6 percent of GDP in 2013 and 0.1 percent of GDP in 2014. Thus, an expansionary fiscal impulse would be observed this year and next year.

v. The Board of the Central Bank decided to lower the monetary policy **benchmark interest rate** from 4.25 percent to 4.00 percent in November 2013, after maintaining this rate at this level since May 2011. The Board's decision is based on

the fact that inflation is foreseen to return to the target range after the reversal of the supply factors that have transitorily increased the rate of inflation.

vi. Additionally, since May 2013 the BCRP has implemented measures to ease reserve requirements in order to ensure an orderly evolution of credit in domestic currency.

vii. In November **inflation** in the last 12 months showed a rate of 2.96 percent, within the target range. The central forecast scenario considers that inflation will remain within the target range and that it will gradually converge to the 2.0 percent target. This scenario considers that there would be no major inflationary pressures associated with increases in the prices of commodities and that monetary policy actions would maintain inflation expectations anchored within the target range. Thus, the inflation forecast for 2014-2015 is that the rate of inflation will be around 2.0 percent.

viii. The **downward risks** in the inflation forecast are, on the one hand, external factors associated with the possibility that volatility may return to international financial markets and with a slower pace of growth in many economies, and, on the other hand, internal factors associated with a slower pace of recovery in domestic demand due to the postponement of some investment projects.

On the other hand, the **upward risk** for inflation is associated mainly with the increase in fuel prices due to geopolitical factors, although this risk has declined significantly compared to the situation in our previous report.

ix. The **balance of these risks results in a negative bias** in the inflation forecast; therefore, the probability that inflation is lower than the projected rate of around 2 percent in the 2014 - 2015 horizon is greater than the probability of it being higher than this rate.

FORECAST SUMMARY

	2012	2013 1/		2014 1/		2015 1/	
		IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
Real % change							
1. GDP	6.3	5.5	5.1	6.2	6.0	6.7	6.5
2. Domestic demand	7.3	6.5	5.8	6.1	6.0	6.3	6.1
a. Private consumption	5.8	5.2	5.2	5.3	5.2	5.4	5.4
b. Public consumption	9.4	7.6	5.5	4.0	6.3	4.2	4.2
c.,Private fixed investment	13.5	7.7	4.3	7.7	6.3	7.9	6.6
d. Public investment	20.8	16.3	18.1	17.0	15.5	14.6	14.6
3. Exports (goods and services)	5.4	0.7	1.5	9.3	6.3	11.4	10.9
4. Imports (goods and services)	10.4	6.3	5.5	7.9	6.3	8.6	7.9
5. Economic growth in main trading partners	2.9	2.4	2.5	3.1	3.1	3.4	3.3
Memo:							
Output gap 2/ (%)	0.5	-1.0 ; +1.0	-1.0 ; +1.0	-0.5 ; +0.5	-0.5 ; +0.5	-0.5 ; +0.5	-0.5 ; +0.5
% change							
6. Forecast inflation	2.6	2.5-3.5	2.5-3.0	1.5-2.5	1.5-2.5	1.5-2.5	1.5-2.5
7. Average price of crude oil	-1.0	5.9	3.6	-2.4	-0.8	-7.6	-3.1
8. Nominal exchange rate 3/	-4.8	9.1	9.1	0.8	2.0	1.2	0.4
9. Real multilateral exchange rate 3/	-7.4	6.1	6.2	0.3	1.7	1.6	0.5
10. Terms of trade	-5.0	-4.5	-4.7	-1.6	-2.2	0.1	-0.1
a. Export price index	-3.3	-6.2	-7.3	-1.9	-4.5	0.9	0.3
b. Import price index	1.7	-1.8	-2.8	-0.3	-2.4	0.8	0.4
Nominal % change							
11. Currency in circulation	18.3	15.7	13.0	13.2	12.7	11.9	11.9
12. Credit to the private sector 4/	15.5	12.2	14.5	12.4	13.5	12.0	12.0
% GDP							
13. Gross fixed investment rate	26.6	28.0	27.5	29.0	28.2	29.8	28.6
14. Current account of the balance of payments	-3.4	-4.9	-4.9	-4.6	-4.6	-4.1	-4.2
15. Trade balance	2.4	-0.3	-0.2	0.1	0.0	1.0	0.7
16. Gross external financing to the private sector 5/	10.5	10.0	10.3	7.2	6.4	6.4	6.2
17. Current revenue of the general government	21.6	21.3	21.7	21.3	21.6	21.4	21.7
18. Non-financial expenditure of the general government	18.6	20.0	20.2	20.2	20.5	20.4	20.7
19. Overall balance of the non-financial public sector	2.1	0.4	0.6	0.1	0.1	0.0	0.0
20. Total public debt balance	19.7	18.1	18.1	17.4	17.2	16.5	16.4

IR: Inflation Report.
1/ Forecast
2/ Differential between GDP and potential GDP (%).
3/ Survey on exchange rate expectations.
4/ Includes loans made by banks' branches abroad.
5/ Includes foreign direct investment and private sector's long term disbursement.

I. International Environment

1. Since our last Inflation Report was published in September, the world economy has continued to show a moderate recovery. The developed economies have recorded on average a growth rate close to 2 percent while the growth rates in the emerging economies have stabilized after the slowdown observed in the first half of the year. Factors contributing to this include the recovery of international trade and resuming normal international financial conditions to some extent.

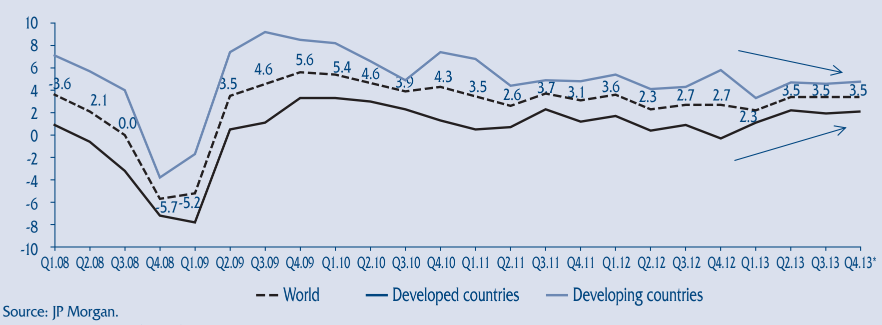
   In line with these developments, global growth is estimated to register a rate of 2.9 percent in 2013 and to show a recovery in 2014 (3.6 percent) and 2015 (3.8 percent). This forecast considers that international financial markets will experience an orderly correction after the reduction of monetary stimulus announced by the U.S. Federal Reserve at its meeting of December 17-18 and that the U.S. Congress will reach an agreement on the debt limit. The forecast also considers that the larger emerging economies will maintain growth rates similar to the ones recorded in 2013, in line with the evolution observed in their main economic indicators.

   Under these assumptions, after decreasing by 4.7 percent in 2013, the terms of trade would show a lower correction in 2014 stabilizing thereafter in the following year.

Global economic activity

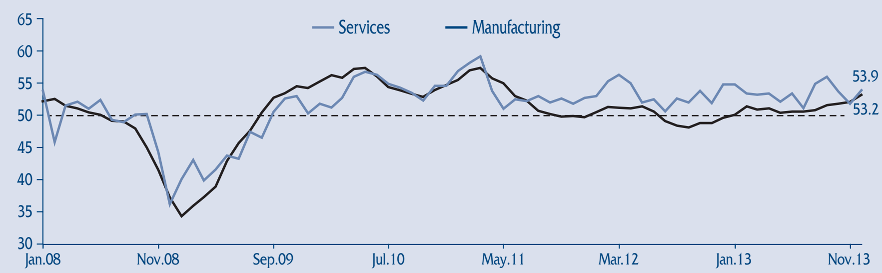
2. It is estimated that the rate of global growth in Q4 is about 3.5 percent. In recent months, the purchasing managers indexes (PMI) for manufacturing and services have remained in the expansion area and thus register 12 and 52 consecutive months of growth, respectively.

Graph 1
GDP: SEASONALLY ADJUSTED QUARTERLY GROWTH
(% annualized rates)



Source: JP Morgan.
* Forecast (December 13, 2013).

Graph 2
JP MORGAN GLOBAL PMI INDEX
(January 2007 - November 2013)



Source: Bloomberg.

3. In line with these developments, it is estimated that global growth will register a rate of 2.9 percent in 2013, a similar rate to the one forecast in our September report. A recovery supported by the improvement of activity in both the developed countries and emerging economies would be observed in 2014 with an estimated rate of 3.6 percent. Moreover, a global growth rate of 3.8 percent is estimated for 2015.

Table 1
WORLD GDP GROWTH
(Annual % change)

	%	Executed		2013		2014		2015	
	2011	2011	2012	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
Developed countries	**51.2**	**1.7**	**1.5**	**1.1**	**1.2**	**2.0**	**2.1**	**2.3**	**2.3**
Of which:									
1. United States	19.6	1.8	2.8	1.6	1.8	2.5	2.7	3.0	3.0
2. Eurozone	14.0	1.6	-0.7	-0.5	-0.5	1.0	1.0	1.3	1.3
Germany	3.9	3.4	0.9	0.5	0.5	1.5	1.5	1.5	1.5
France	2.8	2.0	0.0	0.0	0.1	1.0	0.8	1.2	1.3
Italy	2.3	0.4	-2.4	-1.8	-1.8	0.5	0.5	0.9	0.9
Spain	1.7	0.1	-1.6	-1.5	-1.3	0.4	0.5	0.9	0.9
3. Japan	5.6	-0.6	2.0	1.9	1.8	1.4	1.5	1.1	1.1
4. United Kingdom	2.9	1.1	0.3	1.1	1.8	1.7	2.4	1.8	2.4
Developing countries	**48.8**	**6.2**	**5.1**	**4.7**	**4.5**	**5.2**	**5.1**	**5.6**	**5.3**
Of which:									
1. Developing Asia	24.2	7.8	6.8	6.5	6.5	6.8	6.7	7.2	6.9
China	14.1	9.3	7.7	7.5	7.7	7.6	7.6	8.0	7.6
India	5.7	6.2	5.0	5.0	4.6	6.0	5.4	6.5	6.3
2. Central and Eastern Europe	3.5	5.4	1.4	2.0	2.2	3.2	2.8	3.2	3.3
3. Latin America and the Caribbean	8.7	4.6	3.0	2.6	2.5	3.4	3.1	3.8	3.5
Brazil	2.9	2.7	0.9	2.2	2.2	2.7	2.4	4.0	3.0
World Economy	**100.0**	**3.9**	**3.2**	**2.9**	**2.9**	**3.6**	**3.6**	**3.9**	**3.8**
Memo:									
Peru's trading partners 1/		3.7	2.9	2.4	2.5	3.1	3.1	3.4	3.3
BRICs 2/		7.3	5.8	5.8	5.7	6.2	6.0	6.7	6.3

1/ Basket of Peru's 20 main trading partners.
2/ Brazil, Russia, India, and China.
IR: Inflation Report.
Source: Bloomberg, FMI and Consensus Forecast.

Graph 3
GDP GROWTH

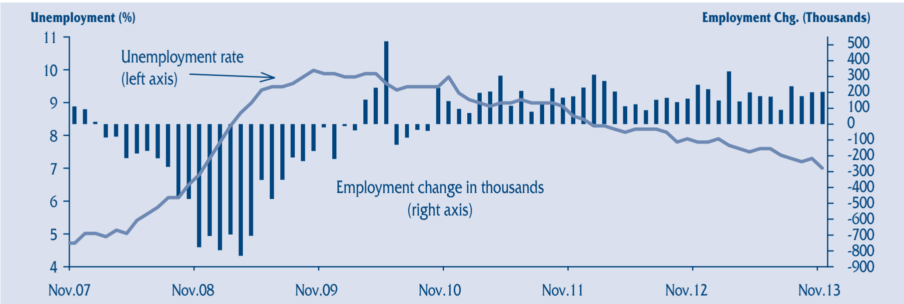
* Forecast.
Source: BCRP.

4. The economy in the **United States** continues showing a recovery. In Q3, the GDP was continuously revised upwards and recorded an annual rate of 4.1 percent, driven by consumption and by a greater accumulation of inventories. Recent indicators show an improvement of employment and a stabilization of the real estate market in Q4, despite the partial government shutdown registered in early October. In this scenario of recovery and controlled inflation, the Fed announced that it would reduce its asset purchase program by US$ 10 billion to US$ 75 billion as from January 2014.

   Consumption continues recovering gradually, supported by the recovery of the labor market. Close to 400,000 new jobs period were created in October-

November, as a result of which 89 percent of the jobs lost during the financial crisis have been recovered. Moreover, the unemployment rate has dropped to 7.0 percent, although part of this decline is attributed to a smaller share of the labor force. A positive wealth effect is also observed due to higher house prices and the improvement of stock markets where the Dow Jones index reached record levels. Other indicators pointing to positive developments include the increase in retail sales, the improvement in wages, and favorable prospects for consumer confidence in the future.

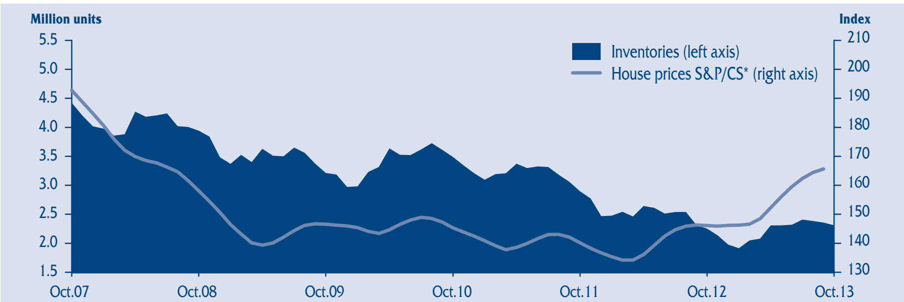
Graph 4
USA: EMPLOYMENT AND UNEMPLOYMENT RATE



Source: Bloomberg.

5. As regards investment, strong gains were recorded in Q3 in the sector of residential construction and non-residential structures. In addition, indicators of the housing market –house prices, builders' confidence, building permits, and applications for mortgages– show some improvement despite the rise in mortgage rates registered since May.

Graph 5
USA: HOUSE PRICES (S&P/CS*) AND INVENTORIES



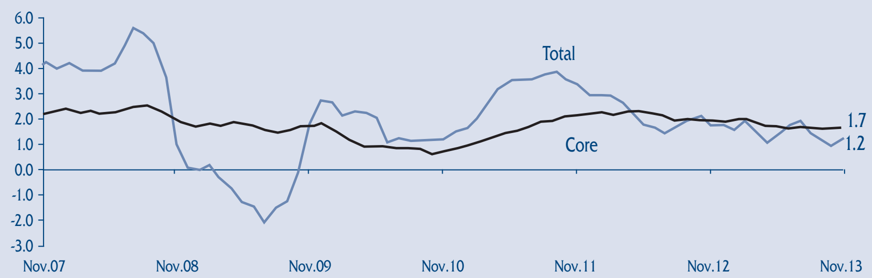
* S&P/CS: S&P/Case-Shiller Home Price Index.
Source: Bloomberg.

6. This recovery takes place within a framework of low inflation. Since our last Inflation report was published in September, inflation has fallen from 1.5 percent in

August to 1.2 percent in November, mainly due to the fall observed in oil prices. Moreover, core inflation –which excludes fuel and food– decreased slightly from 1.8 percent to 1.7 percent in November.

In this context of recovery with controlled inflation pressures, the Fed announced at its meeting of December that it would reduce its monetary stimulus from January 2014. The asset purchase program would decline by US$ 10 billion each month to US$ 75 billion per month, which implies a reduction of US$ 5 billion in Treasury bonds and US$ 5 billion in MBS. If economic conditions continue to improve, the Fed will make further cuts in the upcoming months. In addition, the Fed restated and reinforced that it would keep interest rates low, even if an unemployment rate below 6.5 percent is reached and especially if inflation remains below its 2 percent target. This decision has been made in a context of a favorable development of the labor market, in accordance with what was stated in the minutes of the October policy meeting, and after a budget agreement that would mitigate the impact of the automatic spending cuts in the next two years was reached in December.

Graph 6
USA: CPI
(12 month % change)



Source: Bloomberg.

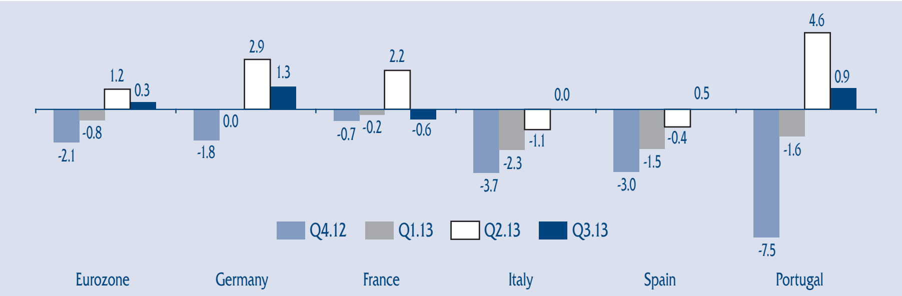
7. The U.S. economy is estimated to grow 1.8 percent in 2013, 2.7 percent in 2014, and 3.0 percent in 2015. Even though the forecasts for the next two years consider a lower impact of the fiscal adjustment, the risks of these forecasts continue to be related to the lack of a definitive agreement about the public debt limit, which is an issue that will be discussed again next February. The other risk is associated with the pace of the Fed withdrawal of monetary stimulus, especially due to the impact this would have on long-term interest rates and, through them, on the housing market.

8. Economic activity in the **Eurozone** recorded a second consecutive quarter of growth in Q3, although showing a lower rate (0.3 percent) than in the previous quarter

(1.2 percent). By spending components, this is explained by private investment (0.8 percent) given that private consumption slowed down and net exports had a negative contribution.

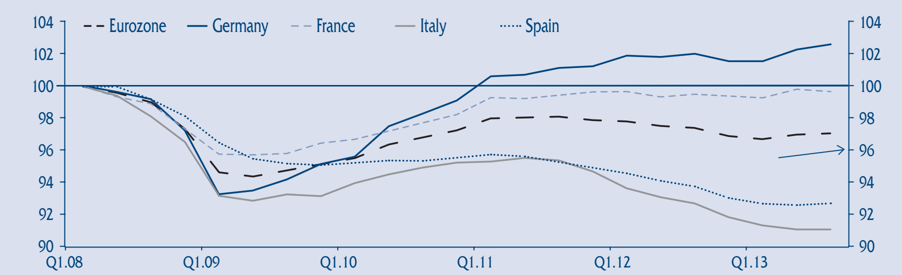
Like other indicators, growth data show that economic activity remains weak since September and that the differences between countries have intensified. Germany continues to show a sustained recovery, while France and several economies with debt problems show less positive results. A similar trend is reflected in other indicators such as the composite PMI index, confidence indices, the rates of unemployment and credit to the private sector.

Graph 7
EUROZONE: QUARTERLY GROWTH
(Seasonally adjusted annualized quarterly rates)



Source: Bloomberg.

Graph 8
EUROZONE: GDP LEVEL
(Q1.08=100)



Source: Bloomberg.

9. **Germany** recorded the highest growth rate in the region in Q3 (1.3 percent) due basically to its strong domestic demand (especially investment). This was also reflected in business confidence indices: in November the ZEW and IFO indices registered their highest levels in over 4 and 1.5 years, respectively. These indicators suggest that investment would continue leading the momentum in Q4.

The other economies recorded in general lower growth rates due to the lower impulse of domestic or external demand. **France** showed a reduction of 0.6 percent in its GDP in Q3 due mainly to the evolution of investment in construction and net exports. The most recent monthly indicators –consumer and business confidence and personal consumer spending– have continued to weaken. Among the economies with debt problems, **Portugal** registered growth for the second consecutive quarter and **Spain** showed a positive growth rate after nine quarters. In both cases, net exports had a positive trend. On the other hand, **Italy** stalled after eight consecutive quarters of contraction.

Table 2
EUROZONE: JP MORGAN PURCHASING MANAGERS INDEX

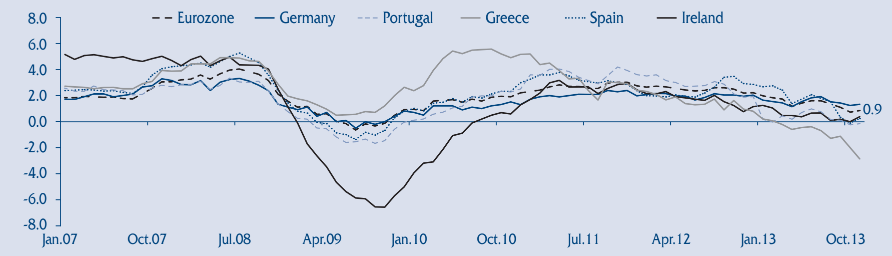
	Dec.10	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Oct.13	Nov.13
Composite								
Eurozone	55.5	48.3	47.2	46.5	48.7	52.2	51.9	51.7
Services								
Eurozone	54.2	48.8	47.8	46.4	48.3	52.2	51.6	51.2
Germany	59.2	52.4	52.0	50.9	50.4	53.7	52.9	55.7
France	54.9	50.3	45.2	41.3	47.2	51.0	50.9	48.0
Italy	50.2	44.5	45.6	45.5	45.8	52.7	50.5	47.2
Spain	46.2	42.1	44.3	45.3	47.8	49.0	49.6	51.5
Manufacturing								
Eurozone	57.1	46.9	46.1	46.8	48.8	51.1	51.3	51.6
Germany	60.7	48.4	46.0	49.0	48.6	51.1	51.7	52.7
France	57.2	48.9	44.6	44.0	48.4	49.8	49.1	48.4
Italy	54.7	44.3	46.7	44.5	49.1	50.8	50.7	51.4
Spain	51.5	43.7	44.6	44.2	50.0	50.7	50.9	48.6

Source: Bloomberg.

10. The weak recovery in the region has been accompanied by low levels of inflation. In October, inflation dropped to 0.7 percent, the lowest level in four years. In this context, at its meeting in the first week of November, the ECB cut its policy rate by 25 bps to 0.25 percent (when no rate cut was expected), maintained its deposit rate at 0 percent, and reduced the rate on emergency loans from 1.0 percent to 0.75 percent. In addition, the ECB extended until mid-2015 the total allocation of regular short-term liquidity (MROs) to offset any liquidity problem.

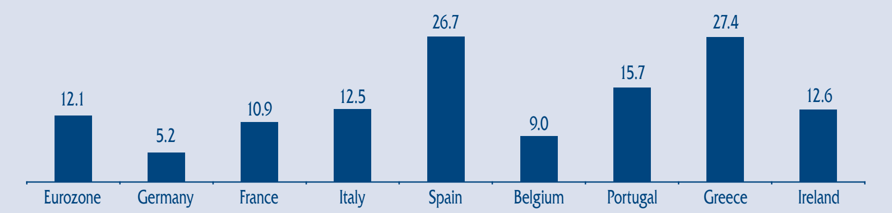
    However, fears of deflation have been fading away since late November due to recent price indicators and due to the explanations provided by some ECB officials about the fact that the region would be going through a prolonged period of low inflation (rather than through a period of deflation).

Graph 9
EUROZONE: CPI
(12 months % change)



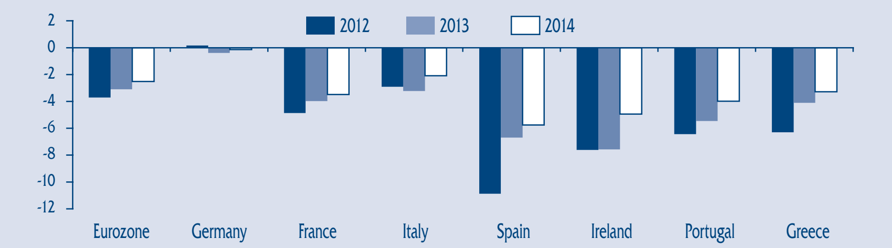
Source: Bloomberg.

Graph 10
EUROZONE: UNEMPLOYMENT RATE (OCTOBER 2013, %)



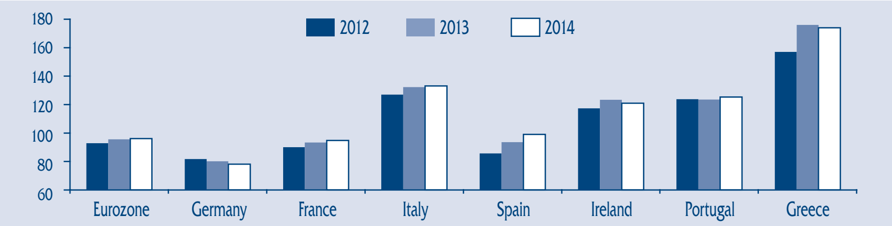
Source: Bloomberg.

Graph 11
EUROZONE: FISCAL BALANCE
(% GDP)



Source: IMF, Fiscal Monitor, October 2013.

Graph 12
EUROZONE: GROSS PUBLIC DEBT
(% GDP)



Source: IMF, Fiscal Monitor, October 2013.

11. In **Japan**, the economy registered a slowdown in Q3 due to a drop in net exports and a moderate growth in consumption. The economy grew 1.1 percent in Q3 after having grown 3.8 percent in previous quarters.

The slower growth in consumption, explained in part by climatic factors (typhoons and unusual high temperatures at the beginning of autumn), has been reflected in the recent indicators of retail sales, spending in actual consumption, and small business confidence and consumer confidence. The dynamism of consumption would improve in anticipation of the increase of the sales tax in the next two years and due to the sustained recovery of the labor market. In October, the unemployment rate was 4 percent, 0.3 percentage points lower than the average level in 2012. .

On the investment side, the construction of public works continued to increase at high rates, although according to the report on futures contracts, this trend would not continue in the coming months. On their side, exports would recover at the beginning of Q4 if external demand stabilizes and is favored by the depreciation of the yen.

In line with these developments, the Japanese economy would grow 1.8 percent in 2013, 1.5 percent in 2014, and 1.1 per cent in 2015. The risks on this forecast are associated mainly with the impact of the increase in the sales tax –which will be implemented in April 2014 and in 2015– and with the effectiveness of monetary policy to reach its 2 percent inflation target. It should be pointed out that the deflationary process has reversed in recent months and that inflation at October of this year has reached 0.9 percent per annum, the highest rate in five years.

12. In the emerging economies, recent economic indicators confirm a normalization of the pace of growth in **China**. In Q3 the GDP grew 7.8 percent relative to the same period of last year (versus 7.5 percent in Q2). The official purchasing managers index for manufacturing confirms this trend in November. Targeted measures introduced by the government to support growth, such as the temporary suspension of taxes to small and medium-sized enterprises, assistance to exporters in the problems faced by exports, and the acceleration of investment in urban infrastructure and railways, have contributed to these results. Moreover, exports continue to increase in a context of gradual recovery of the global economy.

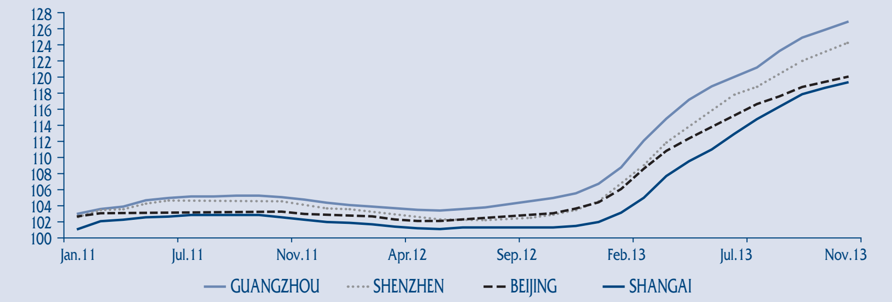
Table 3
CHINA: ECONOMIC INDICATORS

	2011	2012				2013				
	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Oct.	Nov.
Manufacturing PMI index (50 neutral level)	50.3	53.1	50.2	49.8	50.6	50.9	50.1	51.1	51.4	51.4
Non-manufacturing PMI index (50 neutral level)	56.1	58.0	56.7	53.7	56.1	55.6	53.9	55.4	56.3	56.0
Industrial Production (12 month % change)	12.8	11.9	9.5	9.2	10.3	8.9	8.9	10.2	10.3	10.0
Investment in fixed assets (Annual % change)	23.8	20.9	20.4	20.5	20.6	20.9	20.1	20.2	20.1	19.9
Retail sales (12 month % change)	18.1	15.2	13.7	14.2	15.2	12.6	13.3	13.3	13.3	13.7
Exports(12 month % change)	13.4	8.9	11.3	9.9	14.1	10.0	-3.1	-0.3	5.6	12.7
Imports (12 month % change)	11.8	5.3	6.3	2.4	6.0	14.1	-0.7	7.4	7.6	5.3
New loans (Billion yuan)	641	1,011	920	623	455	1,063	863	787	506	625
New financing (Billion yuan)	n.d.	1,870	1,780	1,646	1,628	2,550	1,037	1,405	856	1,230
Consumer Price Index (12 month % change)	4.1	3.6	2.2	1.9	2.5	2.1	2.7	3.1	3.2	3.0
Producer Price Index (12 month % change)	1.7	-0.3	-2.1	-3.6	-1.9	-1.9	-2.7	-1.3	-1.5	-1.4

Source: Bloomberg.

Inflation shows a moderate rise although it is still below the 3.5 percent target established for this year. In addition, in view of the continuous increase of real estate prices –one of the main sources of risk for the Chinese economy–, the monetary authorities are trying to moderate the growth rate of loans to sustainable levels.

Graph 13
CHINA: REAL STATE
(Index, new residential constructions)



Source: National Bureau Statistic (China).

In the field of structural reforms, in its recent plenary session the Chinese Communist Party announced actions on several fronts to complete the transition to a market economy and tackle systemic risks. Measures to be implemented in the financial sector include accelerating the process of liberalization; allowing investors to establish small and medium-sized banks; establishing a deposit insurance system; and developing the market of corporate bonds and bonds of local governments. The tax reforms include implementing a more transparent budget process and improving debt management at all government levels. In terms of market reforms, easing controls over the prices of water, electricity, and natural resources has been proposed, together with opening protected industries (including finance and energy) to greater private participation. In addition, farmers will have the right to own and transfer land, as well as to use the land as collateral for loans, and the control system over people's movements between rural and urban areas will be more flexible to allow the free movement of labor.

In this context, China is expected to grow 7.7 percent in 2013 (in line with the estimates of the authorities) and to grow 7.6 percent in 2014 and in 2015.

13. In **India**, confidence has been affected by a combination of external vulnerabilities and policy uncertainties. Although recent economic indicators suggest some improvement –in Q3 the GDP registered an annual variation of 4.8 percent, versus

4.4 percent in Q2, due mainly to a recovery in the agricultural sector–, they still show a weak rate of activity.

The current account deficit fell in Q3 (1.2 percent of GDP, compared with 5.2 percent of GDP in the same period of the previous year), in part due to the improvement observed in exports as a result of the depreciation of the rupee, but the PMI Indices for manufacturing and services (HSBC/Markit) and the growth rate of industrial production remain at low levels. The risks include the possibility of exceeding the programmed fiscal deficit and uncertainty associated with the electoral context. The central bank maintains a prudent position given the persistence of inflationary pressures.

Table 4
INDIA: ECONOMIC INDICATORS

	2011	2012				2013				
	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Oct.	Nov.
Manufacturing PMI index (50 neutral level)	54.2	54.7	55.0	52.8	54.7	52.0	50.3	49.6	49.6	51.3
Services PMI index (50 neutral level)	54.2	52.3	54.3	55.8	55.6	51.4	51.7	44.6	47.1	47.2
Industrial Production (12 month % change)	2.7	-2.8	-2.0	-0.7	-0.6	3.5	-1.8	2.0	n.a.	n.a.
Exports(12 month % change)	8.6	-5.2	-6.1	-7.2	0.6	6.6	-5.5	11.2	13.5	5.9
Imports (12 month % change)	27.1	23.7	-11.5	5.0	8.3	-4.3	-0.9	-18.1	-14.5	-16.4
Consumer Price Index (12 month % change)	n.a.	9.38	9.93	9.73	10.56	10.39	9.87	9.84	10.09	11.24
Wholesale Price Index (12 month % change)	7.74	7.69	7.58	8.07	7.31	5.65	5.16	6.46	7.00	7.52

Source: Bloomberg.

In this context, India is expected to grow 4.6 percent in 2013, 5.4 percent in 2014, and 6.3 percent in 2015.

14. Like in the period analyzed in our previous Report, **Latin American countries** have shown moderate growth rates, affected by a less favorable international environment and, in many cases, by a lower dynamism of domestic demand. In some economies, such as Mexico and Chile, where growth has been lower than the potential level of growth, central banks have reduced their interest rates, this decision being favored by low inflation levels. In other economies, such as Brazil, inflationary and depreciation pressures have limited policy response and have even led to a rise in rates.

It is estimated that in 2013 the region would grow 2.5 percent, a similar rate to the one foreseen in our previous Inflation Report. In 2014 and 2015, the region would show greater dynamism with rates of 3.1 and 3.5 percent, respectively, in line with the higher growth estimated in the world economy. However, these rates are still below the growth rates recorded during the decade before the global financial crisis of 2008.

Graph 14
LATIN AMERICA: GDP GROWTH FORECAST 2014
(%)

Source: Latin America Consensus Forecast (December 2013) and BCRP (Peru).

Graph 15
LATIN AMERICA: INFLATION FORECAST 2014
(Dec./Dec.)

Source: Latin America Consensus Forecast (December 2013) and BCRP (Peru).

Financial markets

15. Since September, international financial markets have been affected by uncertainty associated with the fiscal negotiations in the USA and by expectations about the Fed purchase program.

    In the first case, the Government and the U.S. Congress reached an agreement at the beginning of October and this reduced risk aversion in the following months. This trend was favored by the budget agreement approved in December by the House of Representatives, which would mitigate the automatic spending cuts in the next two years. However, the definition of the debt limit has only been postponed until February 2014, which could imply an increase in risk aversion as the deadlines for reaching definitive agreements approach.

    As regards monetary policy, the lack of definition about tax agreements and evidence of a slow economic recovery have led the Fed to postpone the tapering of its asset purchase program scheduled for September. Since that month, the market expected the Fed to start reducing the monthly amount of purchases by the end of 2013 or early next year. On 18 December the Fed announced a reduction of US$ 10 billion that would begin in January 2014.

16. The reduction of risk aversion observed since September was also favored by developments in other countries and regions, including (i) the political and financial stability in the Eurozone countries and the ECB cut of its policy rate, (ii) greater signs of moderate growth in China and the reforms announced in the third plenary of the Communist Party of China, and (iii) minor geopolitical fears in the Middle East after Iran and the 5 permanent members of the Security Council of the United Nations and Germany reached an interim agreement –for six months– to reduce Iran's nuclear program.

17. The **Eurozone sovereign debt markets** showed a positive development thanks to the better political and financial conditions in the Eurozone and to the ECB rate cut.

    In line with this, the major rating agencies upgraded the rating or the outlook for several European economies with debt problems. Moody's upgraded Portugal's outlook from negative to stable and raised the rating of Greece. Standard&Poors improved the outlook for Spain, but downgraded the rating assigned to Holland and France.

    In this context, the credit spreads of the Eurozone peripheral economies, such as Greece, Portugal, Italy, Spain and Ireland, recorded significant reductions.

Table 5
SOVEREIGN SPREADS OF DEVELOPED COUNTRIES

	End of period						Difference in basis points		
	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Dec.13*	Dec.13/Dec.11	Dec.13/Dec.12	Dec.13/Sep.13
CDS (bps)									
USA	49	38	38	28	35	32	-17	-6	-3
United Kingdom	98	41	45	50	33	27	-70	-14	-6
Germany	102	42	37	32	24	25	-78	-17	1
France	220	93	83	80	69	53	-167	-40	-16
Spain	380	300	302	284	227	151	-230	-149	-76
Italy	484	289	306	284	267	169	-316	-121	-99
Ireland	724	220	190	166	143	122	-603	-98	-22
Greece 1/	8,786	4,265	3,890	1,144	987	734	-8,053	-3,531	-253
Portugal	1,082	443	418	401	491	355	-727	-88	-136
10 Year Treasury yields (%)									
USA	1.88	1.76	1.85	2.49	2.61	2.86	99	111	25
United Kingdom	1.98	1.83	1.77	2.44	2.72	2.90	92	107	18
Germany	1.83	1.32	1.29	1.73	1.78	1.83	0	51	5
Japan	0.99	0.79	0.55	0.85	0.69	0.70	-29	-10	1

* Data as of December 13, 2013.
1/ After the first proceed from the Greek debt restructuring, the Greek spread was reduced to a level of 5,730 basis points. In January 2013, with the Greek debt repurchasing the index fell again.
Source: Bloomberg.

18. Developments in the **fiscal arena** included the following events in countries with programs with the European Union/IMF. In **Ireland**, the troika concluded the last review of the program with positive results. This country will be the first to conclude a bailout program successfully. Moreover, the Irish government has reported that it will not request a preventive credit line once the program is complete. In **Portugal**, the eighth and ninth reviews of the agreement concluded positively. In **Greece**, on the other hand, the negotiations between the troika and the Greek government have still not finished, which is delaying the conclusion of the program review. The points in which there was disagreement with the Greek government included the progress of the program and the size of the financing gap.

    On the other hand, the European Commission (EC) released their assessments to the 2014-2016 budgets of the economies without UE/FMI programs. Warning that the medium-term economic prospects would not be aligned with fiscal targets in the case of Spain and Italy, it requested that these countries review their budgets to ensure compliance with the program.

    Furthermore, in the **financial arena, Spain** would be about to conclude its financial rescue program and the Spanish government said that it will not request further assistance of the ESM after finishing its program in January 2014. The facility assigned to the country was €100 billion, but only €41 billion was required.

    At the level of the region, some progress was made in the area of the **banking union** according to what was agreed in June, especially in terms of the bank resolution mechanism and resolution fund, after the coalition government was formed in Germany. In October, the ECB announced its plan for the comprehensive assessment of banks in the Eurozone –Asset Quality Review (AQR)– which will begin soon and includes the evaluation of risk, the evaluation of the quality of assets, and stress tests.

19. The yields on **assets considered safe** showed a rising conduct associated basically with concerns of a Fed withdrawal of quantitative easing that would imply a lower demand for US Treasury bonds and with better prospects for economic activity. The yield on ten-year Treasury bonds rose 25 bps between September and December.

    In **Germany** and **Japan**, yields recorded lower growth after the ECB cut rates in the first week of November as well as due to the signals of a moderation of growth in the Eurozone peripheral economies and, in the case of the Japanese economy, due to expectations that the central bank will increase its asset purchase program.

    The debt markets of Latin American countries, except Brazil, showed a positive evolution, in line with the lower risk aversion registered since October.

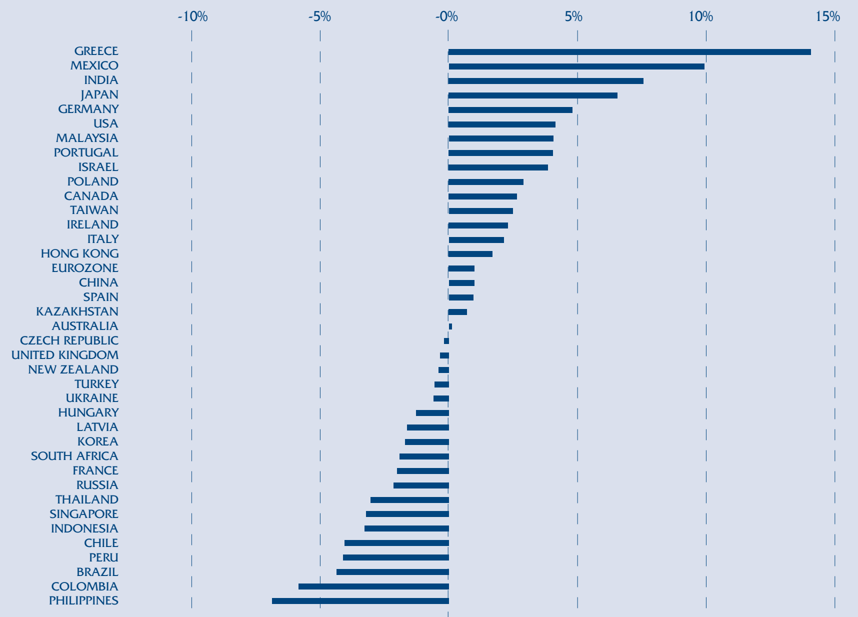
Table 6
SOVEREIGN CDS SPREADS OF EMERGING COUNTRIES
(Basis points)

	End of period						Difference in basis points		
	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Dec.13*	Dec.13/Dec.11	Dec.13/Dec.12	Dec.13/Sep.13
Brazil	161	108	137	187	176	180	19	72	4
Chile	132	72	65	100	90	77	-56	5	-13
Colombia	154	96	99	143	134	116	-39	20	-19
Mexico	153	97	97	132	122	89	-64	-8	-33
Peru	172	97	97	145	148	129	-43	32	-19
Hungary	635	278	390	321	280	272	-363	-6	-8
Poland	281	78	99	104	89	76	-205	-2	-13
Russia	278	135	166	196	179	162	-116	27	-17
Turkey	291	131	146	191	219	193	-99	61	-27
China	147	66	74	119	89	66	-82	-1	-23
Israel	198	135	126	127	122	100	-98	-35	-22
South Africa	203	149	183	218	201	198	-6	49	-3

* Data as of December 13, 2013.
Source: Bloomberg.

20. **Stock markets** also recovered, recording gains in the major developed markets and in some emerging economies as a result of the better economic and financial prospects. However, the Latin American region and some European and Asian emerging economies remain affected by the liquidation of positions associated with increased fears that the Fed will soon start the tapering of QE and in line with the fall of the prices of commodities. In the case of the region, with the exception of Mexico, the main stock exchanges registered losses between September and December.

Graph 16
STOCK MARKETS
(End of period; % chg. Dec.13 respect to Sep.13)



Source: Bloomberg.

Graph 17
RISK AVERSION COEFFICIENT: VIX (S&P'500)
(March 2008 - December 2013)

Source: Bloomberg.

Foreign exchange rate

21. According to the Fed index, the dollar rose 0.5 percent between September and December. The dollar appreciated 5.0 percent against the yen due to expectations that the Bank of Japan (BoJ) would increase monetary stimulus while, on the other hand, the Fed was expected to start the withdrawal of monetary stimulus. On the other hand, the dollar depreciated 0.7 percent against the pound and 1.6 percent against the euro, in both cases basically due to the better outlook for growth in Europe.

Graph 18
US DOLLAR INDEX*
(January 2008 - December 2013)

* A rise in the index represents an appreciation of the US dollar.
Source: Fed.

Moreover, the **currencies of emerging economies** have continued to depreciate against the dollar –the exception in the region being the Mexican peso and the Peruvian nuevo sol– in a context marked by uncertainty associated with expectations that the Fed will begin the withdrawal of QE and by the reduction of commodity prices. As in the period discussed in our previous report, the highest depreciation levels were observed in economies with high current account deficits or relying strongly on external funding. The currencies of the region which depreciated the most included the Argentine peso, the Chilean peso and the Brazilian real.

Table 7
EXCHANGE RATE

	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Dec.13*	% Chg. Dec.13 compared to: Dec.11	Dec.12	Sep.13
Canada	1.02	0.99	1.02	1.05	1.03	1.06	3.85	6.69	2.68
Japan	76.94	86.75	94.22	99.14	98.27	103.21	34.14	18.97	5.03
United Kingdom (US$/c.u.)	1.55	1.63	1.52	1.52	1.62	1.63	4.92	0.30	0.70
Eurozone (US$/c.u.)	1.30	1.32	1.28	1.30	1.35	1.37	6.11	4.15	1.60
Switzerland (US$/c.u.)	0.94	0.92	0.95	0.94	0.90	0.89	-5.17	-2.88	-1.74
Brazil	1.86	2.05	2.02	2.23	2.22	2.33	25.06	13.77	5.14
Chile	519	478	471	507	505	528	1.78	10.50	4.66
Colombia	1,936	1,766	1,819	1,920	1,906	1,931	-0.25	9.36	1.32
Mexico	13.95	12.86	12.31	12.94	13.09	12.87	-7.71	0.06	-1.66
Argentina	4.30	4.92	8.38	5.39	5.79	6.29	46.19	27.96	8.62
Peru	2.697	2.552	2.591	2.781	2.79	2.77	2.71	8.54	-0.57
Hungary	243	220	237	227	220	220	-9.75	-0.30	-0.16
Poland	3.44	3.08	3.26	3.32	3.12	3.04	-11.58	-1.40	-2.54
Russia	32.19	30.55	31.07	32.83	32.38	32.89	2.17	7.66	1.59
Turkey	1.88	1.78	1.81	1.92	2.02	2.04	8.16	14.59	1.09
China	6.29	6.23	6.21	6.14	6.12	6.07	-3.54	-2.55	-0.80
India	53.01	54.99	54.28	59.52	62.58	62.19	17.31	13.08	-0.62
Israel	3.81	3.73	3.65	3.64	3.53	3.50	-8.07	-6.23	-0.67
South Africa	8.07	8.45	9.22	9.83	10.02	10.28	27.51	21.69	2.63
FED basket	100.6	99.2	100.6	102.6	101.3	101.9	1.21	2.67	0.53

* Data as of December 13, 2013.
Source: Bloomberg and Reuters.

Interest rate decisions

22. In the last months, most central banks in the developed countries have maintained their interest rates unchanged. The exception was Sweden and the European Central Bank which, in a decision not expected by the market, reduced the interest rate by 25 bps due given the slow economic recovery and low inflation (at November, inflation recorded 0.9 percent).

    Monetary policy responses in the emerging economies were not uniform. In some countries, such as Thailand, Romania, Mexico, Hungary, Chile, and Serbia, interest rates were lowered to support the recovery of the economy in a context of contained inflationary pressures. On the other hand, other emerging economies raised interest rates because of inflationary pressures and imbalances in their external accounts. It should be pointed out that in no case are interest rates at higher levels than those observed before the international financial crisis.

Table 8
MONETARY POLICY INTEREST RATE

	Dec.12	Mar.13	Jun.13	Sep.13	Dec.13	Differences in basis points Dec.13 respect to:		
						Sep.13	Dec.12	Sep.08
Brazil	7.25	7.25	8.00	9.00	10.00	100	275	-375
Pakistan	9.50	9.50	9.00	9.50	10.00	50	50	-300
Serbia	11.25	11.75	11.00	11.00	9.50	-150	-175	-625
India	8.00	7.50	7.25	7.50	7.75	25	-25	-125
Indonesia	5.75	5.75	6.00	7.25	7.50	25	175	-175
Iceland	6.00	6.00	6.00	6.00	6.00	0	0	-950
China	6.00	6.00	6.00	6.00	6.00	0	0	-120
South Africa	5.00	5.00	5.00	5.00	5.00	0	0	-700
Turkey	5.50	5.50	4.50	4.50	4.50	0	-100	-1,225
Chile	5.00	5.00	5.00	5.00	4.50	-50	-50	-375
Peru	4.25	4.25	4.25	4.25	4.00	-25	-25	-250
Romania	5.25	5.25	5.25	4.25	4.00	-25	-125	400
Mexico	4.50	4.00	4.00	3.75	3.50	-25	-100	-475
Philippines	3.50	3.50	3.50	3.50	3.50	0	0	-250
Colombia	4.25	3.25	3.25	3.25	3.25	0	-100	-675
Hungary	5.75	5.00	4.25	3.60	3.00	-60	-275	-550
Malaysia	3.00	3.00	3.00	3.00	3.00	0	0	-50
Poland	4.25	3.25	2.75	2.50	2.50	0	-175	-350
New Zealand	2.50	2.50	2.50	2.50	2.50	0	0	-500
Australia	3.00	3.00	2.75	2.50	2.50	0	-50	-450
South Korea	2.75	2.75	2.50	2.50	2.50	0	-25	-275
Thailand	2.75	2.75	2.50	2.50	2.25	-25	-50	-150
Taiwan	1.88	1.88	1.88	1.88	1.88	0	0	-163
Norway	1.50	1.50	1.50	1.50	1.50	0	0	-425
Canada	1.00	1.00	1.00	1.00	1.00	0	0	-200
Israel	2.00	1.75	1.25	1.00	1.00	0	-100	-325
Sweden	1.00	1.00	1.00	1.00	0.75	-25	-25	-400
United Kingdom	0.50	0.50	0.50	0.50	0.50	0	0	-450
Eurozone	0.75	0.75	0.50	0.50	0.25	-25	-50	-400
USA	0.25	0.25	0.25	0.25	0.25	0	0	-175
Switzerland	0.00	0.00	0.00	0.00	0.00	0	0	-275

Box 1

THE FED'S MONETARY STIMULUS

This box renews the quantitative easing programs implemented by the US Federal Reserve (Fed) and discusses the impact that expectations on the tapering of the Fed asset purchase program has in the economies of the region, especially in the market of government bonds, the country risk, and the value of currencies.

With the bankruptcy of Lehman Brothers in September 2008, the U.S. accelerated the provision of liquidity to the financial system at the global level through increases of swap lines with the main central banks and, at the local level, through purchases of troubled debt for up to US$ 700 billion using Treasury resources. The Fed also reduced its policy rate to a range between 0 and 0.25 percent and started a quantitative easing strategy purchasing highly rated assets, mainly mortgage-backed securities[1] through its first quantitative easing program (QE1). In its second and third quantitative programs –QE2 and QE3–, it increased its purchases of U.S. Treasury bonds, especially of the bonds with longer terms in order to reduce the cost of long-term funding so as to reignite economic activity. Additionally, QE2 also included the implementation of "operation twist", which consisted of swapping short-term bonds (with maturities of less than 3 years) by long-term bonds (with maturities between 6 and 30 years) for a total of US$ 400 billion.

1 The first announcement of the Fed was made on November 25, 2008, and referred to the purchase of Government Sponsored Enterprises (GSE) securities and mortgage-backed securities (MBS) for a total of US$ 600 billion.

FED ASSET PURCHASE PROGRAM
(Billion US$)

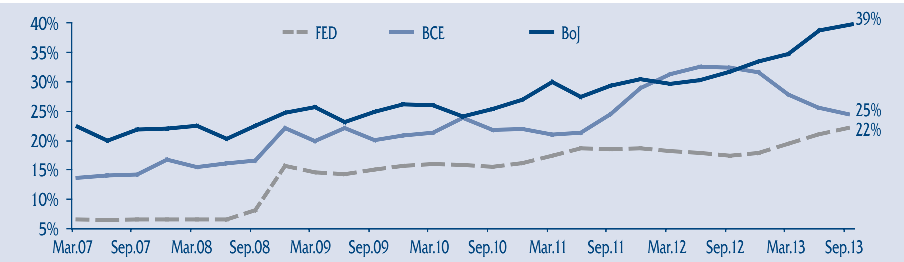
	Total purchases by programs		Monthly purchases
	QE1 (Nov.2008)	**QE2 (Nov.2010)**	**QE3 (Sep.2012*)**
Total	**1,725**	**600**	**85**
GSE bonds	175	0	0
MBS	1,250	0	40
Treasury bonds	300	600	45
Operation "twist"		✓ **	

*QE1 and QE2 are presented in maximum total purchases. QE3 corresponds to monthly purchases in a no defined term.
** Operation "Twist" redeem short-term bonds (<3 years) for long-term bonds (between 6 and 30 years) for US$ 400 billion.

	Flows of Balance Assets from the FED		Flow of assets
	Sep.08-Oct.10	**Nov.10-Aug.12**	**Sep.12-Nov.13**
Total Assets	**1,300**	**517**	**1,113**
Bonds:	1,559	532	1,092
MBS	1,051	-207	596
Treasury bonds	358	802	524
GSE bonds	150	-62	-29

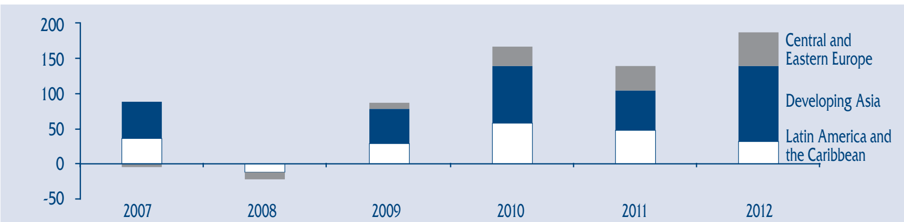
As a result of quantitative easing, between September 2008 and November 2013, the balance sheet of the Fed has quadrupled with an intake of assets of US$ 2.93 billion, of which the amount for holdings of securities has been US$ 3.18 billion (US$ 1.44 billion in MBS and US$ 1.68 billion in Treasury bonds). This Fed program together with the expansionary monetary policies implemented by the European Central Bank (ECB) and the Bank of England (BoE) have resulted in abundant availability of global financial funds and have induced substantial capital flows to the emerging economies, which has appreciated the currencies of these economies and eased funding conditions significantly, as reflected in lower global interest rates, especially in public and private bonds.

CENTRAL BANKS: TOTAL ASSETS
(% GDP)



Source: Bloomberg.

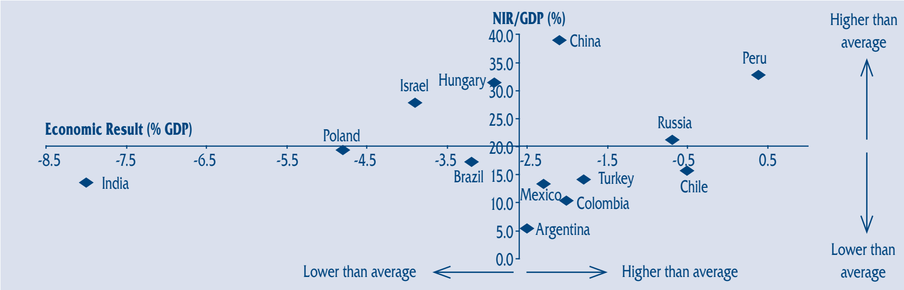
NET FLOWS OF INVESTMENT PORTFOLIO
(Billion US$)



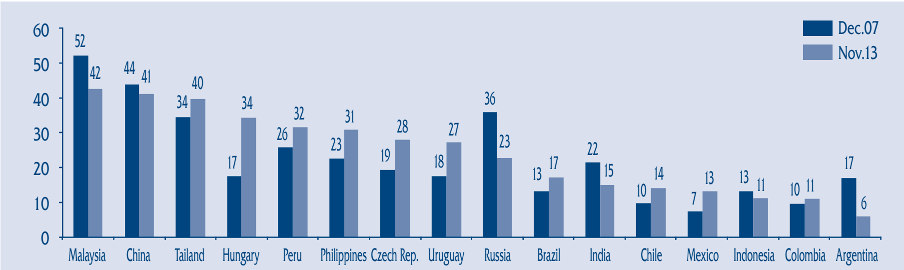
Source: IMF.

In this context of abundant international financial liquidity and with a high probability of substantial reversals, some emerging economies have preventively accumulated international reserves while maintaining a prudent fiscal stance and strengthening at the same time their financial system implementing instruments that reduce their vulnerability to the reversal of capital flows.

EMERGING ECONOMIC INDICATORS



INTERNATIONAL RESERVES
(% GDP)



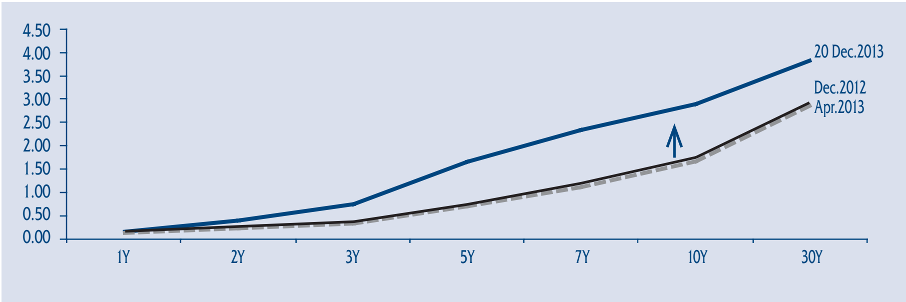
Source: IMF and central banks.

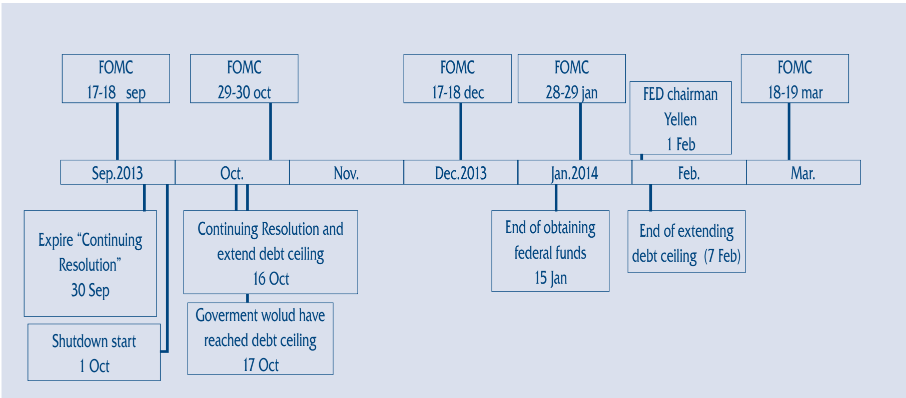
In May 2013, **after five years of monetary stimulus**, the Fed under the chairmanship of Ben Bernanke announced the need to start tapering the assets purchase program in the near future. The continuity of these purchases would be conditioned to whether a substantial progress in economic recovery was achieved, mainly in the job market. By November, 89 percent of the jobs lost during the crisis have been recovered and the unemployment rate has decreased 80 basis points in 2013 to 7 percent. Together with the stabilization of the housing market, this has increased expectations that the Fed will start tapering its asset purchase program – reducing QE by US$ 10 billion– as was announced in December.

It is worth pointing out that this does not imply an increase in the policy interest rate, which is expected to occur in 2015 or 2016. In its communiqué of December 2012, the Fed said that interest rates would remain low until the rate of unemployment fell below 6.5 percent, the forecast of the rate of inflation 2 years ahead was below the 2 percent long-term target (with a positive margin of 0.5), and long-term inflation expectations remained anchored.

Influenced by expectations that the Fed would start tapering QE, an increase was observed in the yields of mid- and long-term US Treasury bonds, which corrected the overvalued prices of these assets and reduced in this way the probability of a more abrupt correction in the future.

YIELD CURVE OF US TREASURY BONDS
(%)



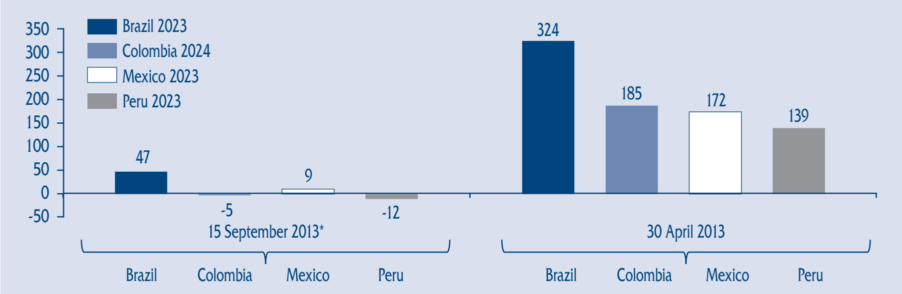


On the other hand, the increase in global long-term interest rates due to the beginning of the Fed's tapering of its asset purchase program would lead investors to restructure their portfolios and migrate from more risky securities to those considered safer, which would induce an increase of the interest rates of debt instruments. The expectation of an impending reduction of monetary stimulus has probably been anticipated by the market, as reflected in the higher rates on sovereign bonds of the region and also in the correction of the prices of those assets.

10 YEARS SOVEREIGN BOND YIELDS
(%)

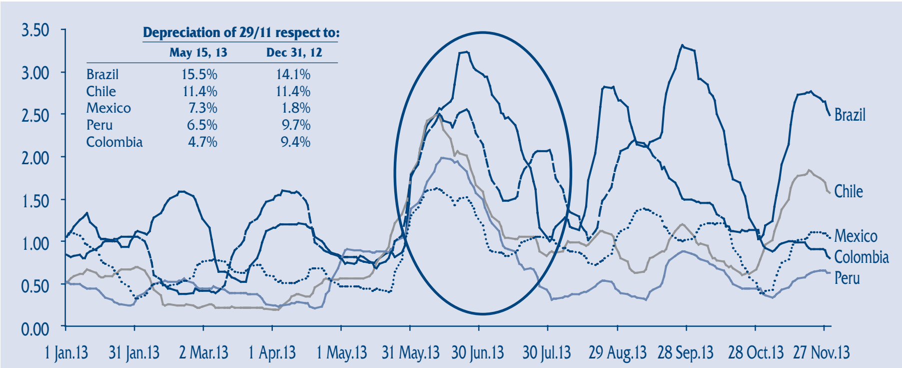
Sovereign bonds	29 Nov.13	15 Sep.13	30 Apr.13	15 Nov.12	31 Oct.10
Brazil	12.94	12.47	9.70	9.46	12.16
Colombia	6.77	6.81	4.91	6.27	7.44
Mexico	6.31	6.23	4.59	5.56	6.36
Peru	5.50	5.62	4.11	4.45	5.47
Global bonds					
Brazil	4.75	4.75	3.05	2.51	4.32
Colombia	4.63	4.86	3.17	2.99	4.55
Mexico	4.30	4.40	2.57	2.77	3.74
Peru	4.49	4.74	3.19	2.90	4.37
US Treasury bonds	2.75	2.89	1.67	1.62	2.60

CHANGES OF 10 YEAR US SOVEREIGN BOND YIELDS (IN BPS.)
NOVEMBER 2013 RELATIVE TO:



* On Sep.17-18, Fed announces to continue buying bonds.
Source: Bloomberg.

EXCHANGE RATE VOLATILITY
(Variation coefficient of last 30 business days)



Source: Reuters.

In conclusion, the markets have already internalized the beginning of the tapering of the Fed's asset purchase program and consequently, although with high volatility, the various prices in the financial markets –the yields of assets, interest rates, the exchange rates, and the prices of commodities, among others– have been registering early adjustments with some differenciation among the various emerging economies associated with their fundamentals. These earlier adjustments will imply lower voltility on these prices when the tapering effectively begins.

II. Economic Activity

23. The projected growth rate of GDP in **2013** is revised in this report to 5.1 percent, a lower rate than the 5.5 percent rate considered in our report of September. This lower growth of GDP is associated with the lower dynamism of domestic demand (5.8 percent versus 6.5 percent in our previous report), due mainly to the lower growth of private investment in the year (down from 7.7 to 4.3 percent). A recovery of exports is expected in the last quarter (this projection incorporates data from the first three quarters of the year).

The slowdown in the growth of GDP –from 6.3 percent to 5.1 percent– between 2012 and 2013 is explained by the reduction in the growth of private investment –from 13.5 percent to 4.3 percent– and by a lower consumption rate –down from 5.8 to 5.2 percent. This result is accompanied by a lower increase of exports, which went from 5.4 per cent to 1.5 percent in the same period. Moreover, in the first nine months of the year, compared with same period of the previous year, private investment decelerated significantly from 14.1 percent to 4.8 percent, while private consumption slowed down from 6.3 percent to 5.2 percent, and exports slowed down from 6.8 percent to a nil result.

Table 9
GDP AND DOMESTIC DEMAND
(Real % change)

	2012	2013*			2014*		2015*	
	Year	Jan-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
I. Domestic demand	**7.3**	**6.1**	**6.5**	**5.8**	**6.1**	**6.0**	**6.3**	**6.1**
a. Private expenditure	**6.4**	**5.3**	**5.8**	**5.0**	**5.5**	**5.3**	**6.0**	**5.7**
Consumption	5.8	5.2	5.2	5.2	5.3	5.2	5.4	5.4
Private fixed investment	13.5	4.8	7.7	4.3	7.7	6.3	7.9	6.6
b. Public debt	**13.3**	**12.0**	**10.8**	**10.1**	**9.0**	**9.9**	**8.4**	**8.5**
Consumption	9.4	7.4	7.6	5.5	4.0	6.3	4.2	4.2
Investment	20.8	20.5	16.3	18.1	17.0	15.5	14.6	14.6
II. Exports	**5.4**	**0.0**	**0.7**	**1.5**	**9.3**	**6.3**	**11.4**	**10.9**
III. Imports	**10.4**	**6.6**	**6.3**	**5.5**	**7.9**	**6.3**	**8.6**	**7.9**
GDP (I+II-III)	**6.3**	**4.9**	**5.5**	**5.1**	**6.2**	**6.0**	**6.7**	**6.5**

IR: Inflation Report.

Table 10
GDP AND DOMESTIC DEMAND
(Contributions to the real % change)

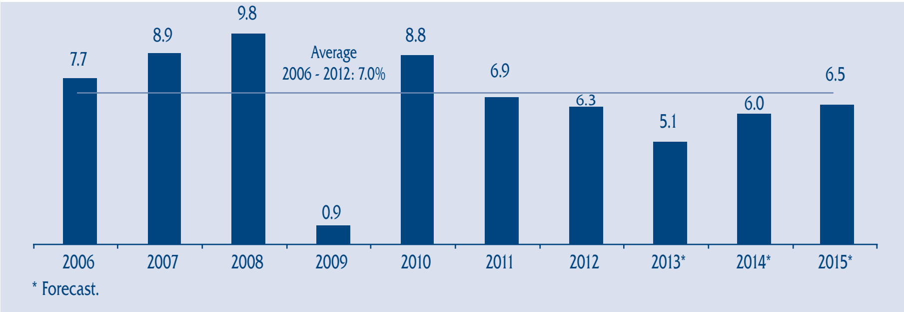
	2012		2013*			2014*		2015*	
	Jan-Sep	Year	Jan-Sep	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
I. Domestic demand	**7.5**	**7.7**	**6.4**	**6.8**	**6.1**	**6.4**	**6.3**	**6.7**	**6.5**
a. Private expenditure	6.0	5.9	4.9	5.2	4.6	5.0	4.8	5.4	5.1
Of which:									
Consumption	3.9	3.9	3.5	3.5	3.4	3.5	3.4	3.5	3.5
Private fixed investment	3.2	3.0	1.2	1.8	1.0	1.9	1.5	2.0	1.6
b. Public expenditure	1.4	1.9	1.5	1.6	1.5	1.4	1.6	1.4	1.4
Consumption	0.3	0.9	0.6	0.7	0.5	0.4	0.6	0.4	0.4
Investment	1.1	1.0	0.9	0.9	1.0	1.0	0.9	1.0	1.0
II. Exports	**1.3**	**0.9**	**0.0**	**0.1**	**0.3**	**1.6**	**1.1**	**2.0**	**1.9**
III. Imports	**2.4**	**2.3**	**1.5**	**1.5**	**1.3**	**1.8**	**1.5**	**2.0**	**1.8**
GDP (I+II-III)	**6.4**	**6.3**	**4.9**	**5.5**	**5.1**	**6.2**	**6.0**	**6.7**	**6.5**

IR: Inflation Report.
* Forecast.

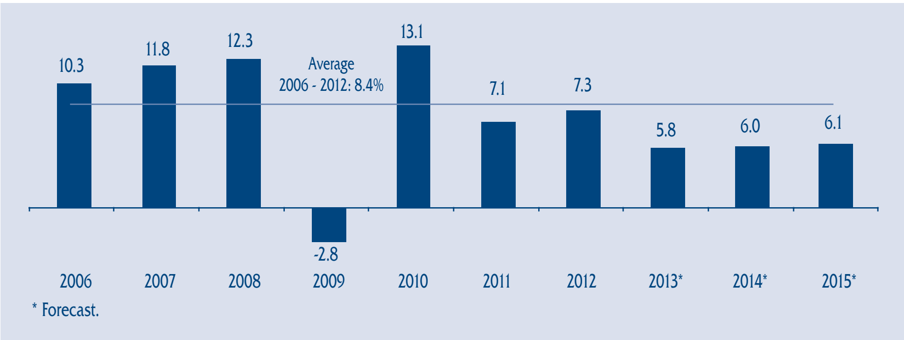
24. The GDP is projected to grow 6.0 percent in 2014 and 6.5 percent in 2015, rates close to the rate of potential activity. This potential growth rate considers the implementation of reforms that would increase productivity. In the last decade, taking into account the breakdown of the potential output by components, the growth rate of potential GDP was mainly explained by the increase in capital stock, which contributed 2.1 percentage points, and by total factor productivity of factors, which contributed 2.3 percent.

25. On the expenditure side, a recovery of exports, which would grow at a higher rate than the average rate of the last decade, is foreseen in the forecast horizon. Exports would record a growth of 6.3 percent and 10.9 percent in 2014 and 2015, respectively. Similarly, private investment would show a recovery, reaching a growth rate of 6.3 percent in 2014 and a rate of 6.6 percent in 2015. On its side, private consumption would maintain a growth rate similar to the one recorded in the last decade –with rates of 5.2 percent and 5.4 percent in these years–, while public spending would have a positive performance with rates of 9.9 percent and 8.5 percent in 2014 and 2015, respectively.

Graph 19
GDP: 2006-2015
(Real % change)



Graph 20
DOMESTIC DEMAND: 2006-2015
(Real % change)



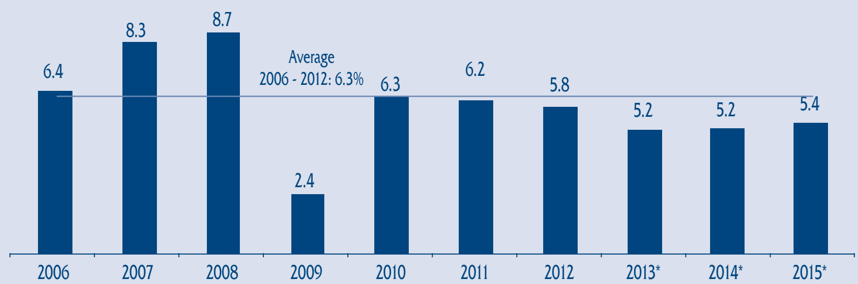
Forecasts on spending components

26. **Domestic demand** showed a slower pace of expansion in Q3-2013 with a rate of 4.4 percent –versus 8.1 and 6.1 percent in Q1 and Q2, respectively. Based on this information and on recent indicators of activity, domestic demand in 2013 has been revised down from a rate of 6.5 percent (September Inflation Report) to 5.8 percent. This decline is explained by the slower growth of private investment, in line with the deterioration of the indicator of investment expectations.

    In 2014 and 2015 domestic demand would grow 6.0 and 6.1 percent, respectively. Private investment is expected to recover the dynamism observed in recent years and to compensate the lower forecast in private spending and exports, the latter of which are expected to recover in a scenario of improvement of global economic activity.

27. Showing a lower dynamism than during the same period of 2012, **private consumption** grew 5.2 percent in the first nine months of the year. The slowdown in consumption is reflected in several indicators, such as INDICCA, the consumer confidence index of Metropolitan Lima, which registered 56 points in December (4 points higher than in November), and consumer loans, which recorded a rate of 11.3 percent in November 2013 (versus 15.9 percent in November 2012).

Graph 21
PRIVATE CONSUMPTION: 2006-2015
(Real % change)

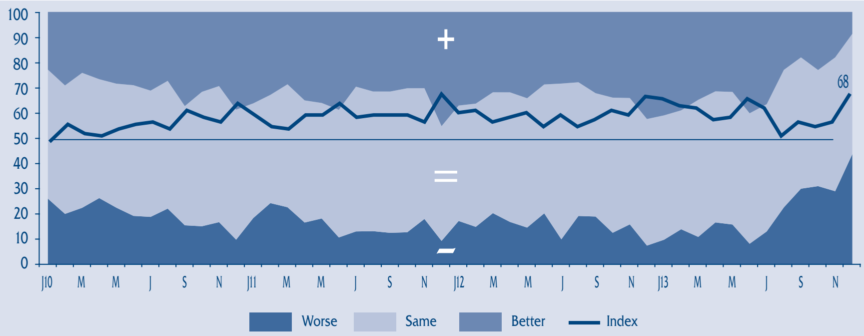


* Forecast.

Other indicators reflecting the recent evolution of private consumption are discussed below:

a. The Consumer Confidence Index showed an optimistic level of 68 points in December. This indicator has maintained a level of 60 points on average during the first three quarters of the year, a slightly higher value than the one recorded in the same period of 2012.

Graph 22
CONSUMER CONFIDENCE INDEX:
HOUSEHOLDS' ECONOMIC SITUATION?



Source: Apoyo.

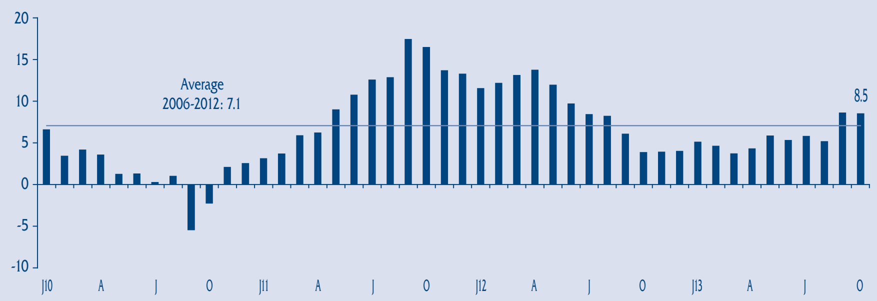
b. The labor force employed grew 2.7 percent in the moving quarter of August-October 2013, showing a higher growth level than the one recorded in the same period of last year (1.7 percent), in line with the average level in 2006-2012 (2.7 percent).

Graph 23
LABOR FORCE EMPLOYED: 2010-2013
(Quarterly moving 12 month % change)

Source: INEI.

c. The main income in Metropolitan Lima grew 8.5 percent in the moving quarter of September-November 2013, a higher level than the one observed in the same period last year (3.9 percent).

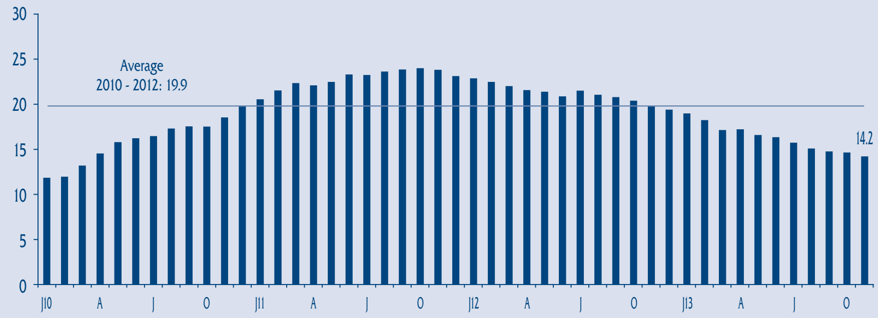
Graph 24
MAIN INCOME IN METROPOLITAN LIMA: 2010 - 2013
(Quarterly moving 12 month % change)



Source: INEI.

d. The growth of credit to individuals, which includes consumer loans and mortgages, continues to moderate compared to the rates observed during 2012. This indicator grew 14.2 percent in November, a lower rate than the average rate observed in the period 2006-2012 (23.4 percent).

Graph 25
CREDIT TO INDIVIDUALS: 2010 - 2013
(12 months % change)



Source: BCRP.

e. The national disposable income in the period of January-September 2013 grew at a rate 2 percentage points lower than during the same period in 2012. In 2013 the national disposable income is expected to show a moderate pace of growth and to record a rate 0.7 percentage points lower than the one estimated in our previous report. Furthermore, the growth forecast of the national disposable income for the next two years has been revised down, in line with the expected evolution of the output.

Table 11
NATIONAL DISPOSABLE INCOME
(Real % change)

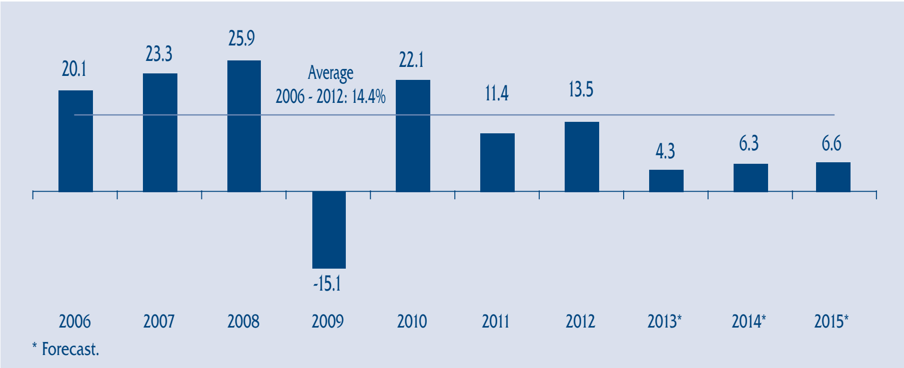
	2012		2013*		2014*	2015*
	Jan-Sep	Year	Jan-Sep	Year		
1. Gross Domestic Product	6.4	6.3	4.9	5.1	6.0	6.5
2. Gross National Product	8.6	8.2	6.1	6.6	6.3	6.3
3. Gross National Income	7.0	6.9	5.0	5.3	6.0	6.5
4. National Disposable Income 1/	**6.8**	**6.6**	**4.8**	**5.1**	**6.1**	**6.4**

* Forecast.
1/ Including factor income, net profits by terms of trade, and net transfers received for non-residents.

28. **Private investment** grew 2.1 percent in Q3 and accumulated a growth rate of 4.8 percent in the first three quarters of the year.

This component of spending reflects a further slowdown so far this year –a growth rate of 4.8 percent (versus a rate of 14.1 percent in the same period in 2012)– and therefore the growth forecast of private investment is revised down to 4.3 percent (from 7.7 percent in our September report). Rates of between 6 and 7 percent are estimated for 2014 and 2015 considering the portfolio of investment projects announced and the expected growth of the economy. Thus, the ratio of private investment to GDP would reach 21.7 percent in 2015, a level not observed since the 1950's.

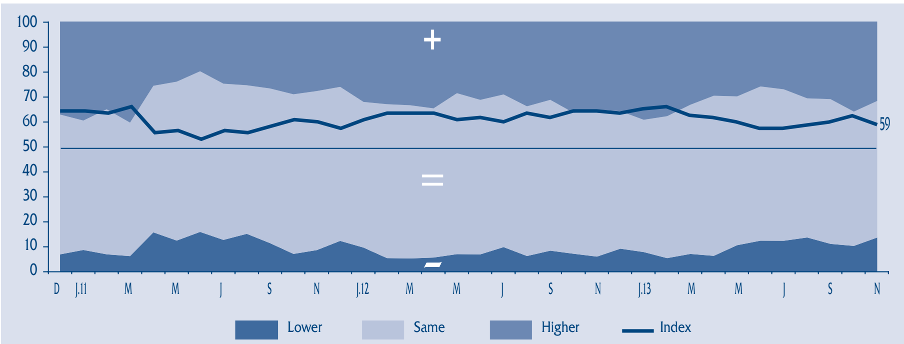
Graph 26
PRIVATE INVESTMENT: 2006 - 2015
(Real % change)



Recent indicators of private investment supporting the forecasts discussed in this report include the following:

a. Expectations about demand in the three months ahead remain on the optimistic segment with a level of 59 points in November (even though this level is lower than the one observed in the previous two months).

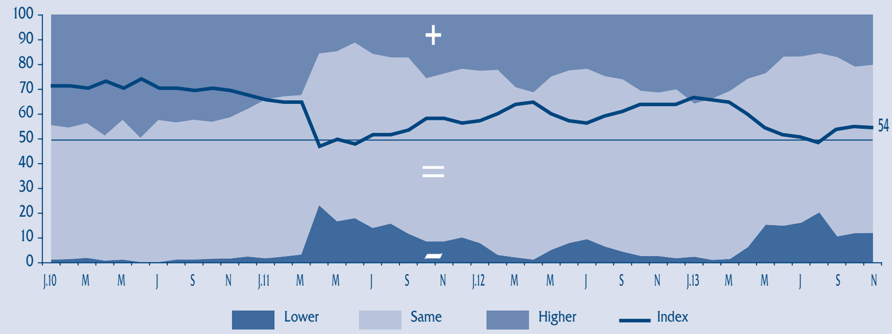
Graph 27
EXPECTATION ABOUT DEMAND IN THE THREE MONTHS AHEAD



Source: Survey of Macroeconomic Expectations, BCRP. Survey conducted during the second fortnight of November 2013.

b. Business expectations on the situation of the economy in the three months ahead declined to 54 points in November, but remain on the optimistic segment.

Graph 28
BUSINESS EXPECTATIONS ON THE SITUATION OF THE ECONOMY IN THE THREE MONTHS AHEAD



Source: Survey of Macroeconomic Expectations, BCRP. Survey conducted during the second fortnight of Novembert2013.

c. Even though economic agents have revised down their expectations about GDP growth, the GDP growth rate is expected to recover in the next years and to register a rate of 5.9 percent on average in 2015.

Table 12
SURVEY ON MACROECONOMIC EXPECTATIONS: GDP GROWTH
(%)

	Expectations about:		
	IR Jun.13	IR Sep.13	IR Dec.13*
Financial entities			
2013	6.0	5.5	5.0
2014	6.0	5.7	5.6
2015	6.0	5.9	5.9
Economic analysts			
2013	6.0	5.5	5.0
2014	6.1	5.8	5.7
2015	6.0	6.0	6.0
Non-financial firms			
2013	6.0	5.5	5.1
2014	6.0	5.6	5.5
2015	6.0	6.0	5.8

IR: Inflation Report.
* Survey conducted during November 30, 2013.

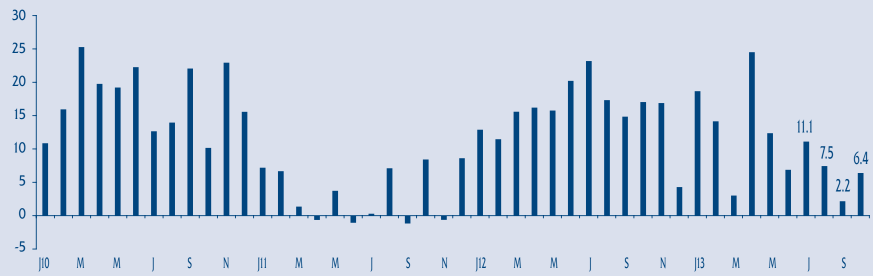
d. The volume of imports of capital goods –indicator of investment demand– showed a rate of 4.6 percent in the period of January-November, a lower rate than the one recorded in the same period last year (12.0 percent).

Graph 29
VOLUME OF IMPORTS OF CAPITAL GOODS: 2010-2013
(12 months % change)

* Preliminary.
Source: SUNAT.

e. The domestic consumption of cement grew at a two-digit rate in the January-October period (10.7 percent).

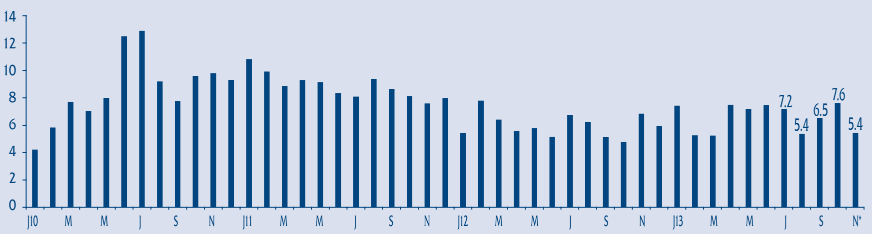
Graph 30
DOMESTIC CONSUMPTION OF CEMENT: 2010-2013
(12 months % change)



Source: ASOCEM and cement companies.

f. The production of electricity continues showing dynamism, with an average growth rate of 6.6 percent in the period January-November (6.0 percent in the same period in 2012).

Graph 31
PRODUCTION OF ELECTRICITY: 2010-2013
(12 months % change)



* Preliminary.
Source: COES.

29. The private investment projects announced to be implemented in 2014-2015 amount to US$ 29 billion, a figure US$ 1.8 billion higher than that of the announced private investment projects considered in our September report.

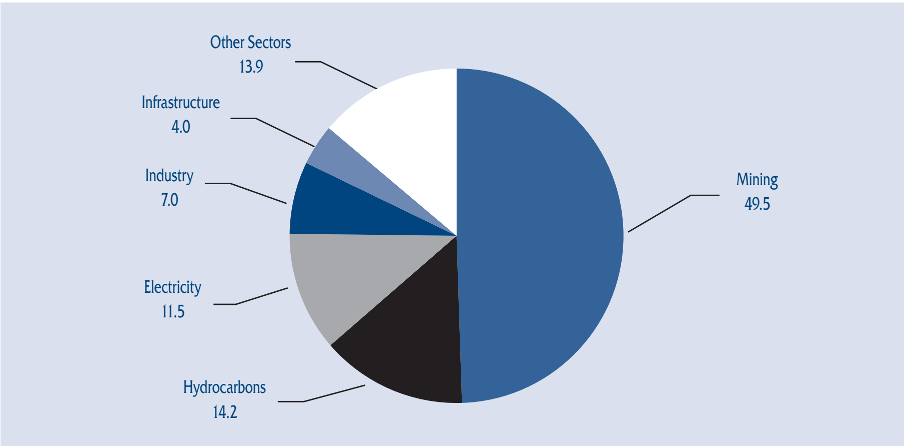
Table 13
PRIVATE INVESTMENT PROJECTS ANNOUNCED
(Million US$)

	2014-2015		
	IR Sep.13	IR Dec.13	Differences
Mining	13,880	14,110	230
Hydrocarbons	3,797	4,036	239
Electricity	2,813	3,293	480
Industry	1,671	1,991	320
Infrastructure	1,133	1,133	0
Other sectors	3,431	3,952	521
Total	**26,725**	**28,515**	**1,790**

IR: Inflation Report.

Projects to be implemented in the sectors of mining and hydrocarbons explain 63.6 percent of the total number of investment projects announced for the period 2014-2015. In the mining sector, projects like Corani and Inmaculada, which already have environmental impact studies (EIS) approved by the Ministry of Energy and Mines, would be carried out with an investment of about US$ 1.1 billion. Moreover, the corporation HudBay Minerals announced that it has increased investment for the Constancia project from US$ 1.5 billion to US$ 1.7 billion. To date, this project has already been implemented by over 50 percent and is expected to be completed in 2014.

Graph 32
FORESEEN INVESTMENT PROJECTS: 2014-2015
(% share)



In the hydrocarbons sector, investments worth pointing out include Pluspetrol's investment of US$ 480 million in the exploration of six new wells in lot 88.

In the electricity sector, Proinversión awarded contracts for the implementation and operation of two thermal power stations that make up the Nodo Energético del Sur and would begin operating in 2017. Samay I, company linked to Kallpa Generación, one of the subsidiaries of the international corporation IC Power in Peru, was awarded the contract for the construction and operation of a 593 MW dual thermal power plant in Mollendo, Arequipa. On the other hand, Enersur was awarded the contract for the implementation and operation of the energy plant that will be located in the province of Ilo, Moquegua, which will have a capacity of around 500 MW. The amount of investment for the implementation of both projects is estimated at around US$ 900 million.

Furthermore, construction projects as well as expansion and remodeling projects continue to be announced in the sectors of real estate, hotels, and health, both in Lima and in the provinces.

Table 14
MAIN INVESTMENT PROJECTS ANNOUNCED: 2013-2015

SECTOR	COMPANIES	PROJECT NAMES
Mining	Xstrata Copper Freeport-Macmoran Copper Antares Minerals Inc. Norsemont Mining Inc. and HudBay Minerals Inc. China Minmetals Corporation and Jiangxi Copper Company Limited Aluminium Corp of China Ltd. (Chinalco) Bear Creek Mining Corporation Cumbres Andinas and Korea Resources Corp. Grupo Milpo Hochschild Mining International Minerals Corporation Anglo American Plc.	Las Bambas Expansion of Cerro Verde Haquira Constancia El Galeno Expansion of Toromocho Corani Mina Justa Expansion of Cerro Lindo and El Porvenir Inmaculada Quellaveco
Hydrocarbons	Savia Perú S.A Repsol YPF Perenco Transportadora de Gas del Perú S.A. Pacific Rubiales Energy Pluspetrol Perú Corp. S.A. Cálidda Gas Natural del Perú Karoon Gas Australia and Vietnam American Petroleum	Lot Z-2B: Perforation, exploration and other investments Exploration of Lot 39 (21 well) Exploration of Lot 67 and pipeline Expansion of gas and capacity of transportation Lots: Z1-135 - 137 - 116 - 138 Exploration of Lots 88 and 56 Expansion of the use of natural gas nationwide Exploitation: Lot Z - 38 (20 well)
Electricity	Odebrecht S.A. Inkia Energy and Quimpac S.A. Energía Azul S.R.L. Kallpa y Enersur	Hydroelectric Power Plant of Cerro de Chaglla Hydroelectric Power Plant of Cerro del Águila Hydroelectric Power Plant of Santa María Energy node in South
Industry	Repsol YPF Vale do Rio Doce Hochschild Mining, Mitsubishi, and Cementos Pacasmayo Grupo Hochschild Siderperú SAB Miller Grupo de Pilkington Limited	Expansion of La Pampilla plant Bayovar II (Expansion) Phospates projects New cemen plant in Piura Modernization of plant Investment 2012-2014 Manufacture plant of float glasses
Infrastructure	OAS S.R.L. APM Terminal, Callao Port Holding and Central Portuaria Covisol Autopista del Norte SAC Odebrecht	Parque Rimac express way Modernization of North Pier Trujillo-Sullana: Sol Highway Pativilca – Port of Salaverry Road Network No. 4 New highways in Lima
Other sectors	Grupo Falabella Graña y Montero Holding Banmédica - Grupo Roe Ingenieros Civiles Asociados Besalco S.A. Inmobiliari S.A Pontificia Universidad Católica del Perú Cinépolis Ingenieros Civiles Asociados Grupo Interbank Grupo Gloria Pesquera Hayduk S.A. Pesquera Exalmar SA Grupo Telefónica América Móvil S.A.B. de C.V. and Telmex Perú S.A. Americatel Perú and Movistar	Expansion and new malls Real state Health center: San Felipe Fleet and equipments Real state Residential, commercial and office center in Surco Expansion: University infrastructure and CC Plaza San Miguel Movie theater in 4D Fleet and equipments Expansion and new malls Casagrande,Cartavio and San Jacinto - Olmos project Modernization and expansion of Paita - Chimbote plant Investment projects Expansion and fiber optics in andean mountain Expansion of infrastructure, capacity and technological innovation Broadband expansion

Source: Press media and business information.

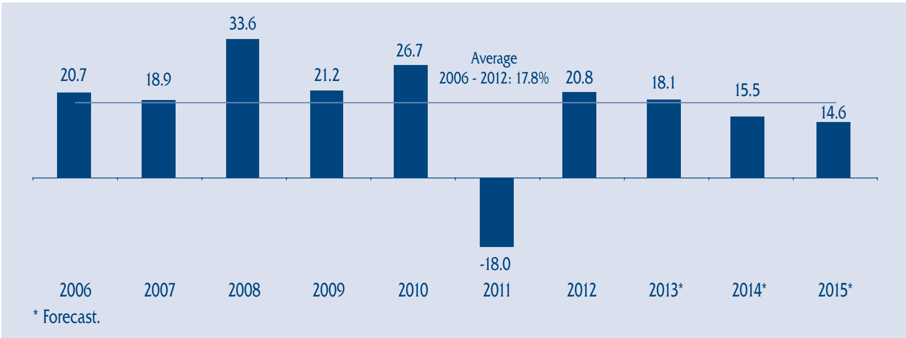
30. Concession contracts involving a total investment of US$ 4.52 billion have been awarded during 2013. The concession of the irrigation project Chavimochic – Stage 3, which will provide irrigation to over 100 thousand hectares in La Libertad was awarded for 25 years to Consorcio Río Santa-Chavimochic (integrated by companies Odebrecht and Graña y Montero) in December. Moreover, the concession contract of the road project Carretera Longitudinal de la Sierra - Section 2 (La Libertad - Cajamarca) was awarded to Consortium Consierra Tramo 2 also in December.

Table 15
INVESTMENT PROJECTS TO BE IMPLEMENTED THROUGH CONCESSIONS IN 2014
(Million US$)

	Estimated investment
Line 2 and Faucett – Gambetta Avenue stretch of Metro Network of Lima and Callao	5,701
Improvement of the Energy Security in the country and development of Gas Pipeline in the South	3,000
New International Airport of Chinchero - Cusco	659
Moyobamba - Iquitos Transmission Line (220 KV)	434
Drinking Water Works for Lima	400
Supply System of LPG for Lima and Callao	260
Supply System of LNG for the domestic market	250
Port Terminal General San Martín	103
Amazon Waterway	74
La Planicie - Industriales Transmission Line (220 kV) and Associated Sub-stations	57
Choquequirao Cable railway	55
Works Regulatory in Chillon River	45
Friaspata - Mollepata Transmission Line (220 kV) and Sub-station Orcotuna	44
Kuelap cable railway	17
Private Sector Provision of Technology Security in Prisons	4
Total Projects	**11,102**

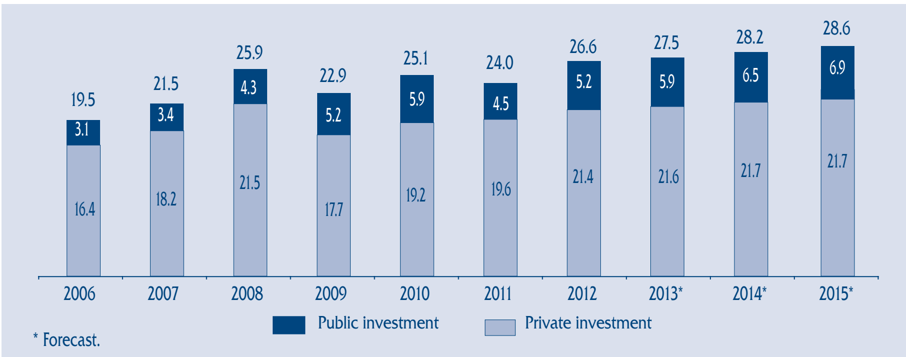
31. **Public investment** accumulated a growth rate of 20.5 percent in January-September, this rate being explained mainly by the higher investment of the local governments and the national government. The most important investments carried out by the national government were associated with road rehabilitation and road improvement and with the project of the Electric Train for Lima and Callao. In line with the investment carried out, public investment would continue to grow in Q4 as well as in 2014 and 2015, showing rates above the average growth rate of GDP.

Graph 33
PUBLIC INVESTMENT: 2006-2015
(Real % change)



32. Considering the evolution of private investment and public investment, the gross investment-to-GDP ratio would be around 28 percent in the forecast horizon. The ratio of fixed gross investment-to-GDP was 22.0 percent on average between 2003 and 2012, which is 3.4 times the growth of the average GDP in this period (6.5 percent). The average investment-to-GDP ratio in the forecast horizon is 28.3 percent, which is compatible with an average GDP growth rate of 5.8 percent.

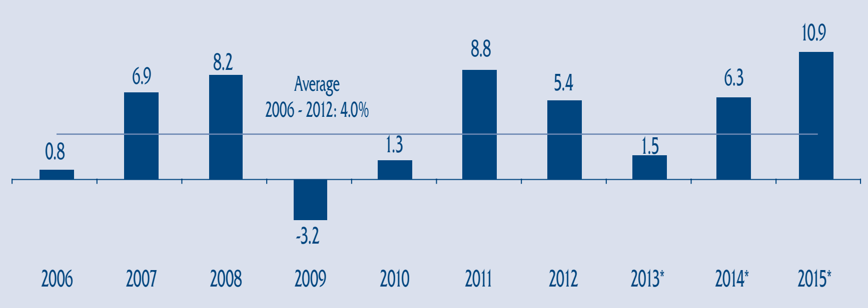
Graph 34
GROSS FIXED INVESTMENT: 2006 - 2015
(% GDP)



33. **Exports of goods and services** recorded a slight increase in Q3 with a rate of 3.6 percent in real terms, due mainly to the recovery registered in terms of the exported volumes of traditional products, such as fishmeal, copper, and zinc. On the other hand, the exports of non-traditional products dropped due to lower shipments of textiles and iron&steel products.

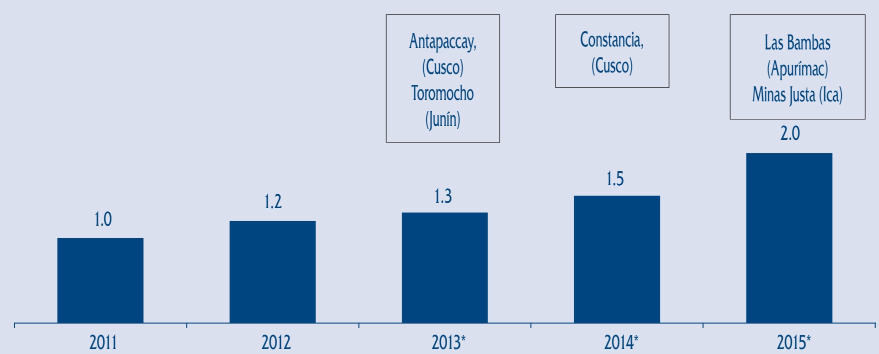
Based on this result, the growth of exports in 2013 is revised up from 0.7 percent in our previous report to 1.5 percent. In line with the trend foreseen in our previous report, the current forecast considers that the growth of exports will show a recovery path in 2014 and 2015 both as a result of the beginning of operations in mining projects such as Toromocho, Las Bambas, and Constancia and of the recovery foreseen in the global demand for non-traditional products.

Graph 35
EXPORTS OF GOODS AND SERVICES : 2006-2015
(Real % change)



* Forecast.

Graph 36
COPPER PRODUCTION
(Million FMT)

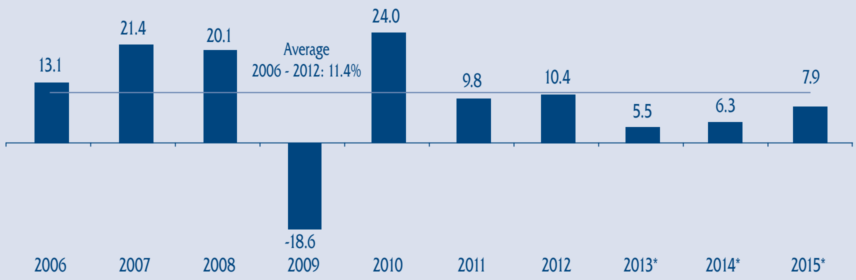


* Forecast.

34. **Imports** of goods and services grew 3.8 percent in Q3, recording a lower rate than in Q1 and in Q2 (8.7 and 7.8 percent, respectively) due to lower imports of capital goods and non-financial services as well as due to the effect of depreciation. Because of the moderation of the pace of GDP growth, the forecast on the growth of imports in 2013 has been revised down from 6.3 percent (Inflation Report of September) to 5.5 percent. In the forecast horizon,

imports are expected to grow at lower rates than the average growth rate in the last 6 years, in line with the slowdown registered in the growth of domestic demand.

Graph 37
IMPORTS OF GOODS AND SERVICES: 2006-2015
(Real % change)



* Forecast.

GDP by production sectors

35. Between January and September 2013, GDP accumulated a growth rate of 4.9 percent. This result reflects the greater dynamism of non-primary sectors, such as construction, trade and services, which grew at rates of between 5.5 and 10.5 percent. On the other hand, the primary sectors showed a slower pace of growth than in the same period of 2012 and registered a rate of 1.8 percent (2.7 percent in January-September 2012).

The slowdown in the GDP growth rate observed between 2012 (6.3 percent) and 2013 (5.1 percent) is explained mainly by the slowdown of activity in the sectors of agriculture, construction, and trade. The decline of activity in the agriculture sector, which accounts for 0.3 percentage points of this fall, is explained by unfavorable weather conditions given that the episode of cold temperatures of 2013 had a negative impact on agricultural production. On the other hand, the slowdown in the construction sector –from 15.1 percent in 2012 to 9.0 percent in 2013–, which accounts for 0.4 percentage points of the fall of GDP growth, was associated with the slowdown of domestic consumption of cement and with a lower dynamism of self-construction.

Metal mining had a slower growth due to technical problems and strikes, which are estimated to have had an impact of -0.1 percentage points of GDP growth.

Table 16
GROSS DOMESTIC PRODUCT BY ECONOMIC SECTORS
(Real % change)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
Agriculture and livestock	**5.7**	**5.7**	**1.7**	**2.4**	**1.9**	**4.2**	**3.0**	**4.2**	**4.2**
Agriculture	5.2	5.6	1.3	1.7	1.7	4.0	2.6	4.0	4.0
Livestock	6.4	5.9	2.1	3.3	2.2	4.4	3.7	4.7	4.7
Fishing	**-7.5**	**-11.7**	**0.3**	**5.0**	**8.3**	**3.0**	**6.6**	**3.3**	**3.3**
Mining and hydrocarbons	**3.7**	**2.2**	**1.7**	**3.1**	**2.4**	**11.4**	**9.4**	**13.4**	**13.3**
Metallic mining	3.9	2.2	0.7	2.0	1.6	11.6	9.1	13.0	13.0
Hydrocarbons	3.1	2.3	6.3	8.5	6.1	10.5	10.8	15.2	14.8
Manufacturing	**1.2**	**1.5**	**1.5**	**2.9**	**2.3**	**4.6**	**4.1**	**5.5**	**5.1**
Based on raw materials	-6.0	-6.2	3.0	4.7	5.5	3.0	3.5	3.3	3.4
Non-primary industries	2.5	2.9	1.3	2.5	1.7	4.9	4.3	6.0	5.5
Electricity and water	**5.4**	**5.2**	**5.6**	**5.7**	**5.6**	**6.1**	**6.1**	**6.1**	**6.1**
Construction	**16.2**	**15.1**	**10.5**	**11.0**	**9.0**	**8.3**	**7.3**	**8.0**	**8.0**
Commerce	**6.8**	**6.7**	**5.5**	**5.7**	**5.6**	**5.9**	**5.9**	**6.4**	**6.3**
Other services	**7.2**	**7.1**	**5.9**	**6.0**	**5.9**	**6.2**	**6.2**	**6.6**	**6.5**
GDP	**6.4**	**6.3**	**4.9**	**5.5**	**5.1**	**6.2**	**6.0**	**6.7**	**6.5**
Memo:									
Primary GDP	**2.7**	**2.0**	**1.8**	**3.1**	**2.8**	**6.3**	**5.2**	**7.1**	**7.1**
Non-Primary GDP	**7.1**	**7.0**	**5.4**	**5.9**	**5.4**	**6.1**	**6.1**	**6.6**	**6.4**

IR: Inflation Report.
* Forecast.

36. The forecast on the growth rate of **primary GDP** in 2013 has been revised down from 3.1 percent (estimated in our previous report) to 2.8 percent due to the lower growth rate of the sectors of agriculture and mining. However, the pace of growth of the primary GDP in the following years is expected to accelerate, in line with the onset of operations of new mining and hydrocarbons projects.

The **agricultural sector** would grow 1.9 percent in real terms due to the increased supply of agricultural and livestock products oriented to the domestic market, especially greater volumes of rice, cassava, onion, and garlic, as well as larger volumes of livestock products, such as poultry and eggs.

In 2014 and 2015, with better weather conditions after the cold event in 2013, the production of the main agricultural products –i.e. rice, potatoes, cassava, and banana– would recover; the effect of yellow rust in coffee would be offset with the application of sanitary measures, and the production of olives would increase in 2014 as a result of a cycle of favorable yields. The livestock production would also increase with the recovery of domestic demand and the areas cultivated with grapes, avocado, mango and sugar cane for the production of ethanol are also expected to increase.

As regards the **fishing sector**, the growth forecast of this sector in 2013 has been revised up from 5.0 percent to 8.3 percent due mainly due to the upward revision of fishing for human consumption and to the higher quota of anchovy established for the period November 2013-January 2014 (2.3 million tons).

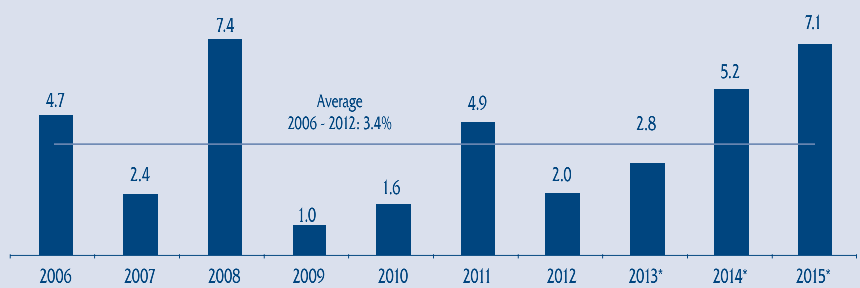
Between January and September of 2013, the **metal mining sector** grew 0.7 percent. This rate is explained by the greater extraction of copper after the beginning of production at Antapaccay in November 2012, which was partially offset by a lower production of gold and zinc. As a result of this, the projected growth of this sector in 2013 has been revised slightly down compared to our previous Inflation Report (down by 0.4 percentage points). An increase in production is foreseen for 2014 and 2015, mainly in copper production due to the onset of operations of important projects such as Toromocho, Constancia, and Las Bambas.

Table 17
MINING PRODUCTION
(%)

	2013*	2014*	2015*
Gold	-6.9	1.4	0.7
Copper	7.8	17.3	30.7
Zinc	5.1	4.8	4.3

* Forecast.

Graph 38
PRODUCTION IN PRIMARY SECTORS: 2006-2015
(Real % change)

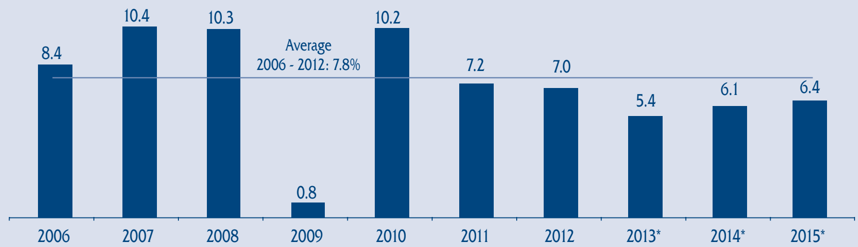


* Forecast.

37. Lower growth is foreseen in the **non-primary GDP** in 2013, in line with the lower growth expected in domestic demand. A slight decline is estimated in the growth rates in 2014 and 2015 –6.1 percent and 6.4 percent, respectively– compared to the rates estimated in our previous report. As regards non-primary manufacturing, its growth would be associated with the greater growth of the world economy

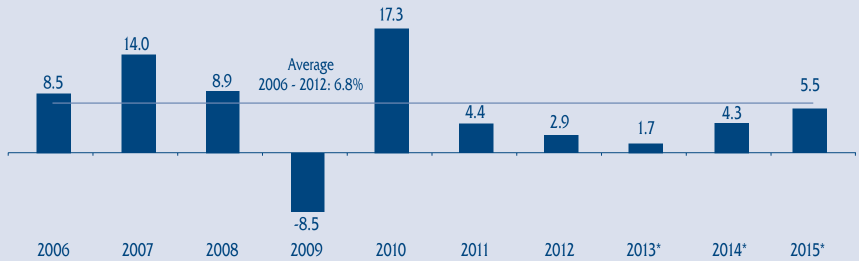
and therefore to an increase in exports of non-traditional manufacturing products, as well as with greater domestic demand for consumer goods associated with income increases. On its side, the construction sector would continue to grow supported by the construction of housing projects, shopping malls, road and public infrastructure works, both in Lima and in the rest of the country, but showing more moderate rates.

Graph 39
PRODUCTION IN NON-PRIMARY SECTORS: 2006-2015
(Real % change)



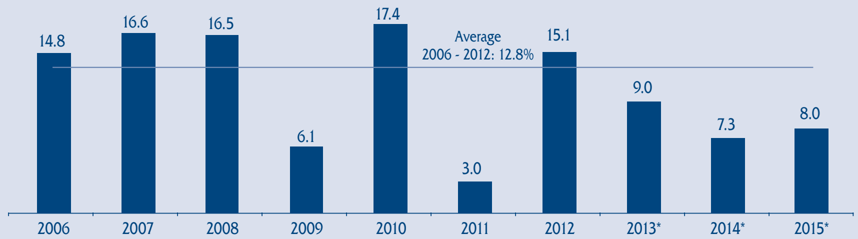
* Forecast.

Graph 40
NON-PRIMARY MANUFACTURING: 2006-2015
(Real % change)



* Forecast.

Graph 41
CONSTRUCTION: 2006-2015
(Real % change)



* Forecast.

Box 2

COMPETITIVENESS AND BUSINESS CLIMATE IN PERU

The growth of income per capita in Peru between 2000 and 2012 (4.6 percent), which more than doubled the growth of GDP per capita in the world (2.2 percent), has led Peru to rank 34th among 170 countries in terms of the growth of per capita income during this period. However, since Peru is still an average-income economy –which ranks 77th among 170 countries in terms of GDP per capita–, the sustainability of its long-term growth is a necessary condition for the economic development of the country.

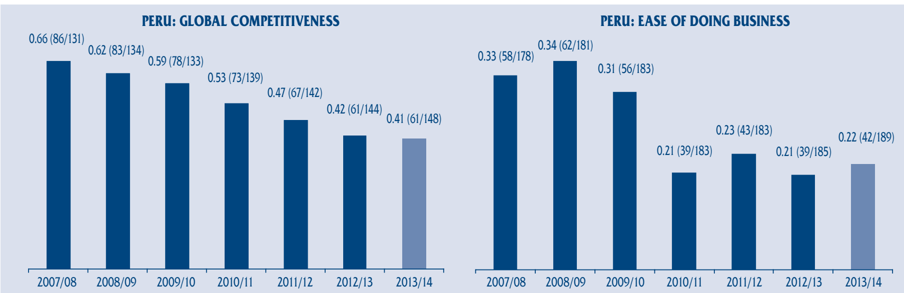
Economic literature suggests that the growth of total factor productivity (TFP) is the main source of a country's sustained economic growth. A competitive economy with a business climate that contributes to an efficient allocation of resources provides the conditions required for the sustained growth of TFP. Therefore, monitoring the international indicators that measure **competitiveness and the business climate** is a useful tool to design and improve growth policies.

Peru: Competitiveness and business environment

The World Economic Forum (WEF) defines competitiveness as a set of institutions, policies and factors that determine a country's level of productivity. In addition, the World Bank (WB) defines the business environment or business climate as the set of institutional factors that shape the incentives conducive to private investment in socially desirable projects.

The WEF's Global Competitiveness Report 2013-2014 ranks Peru in position 61 in a world ranking of 148 countries; in other words, the country is still among the top half of countries in terms of competitiveness, although there has been no improvement in the position Peru holds in this ranking compared to the one it held in the previous year. Moreover, the World Bank's Doing Business 2014 report ranked Peru in position 42 in a ranking of 189 countries, which means that the country is within the upper third of countries worldwide in terms of business climate, even though it has fallen three positions in comparison to the previous year. Thus, despite the progress Peru has made in both rankings in recent years, it has not made any significant improvement in its ranking compared to the previous year.

PERU: GLOBAL COMPETITIVENESS INDEX AND EASE OF DOING BUSINESS INDEX
(Percentile, Relative position)



Memo: The percentile (between number of countries since) summarizes the relative location of the country and corrects the effect of the variation of number of countries in the annual ranking, a lower value in the percentile implies a better location . The information shows the general location of Peru issued by the relevant annual report, except reports 2012/2013 that considered a methodological changes-year adjustments in the recent reports.
Source: Global Competitiveness Report and Doing Business, various issues.

On the other hand, Peru shows mixed results in terms of the WEF's **global competitiveness index**. The country stands out mainly due to its positive performance in 2 of the 12 pillars analyzed: macroeconomic stability (position 20) and sophistication of the financial market (position 40). However, it shows a poor performance in one-third of the pillars (4): innovation (position 122), institutions (position 109), health and primary education (position 95), and infrastructure (position 91).

PERU: GLOBAL COMPETITIVENESS INDEX

Global Competitiveness Index	2012-13	2013-14	Improvement
(General location)	**61**	**61**	**0**
A. Basic requirements	**69**	**72**	**-3**
1. Institutions	105	109	-4
2. Infrastructure	89	91	-2
3. Macroeconomic environment	21	20	1
4. Health and primary education	91	95	-4
B. Reinforcements to the efficiency	**57**	**57**	**0**
5. Higher education and training	80	86	-6
6. Goods market efficiency	53	52	1
7. Labor market efficiency	45	48	-3
8. Financial market development	45	40	5
9. Technological readiness	83	86	-3
10. Market size	45	43	2
C. Factors of innovation and sophistication	**94**	**97**	**-3**
11. Business sophistication	68	74	-6
12. Innovation	117	122	-5

Source: Global Competitiveness Report, various issues.

In comparison to the previous year, the country's recoil in 67 percent of the pillars analyzed (8 of 12) stands out negatively. This is particularly noteworthy because this recoil is more clearly observed in the 4 pillars where Peru shows its worse relative performance.

Peru also shows mixed results in the World Bank's **Ease of doing business index**. The country is ranked in the top quintile worldwide in 3 of the 10 analyzed areas: protecting investors (rank 16), registering property (rank 22), and getting credit (rank 28). However, the country still lags behind internationally in half of the analyzed areas (5): paying taxes (rank 73), getting electricity (rank 79), enforcing contracts (rank 105), resolving insolvency (rank 110), and dealing with construction permits (rank 117).

PERU: EASE OF DOING BUSINESS INDEX

Index on the ease of Doing Business	2012-13	2013-14	Improvement
(General location)	**39**	**42**	**-3**
Protecting investors	16	16	0
Registering property	19	22	-3
Getting credit	24	28	-4
Trading across borders	49	55	-6
Starting a business	60	63	-3
Paying taxes	76	73	3
Getting electricity	78	79	-1
Enforcing contracts	108	105	3
Resolving insolvency	108	110	-2
Dealing with construction permits	97	117	-20

Source: Doing Business Report, various issues.

In comparison to the previous year, the recoil of Peru in 70 percent of the monitored areas stands out in a negative manner, especially in the case of the decline of 20 positions in the indicator of construction permits due to the increase of the costs of construction permits for industrial facilities associated with the increase in the price of land.

Final considerations

Although competitiveness and the business climate in the country have improved over the past years, in line with the economic growth of this country in the last decade, i) no significant improvements have been achieved in terms of competitiveness and business climate in the last year; (ii) Peru still lags behind in several key components required to sustain long-term growth.

In a dynamic global environment in which reforms are implemented in other countries to improve productivity, Peru has to speed up the pace in the implementation of the structural reforms needed to provide the appropriate conditions required for sustained economic growth.

Recent public policies oriented toward this goal include the actions taken by PROINVERSION, Consejo Nacional de la Competitividad, and Equipo Especializado de Seguimiento de la Inversión. The measures and regulations promoted by these entities attached to the MEF have focused on the implementation of concession contracts to carry out infrastructure projects; the improvement of competitiveness strategic lines, such as innovation and technology; the reinforcement of the system aimed at eliminating bureaucratic barriers, and the simplification of administrative procedures.

However, there is still a big challenge ahead in the structural reforms that are still pending. Among others, some of the areas that should be given particular attention include aspects such as infrastructure (e.g. transportation and energy), institutions (e.g. public and legal security), human capital (e.g. quality of education and access to health services), and business regulations (e.g. construction permits, recruitment, payment of taxes, and business closure).

III. Balance of Payments

38. In the period January-September, the current account of the balance of payments recorded a deficit equivalent to 5.4 percent of GDP –2 percentage points higher than the one recorded in the same period of 2012–, in a context in which domestic demand grew at higher rates than the output and a decline was registered in the terms trade. In this period the deficit was financed by long-term capital inflows (US$ 18.3 billion) –a higher flow than the one recorded in the first three quarters of 2012– oriented mainly to investment projects

This larger current account deficit than the one projected for 2013 is explained by lower export prices.

Table 18
BALANCE OF PAYMENTS
(Million US$)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
I. CURRENT ACCOUNT BALANCE	**-4,929**	**-6,842**	**-8,328**	**-10,249**	**-10,098**	**-10,317**	**-10,126**	**-10,134**	**-10,080**
% GDP	*-3.4*	*-3.4*	*-5.4*	*-4.9*	*-4.9*	*-4.6*	*-4.6*	*-4.1*	*-4.2*
1. Trade balance	3,874	4,821	-578	-666	-396	310	40	2,149	1,700
a. Exports	34,465	45,933	31,311	41,877	41,780	45,732	43,114	51,977	48,427
b. Imports	-30,591	-41,113	-31,888	-42,543	-42,176	-45,422	-43,074	-49,828	-46,727
2. Services	-1,619	-2,258	-1,450	-2,375	-2,135	-3,162	-2,977	-3,613	-3,318
3. Investment income	-9,638	-12,701	-8,704	-10,334	-10,734	-10,993	-10,752	-12,339	-12,118
4. Current transfers	2,453	3,296	2,404	3,126	3,166	3,528	3,563	3,669	3,656
Of which: Remittances	2,071	2,788	2,003	2,651	2,659	2,991	2,993	3,106	3,094
II. FINANCIAL ACCOUNT	**16,891**	**21,669**	**12,315**	**13,958**	**13,977**	**11,817**	**11,126**	**11,634**	**11,580**
1. Private Sector	15,289	20,335	12,928	14,376	14,688	11,269	10,935	10,917	10,873
a. Long term	13,233	16,236	15,353	15,383	16,772	10,744	10,410	10,916	10,873
b. Short term 1/	2,056	4,099	-2,425	-1,007	-2,084	525	525	0	0
2. Public Sector 2/	1,602	1,334	-613	-418	-710	548	191	718	707
III. BALANCE OF PAYMENTS (=I+II)	**11,962**	**14,827**	**3,988**	**3,709**	**3,879**	**1,500**	**1,000**	**1,500**	**1,500**
Memo:									
Long-term private capital inflow 3/	15,469	20,914	18,255	20,982	21,343	16,150	14,306	15,578	14,920
GDP (Billion US$)	147	200	155	209	208	224	222	244	241

1/ Includes net erros and omissions.
2/ Includes exceptional financing.
3/ Includes net foreign investments, portfolio investment and private sector's long-term disbursement.
IR: Inflation Report.
* Forecast.

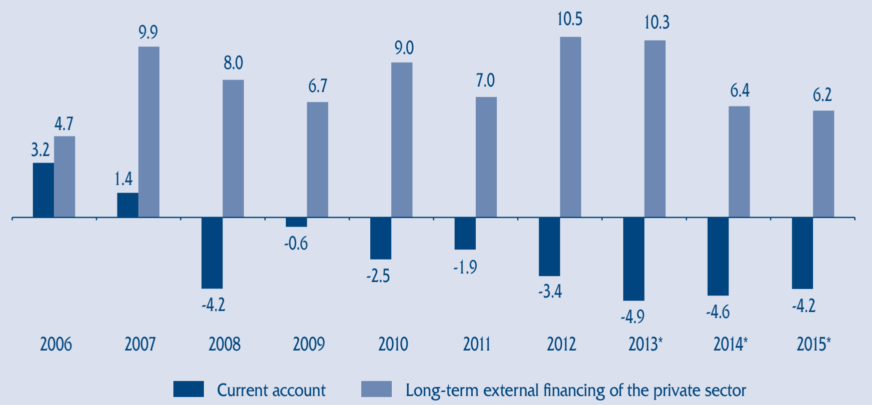
39. The increase in the current account deficit of 2013 is also explained by the growth of investment that contributes to capital stock in the economy, which was financed in part by domestic savings. Higher levels of domestic savings that would offset lower expected foreign savings are expected in the next few years.

Table 19
SAVINGS-INVESTMENT GAP
(% GDP)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
1. Gross fixed investment	**26.5**	**26.6**	**27.5**	**28.0**	**27.5**	**29.0**	**28.2**	**29.8**	**28.6**
2. Net domestic savings 1/	**23.1**	**23.1**	**22.1**	**23.1**	**22.7**	**24.4**	**23.6**	**25.6**	**24.5**
3. External savings	**3.4**	**3.4**	**5.4**	**4.9**	**4.9**	**4.6**	**4.6**	**4.1**	**4.2**

1/ Excluding inventory variations.
IR: inflation report.
*Forecast.

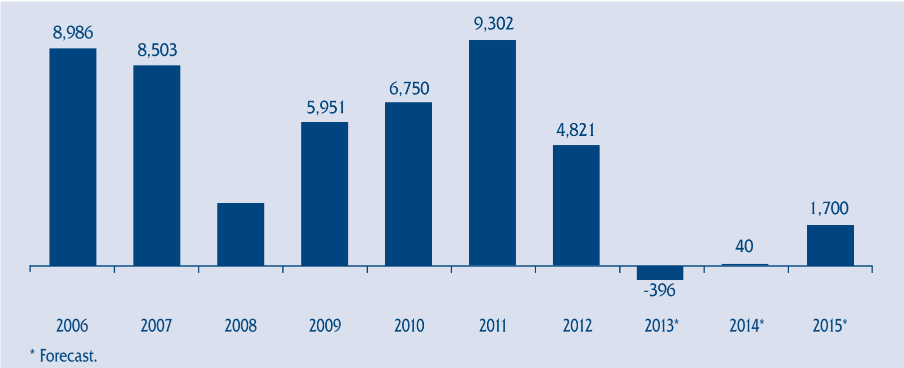
Graph 42
CURRENT ACCOUNT AND LONG-TERM EXTERNAL FINANCING OF THE PRIVATE SECTOR: 2006-2015 1/
(% GDP)



1/ Includes net foreign investments, portfolio investment and private sector's long-term disbursement.
* Forecast.

40. A current account deficit of 4.6 percent of GDP is estimated for 2014, while a deficit on current account of 4.2 percent of GDP is projected for 2015 in a context of almost no growth in the terms of trade. The declining path of the deficit considers the recovery of external demand as well as the onset of operation of mining projects in 2014 and 2015 (Toromocho, Las Bambas, and Constancia).

Graph 43
TRADE BALANCE: 2006-2015
(Million US$)



Terms of trade and prices of commodities

41. After the slight recovery registered in Q3, commodities resumed the downward trend although at lower rates than the ones observed early in the year. It is estimated that in 2013 the terms of trade would drop 4.7 percent: the decline of 7.3 percent in export prices would be in part offset by the decrease of import prices (2.8 percent).

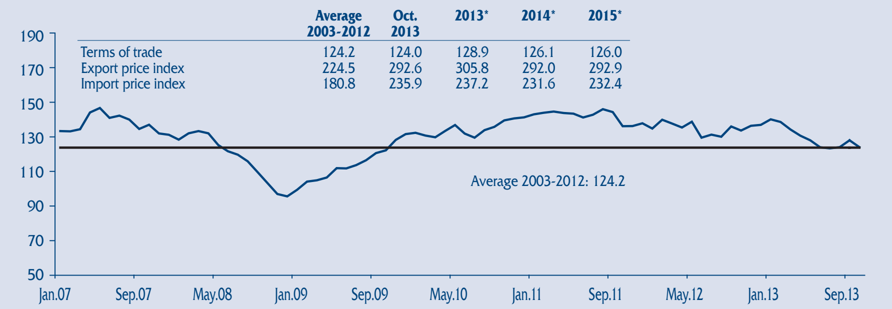
Table 20
TERMS OF TRADE: 2011 - 2015
(Annual average data)

	2011	2012		2013*			2014*		2015*	
	Year	Jan.-Oct.	Year	Jan.-Oct.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
Terms of trade	**5.4**	**-5.8**	**-5.0**	**-3.9**	**-4.5**	**-4.7**	**-1.6**	**-2.2**	**0.1**	**-0.1**
Price of exports	**20.0**	**-4.1**	**-3.3**	**-6.2**	**-6.2**	**-7.3**	**-1.9**	**-4.5**	**0.9**	**0.3**
Copper (US$ cents per pound)	400	362	361	334	333	333	330	330	330	330
Zinc (US$ cents per pound)	100	88	88	87	87	87	89	90	92	90
Lead (US$ cents per pound)	109	92	94	97	98	97	99	97	101	99
Gold (US$ per ounce)	1,570	1,663	1,670	1,443	1,420	1,414	1,330	1,250	1,330	1,250
Price of imports	**13.8**	**1.8**	**1.7**	**-2.4**	**-1.8**	**-2.8**	**-0.3**	**-2.4**	**0.8**	**0.4**
Oil (US$ per barrel)	95	95	94	98	100	98	97	93	90	89
Wheat (US$ per ton)	280	269	276	268	265	267	245	258	246	262
Maize (US$ per ton)	262	271	273	250	241	235	195	174	198	180
Soybean oil (US$ per ton)	1,191	1,144	1,125	1,021	1,015	998	967	920	972	933

* Forecast.
IR: Inflation Report.

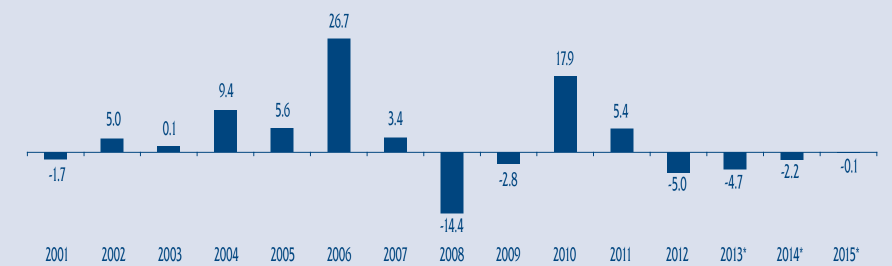
In general terms, the fall in commodity prices in recent months was offset by the stabilization of growth in China and by a decline of risk aversion after a fiscal agreement was reached in the USA in October. The growth of developed economies also provided support to the demand for commodities. In the case of gold, the decrease in the price of this metal is explained by expectations that the dollar will strengthen given that the tapering of monetary stimulus is expected to begin soon. In 2014 the terms of trade would decline by 2.2 percent and in 2015 they would fall slightly (0.1 percent).

Graph 44
EXPORT AND IMPORT PRICE INDICES AND TERMS OF TRADE: JANUARY 2007 - OCTOBER 2013 (1994=100)



* Forecast.

Graph 45
TERMS OF TRADE: 2001-2015
(% change)



* Forecast.

Copper

42. In the last three months, the price of **copper** has slowed down its downward trend and gone from US$ 3.26 per pound in August to US$ 3.20 per pound in November, recording a fall of 1.6 percent. With this, the price of copper accumulates a drop of 11.1 percent in the year.

The price fall was supported by the confirmation of a global surplus supply of copper concentrates in 2013 after three years of deficits. The world's ten largest mining companies recorded an increase in their production with two-digit annual growth rates since Q1-2013 and unplanned stoppages of mine operations have dropped to their lowest level since 2004. However, the abundance of copper has not translated into a similar higher production of refined copper since this production has not increased at the same pace, especially in China.

Table 21
REFINED COPPER: DEMAND AND SUPPLY
(Thousand metric tons)

	2008	2009	2010	2011	2012	2013*	2014*
World mine production	15,571	15,934	16,054	16,079	16,698	17,775	18,579
World refined production (Primary+Secondary)	18,214	18,248	18,981	19,596	20,129	20,912	22,061
World refined usage	18,053	18,070	19,346	19,830	20,550	20,525	21,429
Refined balance 1/	161	178	-365	-234	-421	387	681
Stock inventories 2/	1,102	1,376	1,199	1,205	1,406	1,575	---
Consumption days	22.3	27.8	22.6	22.2	25.0	28.0	---

* Forecast.
1/ Not includes unreported inventories for China apparent usage.
2/ Inventories at the endof period, 2013 corresponds to August.
Source: ICSG.

A slight reduction is expected in the price of copper in the forecast horizon due to the increased supply foreseen in the next years, which would be in part offset by the global economic recovery expected next year. In line with these developments, it is estimated that in the forecast horizon prices would maintain the slightly downward trend that was considered in our previous Inflation Report.

Graph 46
COPPER: JANUARY 2007 - DECEMBER 2015
(ctv. US$/pd.)

Zinc

43. In the last three months, the mean price of **zinc** has declined 1.2 percent and reached an average monthly price of US$. 0.85 per pound. Thus, year-to-day this price accumulates a decrease of 8.2 percent.

This decrease reflects good supply conditions in the world market, especially a high level of inventories. The latest data available at September[2] show that the market continues recording a global surplus despite the closure of some mines (particularly in Canada and Australia) which have reached the end of their useful life. However, a reduction is projected in the supply surplus of zinc in the next few years due to the closure of other important mines, which together with the recovery of demand, would give support to the price of this metal. Thus, in the forecast horizon the international price of zinc is expected to remain within the levels estimated in our September Inflation Report.

Table 22
REFINED ZINC: SUPPLY AND DEMAND
(Million metric tons)

	2008	2009	2010	2011	2012	2013*
World mine production	11.88	11.62	12.39	12.66	13.14	12.95
World refined production	11.77	11.28	12.90	13.08	12.59	13.01
World refined usage	11.57	10.92	12.65	12.71	12.34	12.96
Refined balance (thousands)	200	366	247	374	254	51

* Forecast.
Source: ILZSG.

Graph 47
ZINC: JANUARY 2007 - DECEMBER 2015
(ctv. US$/pd.)

Gold

44. The price of **gold** dropped 5.3 percent in the last three months, from US$ 1,347 per troy ounce in August to US$ 1,276 per troy ounce in November. With this, the price of gold accumulates a drop of 24.2 percent so far this year.

2 According to the International Zinc and Lead Study Group (IZLSG).

The price of gold continued showing a downward path, but recording a pace of slowdown than in the first half of the year, supported by the decline of world demand associated mainly with the retrenchment of investment. The World Gold Council reported that the lower demand for gold was mainly associated with the exchange-traded funds' net redemptions of their gold positions.

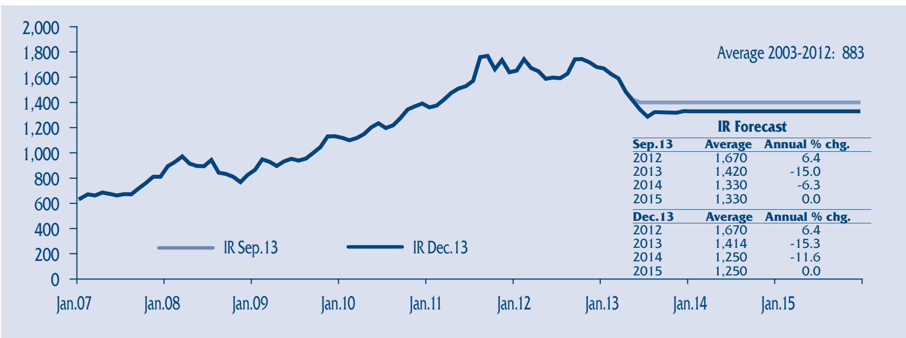
Table 23
GOLD: SUPPLY AND DEMAND
(Tons)

	2010	2011	2012	Q4.12	Q1.13	Q2.13	Q3.13
World mine production	2,635	2,850	2,824	713	671	718	760
Gold recycling	1,711	1,649	1,591	386	359	303	385
Total supply	**4,346**	**4,499**	**4,415**	**1,099**	**1,030**	**1,021**	**1,146**
Jewellery	2,020	1,975	1,896	483	522	617	475
Technology	465	452	407	96	102	104	103
Investment	1,600	1,704	1,535	425	240	129	186
Central banks 1/	77	457	544	150	124	79	93
Gold demand	**4,163**	**4,587**	**4,383**	**1,155**	**989**	**929**	**857**
OTC investments and stock flows 2/	183	-88	32	-56	41	91	289
Total demand	**4,346**	**4,499**	**4,415**	**1,099**	**1,030**	**1,021**	**1,145**
Market balance	**0**	**0**	**0**	**0**	**0**	**0**	**0**

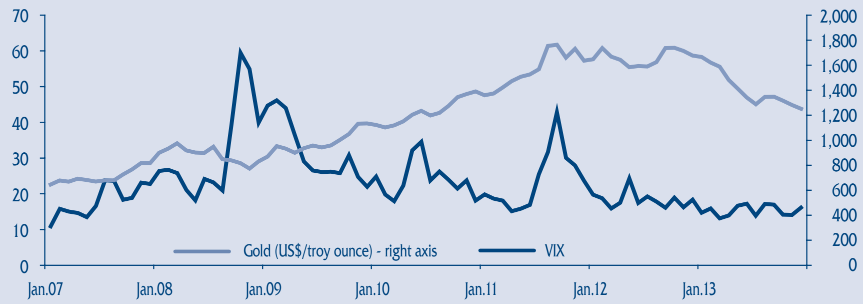
1/ Net purchases.
2/ OTC- Over The Counter.
Source: World Gold Council.

Pressures would continue to be seen in the following months due to the probability that the dollar will appreciate after the Fed starts withdrawing monetary stimulus (which would strengthen the dollar) and due to the lower demand for hedge assets resulting from a preference for other high-risk instruments, such as the stock exchange markets. In this context, it is estimated that the price of gold would decrease slightly in the forecast horizon.

Graph 48
GOLD: JANUARY 2007 - DECEMBER 2015
(US$/tr.oz.)



Graph 49
GOLD PRICE AND VIX INDEX S&P-500
(January 2007 - December 2013)



Source: Bloomberg.

Trade balance

45. The deficit in the **trade balance** for 2013 has been revised downwards from US$ 666 million (Inflation Report of September) to a US$ 396 million, taking into account the higher balance of exports between January and October as well as the lower growth of imports due to the slowdown of economic activity.

Table 24
TRADE BALANCE
(Million US$)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
Exports	**34,465**	**45,933**	**31,311**	**41,877**	**41,780**	**45,732**	**43,114**	**51,977**	**48,427**
Of which:									
Traditional products	26,068	34,523	23,256	30,699	30,803	33,674	31,653	38,739	35,997
Non-traditional products	8,145	11,066	7,856	10,860	10,730	11,726	11,204	12,879	12,154
Imports	**30,591**	**41,113**	**31,888**	**42,543**	**42,176**	**45,422**	**43,074**	**49,828**	**46,727**
Of which:									
Consumer goods	5,957	8,247	6,491	8,778	8,797	9,719	9,287	11,220	10,681
Inputs	14,400	19,256	14,621	19,583	18,931	20,249	18,584	21,882	20,059
Capital goods	10,056	13,356	10,422	13,958	13,745	15,095	14,159	16,356	14,918
TRADE BALANCE	**3,874**	**4,821**	**-578**	**-666**	**-396**	**310**	**40**	**2,149**	**1,700**

IR: Inflation Report.
* Forecast.

Using the index of export prices of the previous year as reference and the volume of exports projected for this year, the negative impact of the lower prices of export on exports in 2013 is estimated at US$ 3.3 billion.

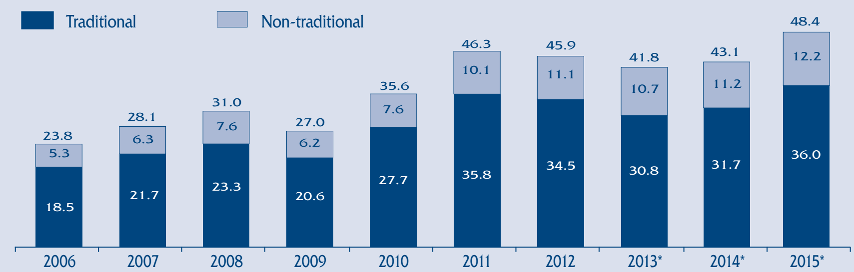
46. The projection of **exports** in 2013 has been revised slightly down to nearly US$ 42 billion, which represents a reduction of 9.0 percent compared to 2012. This revision on the downside compared to our previous estimate reflects mainly the lower prices of exports. The volume of exports in 2013 would fall 1.8 percent due to lower exports of both traditional products (0.9 percent) and non-traditional products (-1.2 percent).

Table 25
TRADE BALANCE
(% change)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
1. Value:									
Exports	-1.8	-0.7	-9.2	-8.2	-9.0	9.2	3.2	13.7	12.3
Traditional products	-5.2	-4.4	-10.8	-10.4	-10.1	9.7	2.8	15.0	13.7
Non-traditional products	10.5	9.2	-3.5	-1.7	-3.0	8.0	4.4	9.8	8.5
Imports	11.4	11.2	4.2	3.5	2.6	6.8	2.1	9.7	8.5
2. Volume:									
Exports	3.2	2.9	-3.3	-2.2	-1.8	11.3	8.0	12.7	12.0
Traditional products	1.7	1.3	-3.6	-2.4	-0.9	14.3	9.4	15.5	14.5
Non-traditional products	9.3	9.2	-1.8	-1.2	-1.2	5.7	3.1	6.6	6.2
Imports	9.9	9.5	6.6	5.4	5.5	7.1	4.6	8.8	8.1
3. Price:									
Exports	-4.6	-3.3	-5.7	-6.2	-7.3	-1.9	-4.5	0.9	0.3
Traditional products	-6.4	-4.6	-7.0	-8.2	-9.2	-4.0	-6.1	-0.4	-0.7
Non-traditional products	1.2	0.3	-1.8	-0.5	-1.9	2.1	1.2	3.1	2.1
Imports	1.5	1.7	-2.2	-1.8	-2.8	-0.3	-2.4	0.8	0.4

IR: Inflation Report.
* Forecast.

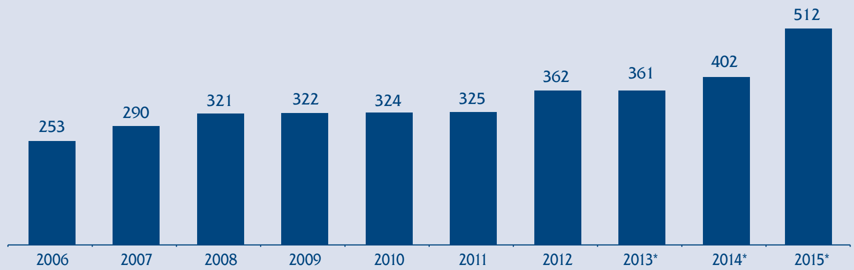
Graph 50
EXPORTS OF GOODS: 2006-2015
(Billion US$)



Memo: Total exports also includes other exports.
* Forecast.

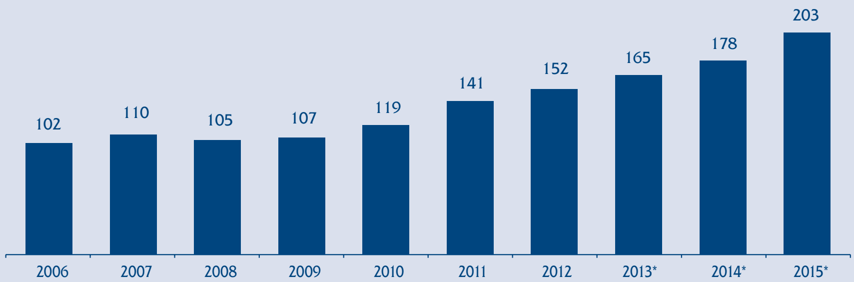
The projected value of exports in 2014 and 2015 is positively influenced by the onset of operation of important mining projects and by the reversal of some technical problems experienced during 2013. Thus, the volume of traditional exports would grow 9.4 percent in 2014 and 14.5 percent in 2015. Despite this, the value of the country's exports would be affected by export prices. Thus, the value of exports is estimated at US$ 43.1 billion in 2014 and at US$ 48.4 billion in 2015, which represents a nominal growth of 12.3 percent between 2014 and 2015. This growth would result mostly from the operation of new copper mining projects, such as Toromocho (Junin), Las Bambas (Apurímac), and Constancia (Cusco).

Graph 51
VOLUME OF COPPER EXPORTS: 2006-2015
(Index 1994=100)



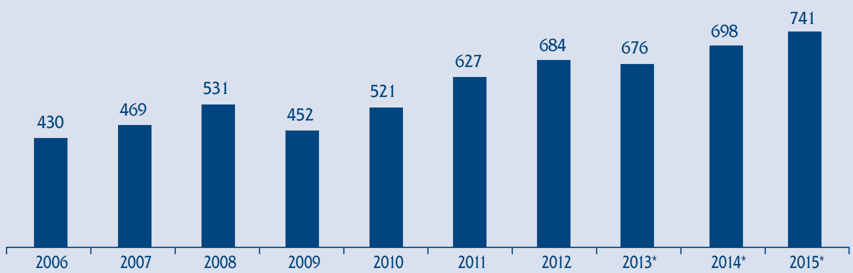
* Forecast.

Graph 52
VOLUME OF IRON EXPORTS: 2006-2015
(Index 1994=100)



* Forecast.

Graph 53
NON-TRADITIONAL EXPORTS VOLUME
(Index 1994=100)

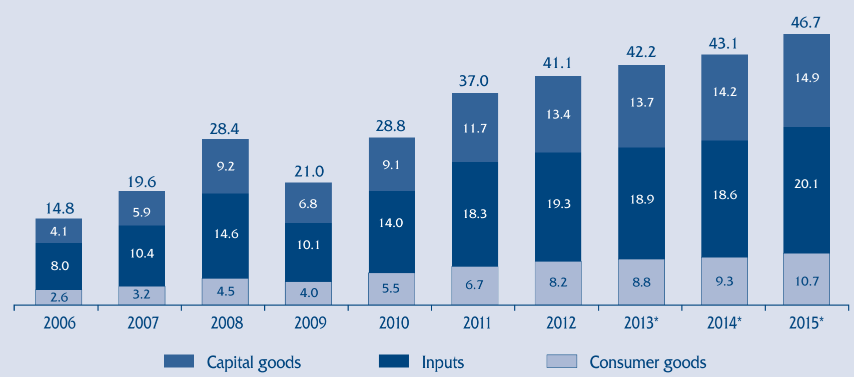


* Forecast.

47. On the other hand, the forecast of **imports** in 2013 has been revised down to around US$ 42 billion, which represents an increase of 2.6 percent compared with 2012. The lower value of imports considered for this year compared to our previous report results from a lower growth of domestic demand and lower import prices.

Imports in 2014 would amount to US$ 43 billion, while imports in 2015 would reach US$ 47 billion. The volumes of imports in the forecast horizon would continue showing a conduct consistent with the evolution of economic activity, a real growth rate of 4.6 percent and 8.1 percent being projected for 2014 and 2015, respectively.

Graph 54
IMPORTS OF GOODS: 2006-2015
(Billion US$)



Memo: Total imports also includes other imports.
* Forecast.

Financial account

48. In the period of January-September, the **long-term financial account of the private sector** amounted to US$ 15.4 billion, which represents a flow equivalent to 9.9 percent of GDP. This amount was higher than the one registered in the same period of the previous year due mainly to the financing operations associated with the issuance of bonds and greater flows of foreign direct investment. In addition to this, a lower acquisition of foreign assets was observed in the case of resident agents.

Table 26
LONG-TERM FINANCIAL ACCOUNT OF THE PRIVATE SECTOR
(Million US$)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
1. ASSETS	**-1,185**	**-2,477**	**-105**	**-3,067**	**-1,454**	**-4,352**	**-2,842**	**-3,577**	**-2,962**
2. LIABILITIES	**14,418**	**18,712**	**15,458**	**18,451**	**18,225**	**15,096**	**13,252**	**14,493**	**13,835**
Foreign direct investment in the country	7,985	12,240	9,004	12,003	11,174	9,392	9,954	9,332	9,438
Non-financial sector	3,574	3,598	4,705	4,561	5,045	4,704	3,298	3,962	3,197
Long-term loans	1,918	2,023	545	518	737	2,022	1,838	1,601	1,566
Portfolio investment	1,656	1,575	4,160	4,043	4,308	2,682	1,460	2,361	1,632
Financial sector	2,859	2,875	1,524	1,886	1,781	1,000	0	1,200	1,200
Long-term loans	2,477	2,093	-11	208	196	424	-549	1,000	1,000
Portfolio investment	383	783	1,535	1,678	1,585	576	549	200	200
3., NET FLOW	**13,233**	**16,236**	**15,353**	**15,383**	**16,772**	**10,744**	**10,410**	**10,916**	**10,873**
% GDP	9.0	8.1	9.9	7.4	8.1	4.8	4.7	4.5	4.5

IR: Inflation Report.
* Forecast.

In **2013** the long term financial account of the private sector would amount to US$ 16.8 billion, a higher flow than the one estimated in our report of September. This revision on the upside considers a higher external financing of the non-financial sector through loans and, to a lesser extent, through the issuance of bonds abroad in the second half of the year amid a context still marked by uncertainty in international financial markets. Another factor contributing to this would be the lower financial requirements of the financial sector due to the lower demand for credit in foreign currency.

Positive flows of US$ 10.4 billion and US$ 10.9 billion, equivalent to 4.7 and 4.5 percent of GDP, are projected for **2014** and **2015**, respectively. This revision is consistent with a lower external financing from the non-financial sector mainly, in a context of lower monetary stimulus from the Fed.

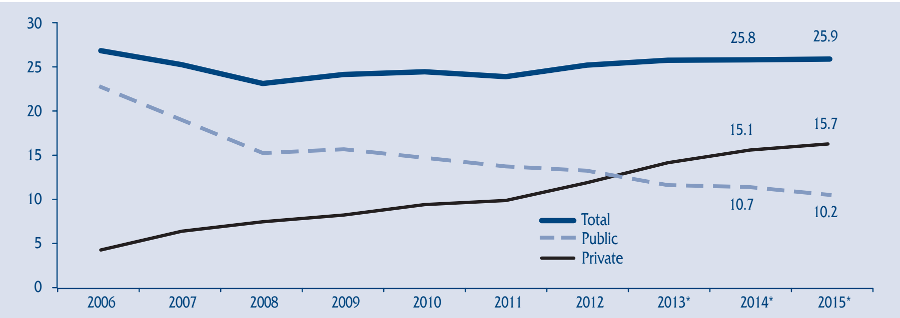
Graph 55
LONG-TERM EXTERNAL FINANCING OF THE PRIVATE SECTOR: 2006-2015 1/
(% GDP)

1/ Includes net foreign investments, portfolio investment and private sector's long-term disbursement.
* Forecast.

49. The **financial account of the public sector** showed a negative flow of US$ 616 million between January and September. This balance is explained mostly by the amortization of the public debt (US$ 2.42 billion), which included the prepayment made to international organizations (US$ 1.68 billion). These operations were in part offset by the disbursement of US$ 1.14 billion to finance several investment projects and by transactions in the secondary market of bonds which resulted in a positive net flow of US$ 648 million.

50. The balance of the medium- and long-term external debt would go from 25.2 percent of GDP in 2012 to 25.8 percent in 2013. The rising trend observed in the external indebtedness of the private sector would continue in the forecast horizon and would determine that, for the first time, the private debt is higher than the public debt. The external public debt, including local bonds held by non-residents, would decline from 13.2 percent of GDP in 2012 to 10.7 and 10.2 percent of GDP in 2014 and 2015, respectively.

Graph 56
MEDIUM- AND LONG-TERM EXTERNAL DEBT: 2006-2015
(% GDP)



* Forecast.

51. Between January and September 2013, the **flow of short-term foreign capital** was negative by US$ 2.13 billion, which contrasted with the positive capital inflow of US$ 1.05 billion observed in the same period in 2012. A higher negative flow (US$ 2.75 billion) than the one forecast in our previous report is estimated for this year. This trend would be reflecting the replacement of external financial sources by the domestic sources offered by local financial entities, which in turn results in a less tight foreign currency liquidity position.

52. To prevent excessive volatility in the foreign exchange market and continue reducing the economy's vulnerability to abrupt reductions of external financing, the Central Bank intervened in the foreign exchange market selling foreign currency for a total of US$ 3.31 billion in Q3. As a result, international reserves at the end of November amounted to US$ 66.28 billion. This level of reserves represents

32.0 percent of GDP, covers approximately 9 times the amount of the short-term external debt, and backs up 94.9 percent of the financial system's total obligations with the private sector (total liquidity).

Table 27
NIR INDICATORS

	November		
	2003	2008	2013
Net International Reserves (NIR, million US$)	10,303	30,970	66,279
BCRP International Position (Million US$)	4,367	21,017	42,151
NIR / GDP (%) 1/	17.1	24.4	32.0
NIR / Short-term external debt (# of times) 2/	2.2	3.3	9.0
NIR / Total liquidity (%)	82.6	92.7	94.9

1/ Accumulated at the previous quarter.
2/ Includes short-term debt balance and amortizations in the next four quarters.

Graph 57
NET INTERNATIONAL RESERVES: 2006 - NOV.2013
(Million US$)

IV. Public Finances

53. The fiscal policy in 2013 was countercyclical since actions were taken to speed up the pace of growth of public spending in a context of economic slowdown. The non-financial public sector is therefore expected to register a lower surplus (0.6 percent) than the one recorded in 2012 (2.1 percent), but higher than the surplus projected in our previous report (0.4 percent).

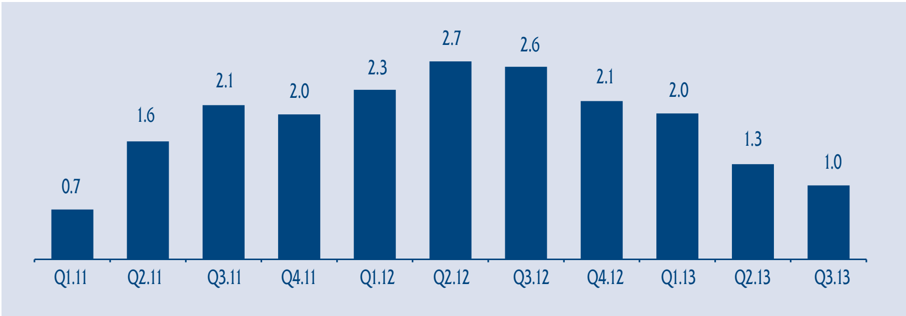
54. The economic balance at September shows a lower surplus than the one recorded in the same period of last year (3.3 percent of GDP versus 5.0 percent of GDP), which reflects a higher non-financial expenditure (1.4 percentage points), particularly an increase in current expenditures (0.8 percentage points). On the other hand, the revenues of the general government were slightly lower (down 0.1 percentage points) in a context of lower terms of trade and a slowdown in the pace of growth of economic activity. At September, the surplus of the last four quarters amounted to 1.0 percent of GDP.

Table 28
NON-FINANCIAL PUBLIC SECTOR
(% GDP)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
1. General government current revenues 1/	**21.9**	**21.6**	**21.8**	**21.3**	**21.7**	**21.3**	**21.6**	**21.4**	**21.7**
Real % change	*6.6*	*7.2*	*2.8*	*2.4*	*3.7*	*6.6*	*5.5*	*7.5*	*7.4*
2. General government non-financial expenditure 2/	**16.1**	**18.6**	**17.5**	**20.0**	**20.2**	**20.2**	**20.5**	**20.4**	**20.7**
Real % change	*4.6*	*8.1*	*12.3*	*11.5*	*11.7*	*7.6*	*8.0*	*8.1*	*8.0*
Of which:									
Current	11.9	13.1	12.7	13.9	13.9	13.6	13.9	13.4	13.6
Real % change	*0.5*	*5.4*	*9.9*	*10.1*	*9.7*	*4.3*	*5.5*	*5.1*	*4.9*
Gross capital formation	3.9	5.2	4.5	5.7	5.8	6.0	6.0	6.4	6.5
Real % change	*19.9*	*15.9*	*17.4*	*13.5*	*15.0*	*12.2*	*10.7*	*15.4*	*15.5*
3. Others	**0.3**	**0.3**	**0.3**	**0.1**	**0.2**	**-0.1**	**-0.1**	**-0.1**	**-0.1**
4. Primary balance (1-2+3)	**6.1**	**3.2**	**4.5**	**1.4**	**1.7**	**1.0**	**1.0**	**0.9**	**0.9**
5. Interests	**1.2**	**1.1**	**1.2**	**1.0**	**1.1**	**0.9**	**0.9**	**0.9**	**0.9**
6. Overall Balance	**5.0**	**2.1**	**3.3**	**0.4**	**0.6**	**0.1**	**0.1**	**0.0**	**0.0**
Memo: (billion S/.):									
1. General government current revenues	85	114	90	119	121	131	131	143	144
2. General government non-financial expenditure	63	98	72	112	113	124	125	136	137
3. Nominal GDP	390	526	413	562	559	613	608	669	661

1/ The central government includes the ministries, national universities, public agencies and regional governments. The general government has a wider coverage that includes the central government, social security, regulators and supervisors, government charity organizations and local governments.
2/ Includes accrued payments by Net payments of the Fuel Price Stabilization Fund.
IR: Inflation Report.
* Forecast.

Graph 58
ECONOMIC BALANCE OF THE NON-FINANCIAL PUBLIC SECTOR: Q1.11 - Q3.13
(Accumulate last 4 quarters - % GDP)



The economic balance of 0.4 percent of GDP estimated for **2013** in our Inflation Report of September has been revised up to 0.6 percent of GDP due basically to the higher growth of revenue in real terms. It should be pointed out that the Financial Equilibrium Law of **2013** (Law 29952, dated December 4, 2012) suspended for this year the applicability of the macro fiscal rules of the Fiscal Transparency and Responsibility Act, which established that the fiscal deficit should be lower than 1 percent of GDP and that the maximum increase in real expenditure in consumption was 4 percent. This regulation established that the economic balance of the operations of the non-financial public sector (NFPS) should show no deficit.

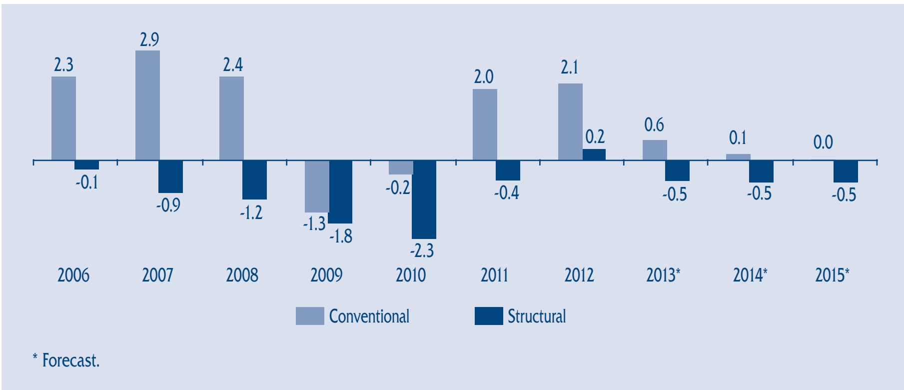
A positive balance of 0.1 percent and a zero balance are expected for **2014** and **2015**, respectively. These balances are similar to those considered in our previous report, since the higher revenues projected in GDP terms are offset by the higher expenditure allocated for those years. In addition, it is worth pointing out that Law 30099 was published on October 31 to strengthen the Fiscal Transparency and Responsibility Act. This law establishes that the new administration will prepare guidelines for the **structural fiscal balance** of the non-financial public sector, which cannot be a deficit higher than 1.0 percent of GDP. The financial expenditure of the national government will grow in accordance with the provisions of these guidelines. In the meantime while this rule is implemented, the balance of the non-financial public sector for FY **2014** cannot show a deficit. In 2015 and in the part of 2016 under the current administration, the rule establishes that the structural fiscal balance will be a deficit of 1 percent of GDP.

Graph 59
ECONOMIC BALANCE OF THE NON-FINANCIAL PUBLIC SECTOR: 2006-2015
(% GDP)

Structural economic balance and fiscal impulse

55. The **structural economic balance** is an indicator that shows the effect of fiscal policy decisions isolating from the conventional economic balance the effects of the business cycle and the effects of the prices of the commodities that are relevant to our economy. Thus, for example, an increase in effective revenues is not part of the structural revenues it is obtained as a result of a temporary rise in the prices of minerals. In 2013 the structural economic balance would show a deficit of 0.5 percent of GDP and similar balances are projected for 2014 and 2015.

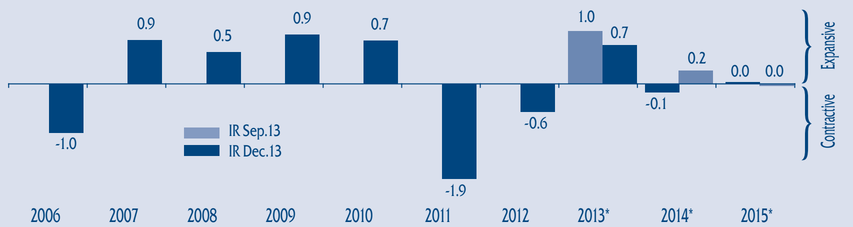
Graph 60
CONVENTIONAL AND STRUCTURAL BALANCE OF THE NON-FINANCIAL PUBLIC SECTOR: 2006-2015
(% GDP)



56. The **fiscal impulse**, the indicator that allows us to identify changes in the fiscal position isolating the effects of the business cycle, would be 0.7 percent in 2013, which indicates a fiscal expansionary position that is consistent with greater government investment and with the salary increases registered over the year.

In 2014 the fiscal impulse would be 0.2 percent of GDP and would converge thereafter to zero in 2015

Graph 61
FISCAL IMPULSE 1/: 2006-2015
(% GDP)



1/ The fiscal impulse is the change in the primary structural balance, which is an indicator of how the fiscal position affects the economic cycle.
* Forecast.

Tax revenues

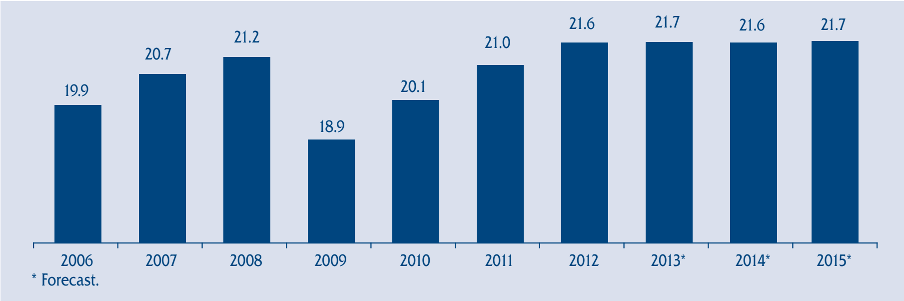
57. In 2013 the **current revenues of the general government** would be equivalent to 21.7 percent of GDP, a rate slightly higher than the one recorded in 2012 (21.6 percent), and with a tax component of 16.4 percent of GDP and a non-tax component of 5.3 percent. It should be pointed out that this outcome occurs in a year in which the lower prices of exports explain the decrease of revenues from the income tax from 7.1 percent of GDP in 2012 to 6.5 percent in 2013. This decline has been offset by measures, such as the expansion of the system of tax withholding to sales of gold exempted from the VAT and to public entertainment, both of which showed high figures of tax evasion.

Table 29
CURRENT REVENUES OF THE GENERAL GOVERNMENT
(% GDP)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
TAX REVENUES	**16.5**	**16.4**	**16.4**	**16.1**	**16.4**	**16.3**	**16.4**	**16.3**	**16.5**
Income tax	7.4	7.1	6.8	6.5	6.5	6.5	6.6	6.5	6.6
Value added tax	8.4	8.4	8.6	8.5	8.5	8.6	8.5	8.6	8.6
Excise tax	0.9	0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Import duties	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Other tax revenues	1.6	1.7	1.9	1.8	2.0	1.8	2.0	1.8	1.9
Tax returns	-2.1	-2.0	-2.1	-2.0	-2.0	-2.0	-1.9	-1.9	-1.9
NON-TAX REVENUES	**5.3**	**5.2**	**5.4**	**5.1**	**5.3**	**5.0**	**5.2**	**5.1**	**5.2**
TOTAL	**21.9**	**21.6**	**21.8**	**21.3**	**21.7**	**21.3**	**21.6**	**21.4**	**21.7**

IR: Inflation Report.
* Forecast.

Graph 62
CURRENT REVENUES OF THE GENERAL GOVERNMENT: 2006-2015
(% GDP)



58. Revenues from the **income tax** at September 2013 amounted to 6.8 percent of GDP, 0.6 percentage points lower than the level recorded in the same period of 2012. This decrease is explained basically by lower advanced payments of third category income tax, especially from the mining sector, which fell 48 percent in this period, in part offset by higher revenues from income taxes from other sectors, such as trade and services. In the forecast horizon, the income tax revenue would remain around 6.6 percent of GDP. In this scenario correspond to higher revenues other than mining, as well as by higher labor income, which would come from an increase in formal employment.

Table 30
THIRD CATEGORY INCOME TAX BY SECTORS
(Million S/.)

	January - September		
	2012	2013	Real % chg.
Other services	5,088	5,659	8.3
Commerce	2,123	2,584	18.5
Mining	4,121	2,201	-48.0
Manufacture	1,970	1,982	-2.0
Hydrocarbons	1,301	1,417	6.0
Construction	624	767	19.7
Fishing	74	48	-37.2
Agriculture and livestock	25	35	35.2
TOTAL	**15,325**	**14,694**	**-6.7**

Source: SUNAT.

59. On the other hand, revenues from the **value-added tax** (VAT) at September 2013 increased 5.3 percent in real terms as a result of a 7.7 percent increase in revenues from the domestic VAT and a 2.3 percent increase in revenues from the external VAT. In terms of sectors, the domestic VAT continues to grow, driven by the sectors of services, trade, manufacturing, and construction, but this growth is

offset by the decline of VAT revenues from primary sectors, such as mining and hydrocarbons.

Table 31
DOMESTIC VALUE ADDED TAX BY SECTORS
(Million S/.)

	January - September		
	2012	**2013**	**Real % chg.**
Other services	7,811	8,982	11.9
Commerce	3,725	4,047	5.7
Manufacture	2,757	2,980	5.2
Construction	1,337	1,683	22.5
Hydrocarbons	1,105	1,113	-2.0
Mining	1,014	873	-16.4
Agriculture and livestock	236	254	4.6
Fishing	108	98	-12.0
TOTAL	**18,094**	**20,030**	**7.7**

Source: SUNAT.

Revenues from the VAT are expected to increase to 8.5 points of GDP at end **2013**. In **2014** these revenues would register a similar ratio to the one recorded in 2013, while in **2015** they are expected to increase slightly to 8.6 percent of GDP, as estimated in our previous report, thus showing a slight rising trend in the most significant tax of our tax system.

Government expenditure

60. The non-financial expenditure of the general government at **September 2013** was equivalent to 17.5 percent of GDP, which represented an increase of 1.4 percentage points compared to the level of the non-financial expenditure of the general government in the same period of 2012. This result reflects the faster pace of spending in the three levels of government spending, which included both current expenditure and capital expenditure. Current expenditure increased in the period due to the various salary increases approved for public servants in sectors such as interior, defense, education, and health, as well as due to increased spending for services provided to the government social and administrative sectors through service contracts (CAS).

61. In **2013** the non-financial expenditure of the general government is estimated to grow by a real 11.7 percent, slightly higher than estimated in our September report (11.5 percent). This increase of expenditure in 2013 is associated with the salary increases mentioned above and with the dynamism of budget capital spending,

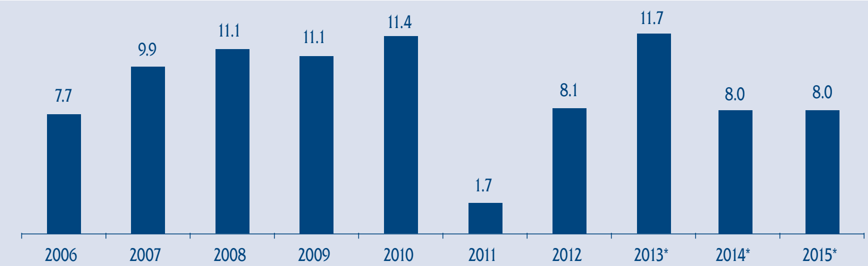
which has been significantly higher than in previous years. Thus, in 2013 the non-financial expenditure of the general government would register a level equivalent to 20.2 percent of GDP, 0.2 percentage points higher than the rate estimated in our Inflation Report of September. In the forecast horizon, this aggregate as a percentage of GDP is expected to follow a rising path and to reach a level of 20.7 percent of GDP in 2015 as a result of the increase in capital spending, whose share in GDP terms would increase from 6.2 percent of GDP in 2013 to 7.1 percent in 2015.

Table 32
NON-FINANCIAL EXPENDITURE OF THE GENERAL GOVERNMENT
(% GDP)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
CURRENT EXPENDITURE	**11.9**	**13.1**	**12.7**	**13.9**	**13.9**	**13.6**	**13.9**	**13.4**	**13.6**
National government	7.8	8.7	8.3	9.3	9.4	9.1	9.1	8.9	9.0
Regional governments	2.4	2.6	2.6	2.7	2.7	2.7	3.0	2.7	2.9
Local governments	1.7	1.8	1.7	1.9	1.8	1.8	1.8	1.7	1.7
CAPITAL EXPENDITURE	**4.2**	**5.5**	**4.9**	**6.1**	**6.2**	**6.6**	**6.6**	**7.0**	**7.1**
National government	1.4	1.9	1.7	2.2	2.3	2.5	2.5	2.6	2.7
Regional governments	0.9	1.3	1.1	1.4	1.5	1.5	1.5	1.6	1.6
Local governments	1.8	2.4	2.1	2.5	2.5	2.6	2.6	2.8	2.8
TOTAL EXPENDITURE	**16.1**	**18.6**	**17.5**	**20.0**	**20.2**	**20.2**	**20.5**	**20.4**	**20.7**
National government	9.2	10.6	10.0	11.5	11.6	11.5	11.7	11.5	11.7
Regional governments	3.3	3.9	3.7	4.2	4.2	4.2	4.5	4.3	4.5
Local governments	3.6	4.2	3.8	4.4	4.3	4.4	4.4	4.5	4.6

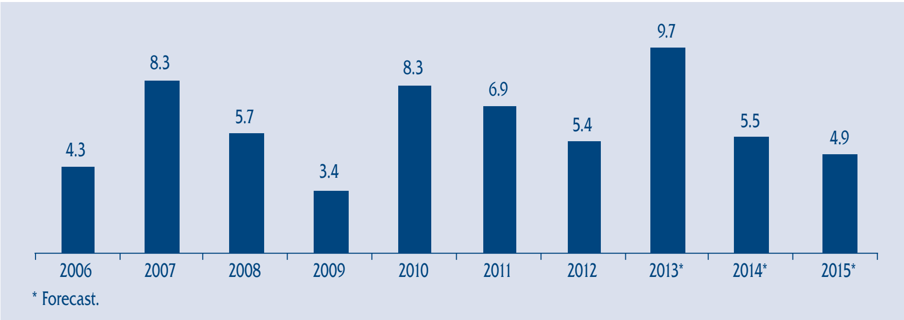
IR: Inflation Report.
* Forecast.

Graph 63
NON-FINANCIAL EXPENDITURE OF THE GENERAL GOVERNMENT: 2006-2015
(Real % change)



* Forecast.

Graph 64
NON-FINANCIAL CURRENT EXPENDITURE OF THE GENERAL GOVERNMENT: 2006-2015
(Real % change)



Graph 65
GROSS CAPITAL FORMATION OF THE GENERAL GOVERNMENT: 2006-2015
(Real % change)

62. It is worth pointing out that the Public Sector Budget Act for 2014, published by Law 30114, established an opening budget (PIA) of S/. 118.93 billion, which represents a nominal increase of 9.7 percent in total expenditure compared with the PIA for 2012. Moreover, 70 percent of the budget is allocated to the national government and 30 percent to sub-national governments (16 percent to regional governments and 14 percent to local governments). By type of expenditure, 63 percent is allocated to current expenditure, 28 percent to capital spending, and 9 percent to the debt service.

Financial requirements and the debt of the non-financial public sector

63. The accumulation of deposits would be higher than previously estimated in our Inflation Report of September due to the higher surplus projected for 2013. It should be pointed out that this requirement excludes the debt management operations carried out in 2013, which include the prepayment of part of the external debt (US$ 1.68 billion) and the issuance of sovereign bonds for a total of S/. 3.09 billion.

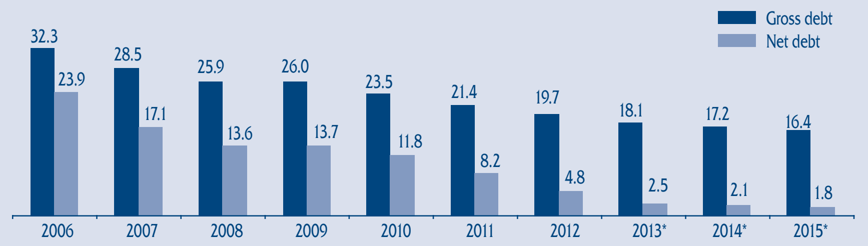
Table 33
FINANCIAL REQUIREMENTS OF THE NON-FINANCIAL PUBLIC SECTOR AND ITS FUNDING 1/
(Million S/.)

	2012		2013*			2014*		2015*	
	Jan.-Sep.	Year	Jan.-Sep.	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13	IR Sep.13	IR Dec.13
I. USES	**-16,091**	**-6,968**	**-10,879**	**1,180**	**323**	**2,884**	**3,275**	**6,215**	**6,301**
1. Amortization	3,319	4,342	2,740	3,221	3,626	3,782	3,875	6,289	6,390
a. External debt	2,351	3,105	1,316	1,707	1,963	2,724	2,724	2,433	2,433
b. Domestic debt	968	1,237	1,424	1,513	1,662	1,058	1,151	3,856	3,958
Of which:									
Recognition bonds	345	509	324	206	444	376	468	386	488
2. Overall balance	-19,410	-11,310	-13,618	-2,041	-3,303	-898	-600	-74	-89
(negative sign indicates surplus)									
II. SOURCES	**-16,091**	**-6,968**	**-10,879**	**1,180**	**323**	**2,884**	**3,275**	**6,215**	**6,301**
1. External	653	1,175	572	2,033	1,866	3,062	3,062	4,909	4,909
2. Bonds 2/	4,077	4,378	924	2,048	1,460	2,925	1,925	2,477	2,377
3. Domestic 3/	-20,820	-12,521	-12,375	-2,901	-3,003	-3,103	-1,712	-1,171	-984
Memo:									
NFPS gross debt									
Billions S/.	98.7	103.8	99.4	101.7	101.1	106.4	104.8	110.3	108.6
% GDP	19.1	19.7	18.1	18.1	18.1	17.4	17.2	16.5	16.4
NFPS net debt 4/									
Billions S/.	18.0	25.4	11.9	13.3	14.2	14.2	12.9	14.4	11.8
% GDP	3.5	4.8	2.2	2.4	2.5	2.3	2.1	2.2	1.8

1/ The effect of exchanging treasury bonds for longer-maturity bonds, as well as the effect of placements made for the prepayment of both internal and external operations has been isolated in the case of amortization and disbursements.
2/ Includes domestic and external bonds.
3/ A positive sign indicates a withdrawal or overdraft and a negative sign indicates higher deposit
4/ Defined as the difference between gross public debt and NFPS deposits.
IR: Inflation Report.
* Forecast.

The gross debt and the net debt of the non-financial public sector at September 2013 amounted to 18.1 percent and 2.5 percent of GDP, respectively. The positive balances expected in public finances would determine that the gross debt and the net debt continue to decline and thus represent 16.4 percent and 1.8 percent of GDP in 2015.

Graph 66
NON-FINANCIAL DEBT OF THE PUBLIC SECTOR: 2006-2015
(% GDP)



* Forecast.

Box 3

MODIFICATION OF THE MACRO FISCAL FRAMEWORK

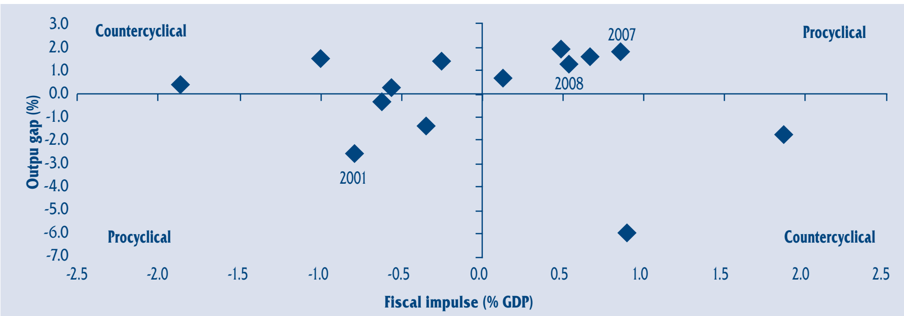
The structural economic balance is the economic balance that the public sector would obtain should there not be any cyclical fluctuations in the economy (or in any other determinant of tax revenues, such as the prices of export commodities). It is thus a non-observable variable, which will be estimated by a method of estimation approved by the Ministry of Economy and Finance (MEF).

Law 30099[3] has modified the macro-fiscal rules by which public finances are implemented in Peru so as to determine the fiscal position of the country in structural terms. With that purpose, the law modifies the rules of the economic balance and government expenditure, both in terms of design and scope.

The new framework eliminates the macro-fiscal rule associated with a conventional deficit of one percent for the non-financial public sector, which is replaced by ex ante guidelines for the structural balance to be obtained. This new framework establishes that every government must enact a macro-fiscal policy statement during the first 90 days in office which explicitly points out the guidelines for the structural balance of the non-financial public sector which that be applied during the whole presidential period. The new framework also establishes that the deficit structural cannot be higher than one percent of GDP.

This new law introduces the structural economic balance as a guide for fiscal management. It is worth mentioning that countries in the region such as Chile and Colombia use the structural balance to design their fiscal policy. Beyond the region, countries such as Switzerland and Germany also apply rules like this one.

FISCAL IMPULSE AND CHANGE IN THE OUTPUT GAP: 1999-2012



The purpose of using a structural rule is to reduce the pro-cyclical bias of fiscal policy which should reduce macroeconomic volatility and favor a stable environment with higher growth. The structural rule also allows the country to save transient revenues associated with booms in commodity prices. Moreover, more public saving makes it easier to implement discretional counter-cyclical policies during recessions, as happened in 2009-2010.

The fiscal rule establishes that the non-financial expenditures of the national government cannot exceed the limit consistent with the guidelines of the structural balance set by the fiscal policy statement. This limit is set for three years and can be annually reviewed when the budget is formulated

The limit to expenditures may be expressed as:

$$GNFGN_t = Structural\ I_t + PBState\ enterprises_t - Interests_t - Structural\ guide_t - GNFGSN_t$$

3 Published on October 31, 2013.

That is, the limit for the national government expenditures in a given year is equal to the structural income of the general government estimated for that year ($Structural\ I_t$), plus the primary balance of state-owned enterprises ($PBState\ enterprises_t$) anticipated for that period, minus the interest of the public debt and the non-financial expenditures of the sub-national governments estimated for that year ($GNFGSN_t$), and minus the guide for the structural balance included in the fiscal policy statement.

The indicated limit on expenditures can be modified if expenditures the year before were lower than the limit (up to 0.2 percent of GDP), if tax measures that affect permanent income by at least 0.3 percent of the GDP are given, and by reason of counter-cyclical measures: If a (negative or positive) gap of at least 2 percent of GDP is anticipated, measures should be taken encompassing not more than 25 percent of the gap, with a limit of 0.5 percent of the GDP. By the same token, the limit of expenditures will be adjusted when deviations from the fiscal rule[4] are observed or when clauses to escape the rule[5] apply.

The law also establishes a limit to the growth of expenditures of the national government in matters of personnel, which will not exceed the rate of growth of the potential GDP.

In the case of regional and local governments, debt limits are established (the ratio of total debt over the average total current income of the last four years cannot exceed 100 percent and also limits to non-financial expenditures (the percent variation of non-financial expenditures will not be higher than the percent variation of the four-year moving average of the income of the subnational government). Should they not fulfill the rule, the subnational governments will not be able to participate in the FONIPREL, in the Program of Incentives for the Improvement of Municipal Management, and will not have access to short-term credit in the financial system.

The Fiscal Stabilization Fund (FSF) managed by the Ministry of Economy (MEF) is kept, although the interest generated by this fund will be freely disposable by the Treasury, and the strategy for its administration will be subject to the Treasury's framework of global management of assets and debts.

The law creates a Fiscal Council[6] as an autonomous commission of the Ministry of Economy that should provide independent technical analysis of macro-fiscal policy. This analysis will result in explicit non-binding opinion on the modification and fulfillment of fiscal rules, the fiscal projections considered in the MMM, the short and long-term evolution of public finances, and the method used to estimate the structural balance and the potential output.

4 If expenditures by the national government deviate from the limit of the fiscal rule, such deviations are accumulated in an informational account. If the balance of that account is lower than 0.5 percent of the GDP, the limit of expenditures during the next two years will have to be adjusted downwards proportionally provided that a negative output gap higher than 2 percentage points of the GDP is not projected for those years. If the balance is higher than 0.5 percent of the GDP, the adjustment in expenditures begins in the period where this anomaly is detected.

5 In cases of national emergency or international crisis, the Executive can ask Congress to modify the guide for the structural balance and, therefore, change the limits for expenditures at the national, regional, and local levels for a period of up to three years. In this case, the government has to indicate the measures to be taken in order to return to the initial guide for the structural balance. Regional governments that confront natural disasters can ask the MEF to be exempted from the application of the rule for increases in expenditures for up to two years. Finally, when a natural resource begins to be exploited within the jurisdiction of a subnational government and its income increases due to taxation or royalties by an amount exceeding 1,500 units of internal revenue (UIT) per year, the subnational government can be exempted from the fiscal rules for two years.

6 The Fiscal Council consists of at least three members that will be appointed by the MEF for a period of four years that can be renewed only once. The first members of the Fiscal Council will be designated for periods of two, three, and four years so as to secure sequential renovation. The persons designated have to be widely recognized as experts on fiscal matters and be morally flawless.

V. Monetary Policy

64. In November, the Board of the Central Bank decided to lower the monetary policy benchmark interest rate to 4.00 percent after having maintained this rate at 4.25 percent since May 2011. This rate cut is consistent with an inflation rate close to 2.0 percent in the 2014-2015 forecast horizon and it also takes into account that the pace of growth of economic activity in the country is below its potential level, that recent indicators show lower growth in the world economy, that expectations of inflation remain within the target range, and that the supply shocks that affected inflation are expected to reverse in the short run.

    The BCRP also continued lowering the rate of reserve requirements in soles in order to provide greater sources of financing for credit in domestic currency, which continued to grow and reached a rate of 23.1 percent in November. The rate of required reserves in soles was lowered from 16 to 15 percent in December.

65. The policy communiqués of the Board of the Central Bank in recent months have highlighted that the expected rates of inflation are within the target range and that the 12-month inflation rate will return to the target range in the coming months as food supply conditions improve, as well as that uncertainty persists in the international financial scenario.

Graph 67
BCRP REFERENCE INTEREST RATE
(%)

SUMMARY OF BCRP MONETARY POLICY COMMUNIQUÉS

September: The Board of the Central Reserve Bank of Peru approved to maintain the monetary policy reference rate at 4.25 percent.

This decision is based on that economic growth in the country is close to the economy's potential level of growth, inflation expectations remain anchored within the target range, the rate of inflation has been affected by temporary factors on the side of supply, and international financial conditions are still uncertain, even though some positive signals have been observed in the developed economies.

October: The Board of the Central Reserve Bank of Peru approved to maintain the monetary policy reference rate at 4.25 percent.

This decision is based on the following factors: i) economic growth in the country is close to the economy's potential level of growth; ii) inflation expectations remain anchored within the target range; iii) the supply factors that affected inflation are reversing, and iv) international financial conditions are still uncertain, even though recent indicators of global activity show some recovery.

November: The Board of the Central Reserve Bank of Peru approved to lower the monetary policy reference rate to 4.0 percent.

The new level of the reference rate is compatible with an inflation forecast of 2.0 percent in the 2014-2015 forecast horizon and also takes into account that: i) economic growth in the country is slowing down to rates below the economy's potential level of growth; ii) recent indicators show a lower growth in the world economy; iii) inflation expectations have declined and remain anchored within the target range, and iv) the supply factors that affected inflation transitorily are reversing.

This decision is preventive and does not imply a sequence of reductions in the reference interest rate.

December: The Board of the Central Reserve Bank of Peru approved to maintain the monetary policy reference rate at 4.0 percent.

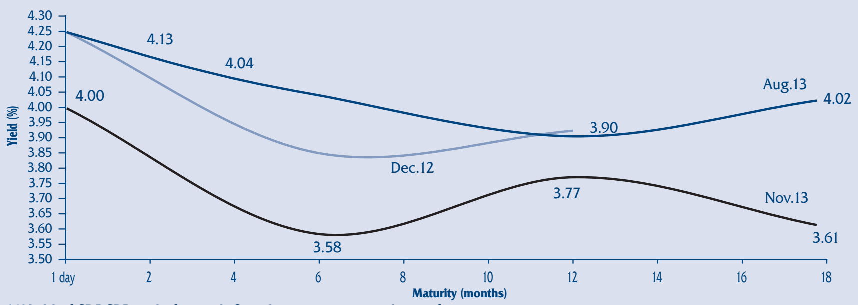
This level of the reference rate is compatible with an inflation forecast of 2 percent in the forecast horizon (2014 – 2015) and takes into account that: i) inflation expectations remain anchored within the inflation target range; ii) GDP has been recording lower growth rates than the country's potential level of growth; iii) recent indicators show some recovery in the world economy, and iv) the supply factors that affected inflation are reversing.

Monetary operations

66. The operations of the Central Bank were aimed mainly at maintaining adequate levels of liquidity and at ensuring the flow of operations in the money market, in a context of lower availability of liquidity in soles in financial entities due to banks' increased purchases of dollars between September and November (US$ 1.45 billion). With this aim, the Central Bank reduced the pace of placements of certificates of deposit and term deposits and made auctions of 1-day and 1-week repos for a daily average of S/. 2.45 billion in September, S/. 1.30 billion in November, and S/. 4.20 billion until December 9.

    The yield curve of 6-month and 18-month CD-BCRP shrank 33 basis points on average in November compared to August due to the reduction of 25 basis points in the BCRP policy rate. Moreover, the yield curve continued showing an inverted curve shape, which would be indicating that further reductions are expected in the policy rate in the future.

Graph 68
YIELD CURVE OF CENTRAL BANK SECURITIES 1/



1/ Yield of CDBCRP end of period. One day rate corresponds to reference rate.

67. As a result of these operations, the share of BCRP instruments decreased in terms of the BCRP total liabilities. The share of BCRP monetary instruments declined from representing 18 percent of the country's international reserves in December 2012 to representing a projected 12 percent in December 2013. On the other hand, the share of required reserves increased from 28 to 32 percent, due mainly to banks' higher deposits in foreign currency, whose share increased from 16 to 22 percent of international reserves. This was offset by the lower share of required reserves in domestic currency, whose share declined from 12 to 10 percent. Public sector deposits continued to be the main source of sterilization interventions, with a share of 36 percent of the total liabilities of the BCRP.

Table 34
SIMPLIFIED BALANCE SHEET OF THE BCRP
(As % of Net International Reserves)

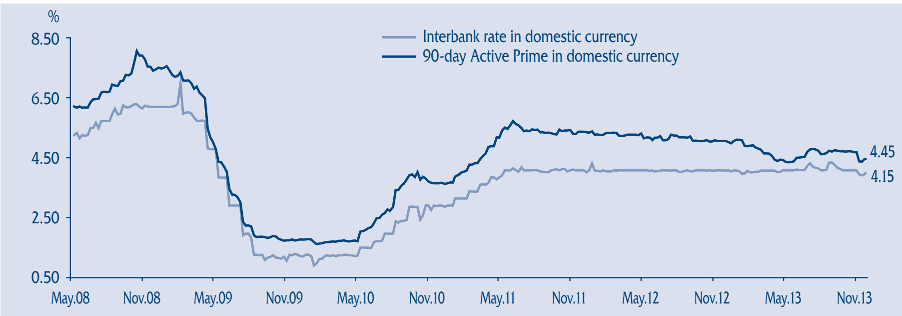
Net assets	Dec.12	Dec.13*
I. Net International Reserves	100% (US$ 63,991 mills.)	100% (US$ 66,161 mills.)
Net liabilities		
II. Total public sector deposits	**36.4%**	**36.3%**
In domestic currency	23.6%	20.1%
In foreign currency	12.8%	16.2%
III. Total reserve requirements	**27.8%**	**32.4%**
In domestic currency	12.1%	10.3%
In foreign currency 1/	15.7%	22.1%
IV. BCRP Instruments	**17.7%**	**11.7%**
CD BCRP	12.3%	10.3%
CDR BCRP	0.0%	1.5%
Term deposits	5.5%	0.0%
V. Currency	**19.0%**	**19.6%**
VI. Others	**-0.9%**	**-0.1%**

1/ Includes banks' overnight deposits at the Central Bank.
* Forecast.

Interest rates on operations in domestic currency

68. The evolution of the interest rates on operations in domestic currency reflects the impact of the policy rate cut carried out in November as well as the reserve requirement measures which provide greater availability of liquidity to financial institutions. Thus, the interbank rate fell 37 basis points relative to August and the 90-day corporate prime interest rate fell by 28 basis points to 4.45 percent.

Graph 69
90-DAY CORPORATE PRIME RATE VERSUS INTERBANK OVERNIGHT RATE IN DOMESTIC CURRENCY: MAY.08 - NOV.13



69. Relative to August, the lending rates in domestic currency also declined, particularly in the segment of corporate loans where they fell from 5.7 to 5.4 percent (32 basis points), as well as in loans to medium-sized companies (49 basis points) and loans to small companies (55 basis points), following the lower reference rate.

Table 35
INTEREST RATE BY TYPE OF LOANS 1/
(%)

	Domestic currency					
	Corporate	Large companies	Medium-sized enterprises	Small businesses	Consumer	Mortgage
Dec.10	4.6	5.9	10.3	23.3	40.7	9.3
Dec.11	6.0	7.4	11.2	23.2	38.5	9.4
Mar.12	6.1	7.0	11.2	23.4	35.6	9.4
Jun.12	6.0	7.3	11.2	23.1	34.9	9.3
Sep.12	5.7	7.5	11.1	22.9	38.0	8.9
Dec.12	5.8	7.4	11.0	22.5	41.2	8.8
Mar.13	5.8	7.4	10.8	22.0	39.3	9.2
Jun.13	5.3	7.2	10.6	21.2	41.3	9.1
Jul.13	5.4	7.1	10.5	21.0	42.0	9.2
Aug.13	5.7	7.0	10.8	21.4	41.8	9.3
Sep.13	5.5	7.1	10.9	21.5	41.7	9.3
Oct.13	5.8	7.1	11.0	21.2	41.3	9.2
Nov.13	5.4	7.2	10.3	20.9	41.8	9.2
Accumulated change (bps)						
Nov.13-Aug.13	-32	16	-49	-55	-6	-18
Nov.13-Jun.13	7	-2	-26	-34	43	5
Nov.13-Dec.12	-41	-17	-62	-159	61	40

1/ Annual active interest rates on the operations carried out in the last 30 working days.
Source: SBS.

70. On the other hand, the deposit rates in domestic currency remained at relatively similar levels to the ones recorded in August, showing a slight reduction in the rate on 30-day deposits (6 basis points) and an increase of 10 basis points in the rates on 31-day to 180-day deposits.

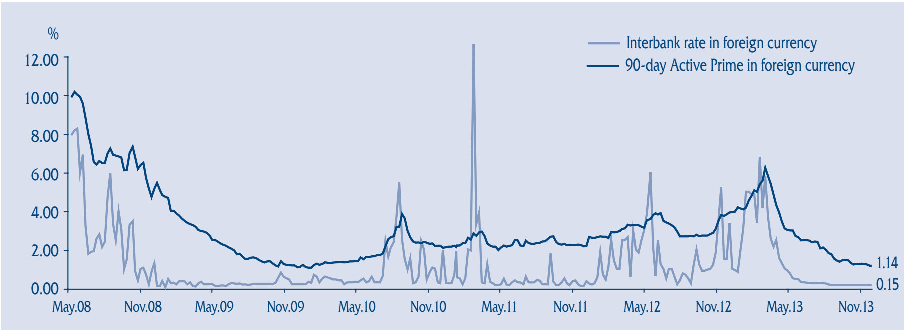
Table 36
INTEREST RATES IN NUEVOS SOLES
(%)

	Deposits up to 30 days	Rate on 31 to 180-day term deposits	Rate on 181 to 360-day term deposits
Dec.10	2.2	2.9	3.8
Dec.11	3.9	4.1	4.7
Mar.12	3.7	3.9	4.5
Jun.12	3.7	3.9	4.3
Sep.12	3.6	3.8	4.2
Dec.12	3.6	3.8	4.2
Mar.13	3.1	3.6	4.1
Jun.13	3.3	3.4	3.9
Jul.13	3.6	3.4	3.9
Aug.13	3.6	3.4	3.8
Sep.13	3.7	3.5	3.8
Oct.13	3.7	3.5	3.9
Nov.13	3.5	3.5	3.9
Accumulated change (bps)			
Nov.13-Aug.13	-6	10	1
Nov.13-Jun.13	21	12	-4
Nov.13-Dec.12	-7	-26	-33

Interest rates on operations in foreign currency

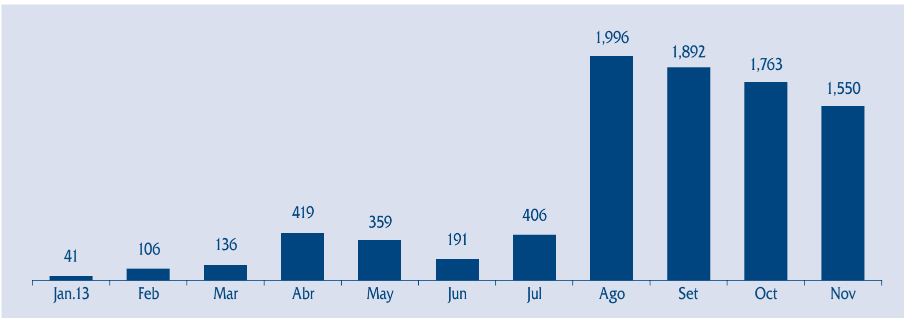
71. Reflecting a lower demand for credit in dollars and a greater preference for saving in dollars, particularly in the case of institutional investors, a high availability of liquidity in foreign currency continued to be seen in this period. This greater availability of liquidity in foreign currency reflected in a declining trend in both the lending and deposit rates in dollars. Thus, the 90-day corporate prime interest rate declined 37 basis points since August to a level of 1.14 percent while the interbank interest rate in foreign currency remained at 0.15 percent in Q3.

Graph 70
90-DAY CORPORATE PRIME RATE VERSUS INTERBANK OVERNIGHT RATE IN FOREIGN CURRENCY: MAY.08 - NOV.13



This greater availability of liquidity in dollars that banks have has allowed them to reduce their short-term liabilities by US$ 1.33 billion between June (US$ 3.04 billion) and November (US$ 1.71 billion) and to accumulate average overnight deposits at the Central Bank for a total of US$ 1.55 billion in November.

Graph 71
OVERNIGHT DEPOSITS IN US$ AT THE CENTRAL BANK
(Period average)



72. The lending interest rates for operations in foreign currency also fell relative to August, especially in the case of the rates for the segments of corporate loans (27 basis points), large companies (72 basis points) and small firms (18 basis points). In contrast, the rates for mortgages and consumer loans increased, reflecting the

reserve requirement measures that would apply depending on the growth of credit in these sectors and the macroprudential measures adopted by the SBS recently.

Table 37
INTEREST RATE BY TYPE OF LOANS 1/
(%)

	Foreign currency					
	Corporate	Large companies	Medium-sized enterprises	Small businesses	Consumer	Mortgage
Dec.10	3.3	5.5	8.6	14.2	19.4	8.1
Dec.11	3.0	5.4	8.9	15.0	22.0	8.2
Mar.12	3.8	5.7	8.9	16.4	23.0	8.2
Jun.12	4.0	6.1	8.7	15.2	22.9	8.0
Sep.12	3.8	5.8	9.2	15.6	23.6	8.0
Dec.12	4.1	6.4	9.0	15.5	22.4	8.0
Mar.13	4.6	7.5	10.1	14.8	24.1	8.2
Jun.13	2.9	6.2	9.2	14.0	25.1	8.6
Jul.13	3.2	6.2	8.9	13.8	25.3	8.5
Aug.13	3.2	6.1	8.6	13.6	25.7	8.4
Sep.13	3.0	6.0	8.8	13.7	25.5	8.8
Oct.13	3.3	5.9	8.8	13.6	25.8	8.6
Nov.13	2.9	5.3	8.7	13.4	26.2	8.5
	Accumulated change (bps)					
Nov.13-Aug.13	-27	-72	5	-18	47	17
Nov.13-Jun.13	3	-86	-57	-53	105	-1
Nov.13-Dec.12	-115	-103	-35	-206	377	57

1/ Annual active interest rates on the operations carried out in the last 30 working days.
Source: SBS.

As regards the deposit rates in foreign currency, a reduction of between 11 and 34 basis points is observed in all the deposit terms relative to August.

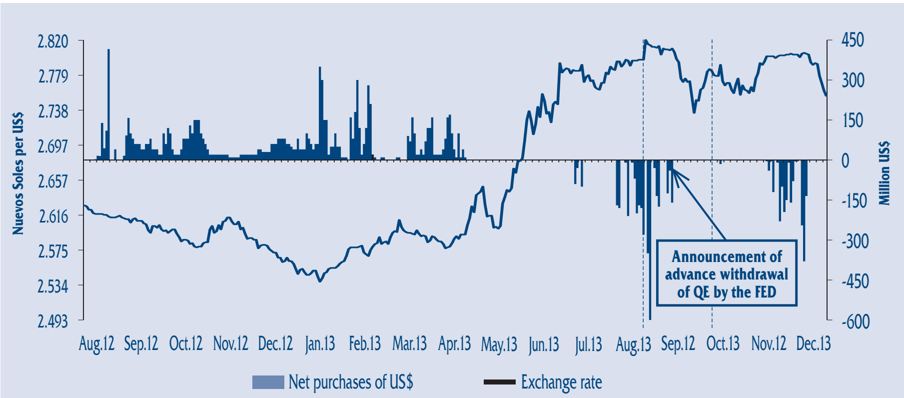
Table 38
INTEREST RATES IN US DOLLARS
(%)

	Deposits up to 30 days	Rate on 31 to 180-day term deposits	Rate on 181 to 360-day term deposits
Dec.10	0.9	1.2	1.7
Dec.11	0.7	1.0	1.6
Mar.12	1.3	1.2	1.6
Jun.12	1.7	1.2	1.6
Sep.12	0.8	1.2	1.6
Dec.12	1.8	1.3	1.7
Mar.13	2.6	1.3	1.7
Jun.13	0.4	1.3	1.7
Jul.13	0.4	1.1	1.7
Aug.13	0.3	1.1	1.6
Sep.13	0.2	1.0	1.5
Oct.13	0.2	0.8	1.4
Nov.13	0.2	0.8	1.4
	Accumulated change (bps)		
Nov.13-Aug.13	-11	-34	-28
Nov.13-Jun.13	-18	-53	-32
Nov.13-Dec.12	-156	-53	-30

Foreign exchange rate

73. The nuevo sol/dollar exchange rate has continued to be affected by volatility since September. In contrast with the depreciation of the sol of 0.18 percent recorded in Q3, so far in Q4 (until December 17) the nuevo sol has appreciated 1.11 percent. Thus, so far in 2013 the local currency has depreciated 7.95 percent. This is consistent with the weakening of other emerging economies' currencies against the dollar observed since April 2013, which is associated with an earlier-than-expected withdrawal of quantitative easing measures by the U.S. Federal Reserve (tapering).

Graph 72
INTERVENTION IN THE FOREIGN EXCHANGE MARKET AND EXCHANGE RATE

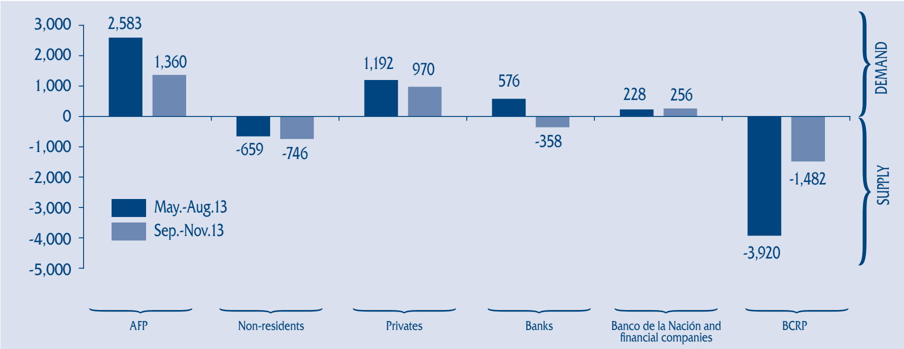


*QE: Quantitative easing.

Between September and October, depreciation pressures on the currencies of the emerging economies decreased after the Federal Reserve decided to maintain its asset purchase programme. In this context, non-resident agents offered dollars mainly in the forward market and the demand for dollars from the non-financial private sector decreased. In addition to this, the Central Reserve Bank slowed down its pace of intervention in the foreign exchange market.

74. However, the demand for dollars intensified since November after the publication of the minutes of the U.S. Federal Reserve, because the Fed did not rule out the possibility of beginning the withdrawal of its asset purchase programs in 2013, and after the publication of recent positive indicators in the U.S. job and real estate markets. This led non-resident agents and pension funds (AFPs) to increase their demand for dollars, especially in the forward market. In this context, in November the Central Bank sold dollars for a total of US$ 1.11 billion and made net placements of CDRBCRP for a total of S/. 2.17 billion (US$ 776 million).

Graph 73
FOREX MARKET FLOWS - SPOT AND FORWARD
(Million US$)



75. The BCRP survey on macroeconomic expectations shows that all the economic agents have lowered the level of foreign exchange rate they expect due to uncertainty about when the Federal Reserve will start to withdraw its asset purchase program in the United States.

Table 39
SURVEY ON MACROECONOMIC EXPECTATIONS: EXCHANGE RATE
(Nuevos Soles per US$)

	Expectations about:		
	IR Jun.13	**IR Sep.13**	**IR Dec.13***
Financial entities			
2013	2.56	2.80	2.80
2014	2.54	2.80	2.85
2015	2.55	2.82	2.85
Economic analysts			
2013	2.55	2.80	2.80
2014	2.55	2.85	2.90
2015	2.50	2.85	2.90
Non-financial firms			
2013	2.60	2.80	2.80
2014	2.60	2.82	2.82
2015	2.63	2.90	2.85
Average			
2013	2.57	2.80	2.80
2014	2.56	2.82	2.86
2015	2.56	2.86	2.87

* Survey conducted during the second fortnight of November 2013.

76. The multilateral real exchange rate index rose from 92.6 to 93.6 between September and November 2013, which represents a real depreciation of the Nuevo sol of 1.02 percent in this period. This real depreciation results from an increase of 0.56 percent in the nominal exchange rate relative to the basket of currencies of Peru's major trading partners, as well as in a higher inflation differential.

Graph 74
MULTILATERAL RER
(Index 2009=100)

Reserve requirements

77. Since May 2013, the BCRP has been implementing measures to ease reserve requirements in domestic currency, establishing caps on the rates of mean reserve requirements which have declined from 20 percent to 15 percent. In this way, the Central Bank has contributed to meet the demand for credit without generating upward pressures on interest rates in soles, in a context of an increased demand for dollars from banks.

The rate of reserve requirements was last reduced in December, when the maximum limit of the mean rate of reserves was lowered and the rate of marginal reserves was lowered from 16 to 15 percent, as a result of which liquidity for about S/. 1 billion was released.

Moreover, additional reserve requirements to the expansion of credit in foreign currency were established since October 2013 (with the exception of earmarked loans for foreign trade operations) as had been done previously in the case of the required reserves for mortgage and vehicle loans in February 2013. In addition to contributing to increase the pace of the de-dollarization of credit, this measure reduces the potential costs of dollarization.

Thus, the base rate of required reserves for financial institutions whose average daily balance of credit in foreign currency –excluding credits for foreign trade– is more than 1.05 times (1.10) the balance of credit in September 2013 will increase by 1.5 (3.0) percentage points. If the average daily balance of credit in foreign currency –excluding credits for foreign trade– exceeds 1.15 times the balance of credit in September 2013, the base rate will increase by 5.0 percentage points.

78. In order to offset the impact of the increase in long-term interest rates in dollars and the increase in the country risk indicator, in September the Board of the BCRP approved to reduce as from October the average term of short-term loans and bonds subject to reserve requirements of 50 percent from 3 years to 2 years. Moreover, the rate of required reserves applied to the excess of loans and bonds with longer terms than 2 years relative to 2.2 times the capital of the bank at December 2012 was lowered from 25 to 20 percent and it was established that new liabilities and 2 - 3 year-bonds will also be subject to the same rate of additional reserves of 20 percent.

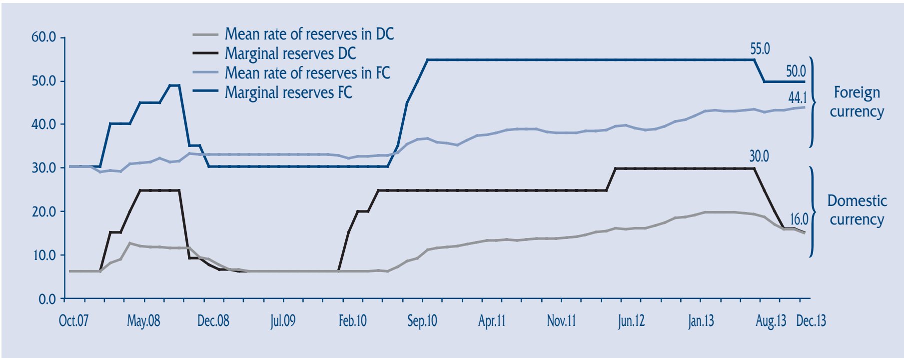
The rate of required reserves for 2 year-credit lines for foreign trade operations is 20 percent if these credit lines do not exceed 35 percent of a bank's capital, which results in a broad margin for trade loans with a low level of reserve requirements for these loans.

With these measures, the mean rate of required reserves in foreign currency went from 43.4 percent in June to an estimated rate of 43.8 percent in November.

Table 40
RESERVE REQUIREMENTS MEASURES

	Legal minimum reserve requirement	Domestic currency			Foreign currency			
					General regime			Foreign liabilitites
		Marginal reserve requirement on deposits	Increase in the mean reserve requirement	Maximum of mean reserve requirement	Marginal reserve requirement on deposits	Increase in the mean reserve requirement	Maximum of mean reserve requirement	Short term
Dec.10	9%	25%			55%			75%
Jan.11	9%	25%			55%			60%
Feb.11	9%	25%	0.25%		55%	0.25%		60%
Mar.11	9%	25%	0.25%		55%	0.25%		60%
Apr.11	9%	25%	0.50%		55%	0.50%		60%
May.12	9%	30%	0.50%		55%	0.50%		60%
Sep.12	9%	30%	0.50%		55%	0.50%		60%
Oct.12	9%	30%	0.50%		55%	0.50%		60%
Nov.12	9%	30%	0.75%		55%	0.75%		60%
Dec.12	9%	30%	-.-		55%	-.-		60%
Jan.13	9%	30%	0.25%		55%	0.75%		60%
Feb.13	9%	30%	-.-		55%	1.00%		60%
Mar.13	9%	30%	-.-		55%	0.50%		60%
Apr.13	9%	30%	-.-		55%	0.25%		60%
May.13	9%	30%	-.-		55%	-.-		60%
Jun.13	9%	30%	-.-	20%	55%	-.-		60%
Jul.13	9%	30%	-.-	-.-	55%	-.-		60%
Aug.13	9%	25%	-.-	19%	50%	-.-	45%	50%
Sep.13	9%	20%	-.-	17%	50%	-.-	-.-	50%
Oct.13	9%	16%	-.-	16%	50%	-.-	-.-	50%
Nov.13	9%	16%	-.-	-.-	50%	-.-	-.-	50%
Dec.13	9%	15%	-.-	15%	50%	-.-	-.-	50%

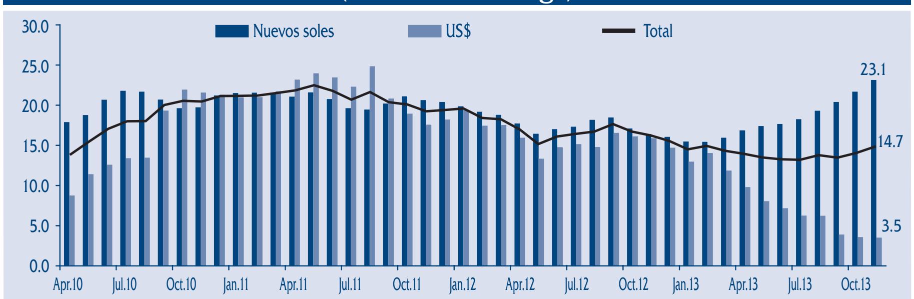
Graph 75
RATES OF RESERVE REQUIREMENTS IN DOMESTIC AND FOREIGN CURRENCY
(As percentage of total obligations subject to legal requeriments)



Credit to the private sector

79. So far in Q4, credit to the private sector in domestic currency continues to show a faster pace of growth with a rate of 23.1 percent in November (versus 17.6 percent in June and 16.0 percent in 2012). This has contributed to offset the lower growth of credit in dollars, whose pace of growth declined from 7.1 percent in June to 3.5 percent in November. The higher pace of growth of credit in domestic currency reflects the greater perception of risk associated with contracting debts in dollars as well as the effect of the reserve requirement measures for loans in dollars implemented by the Central Bank to reduce banks' incentives to grant credit in this currency. A higher ratio of dedollarization of credit contributes to strengthen the financial system because it reduces the risk associated with foreign exchange mismatches in the balance sheet of economic agents.

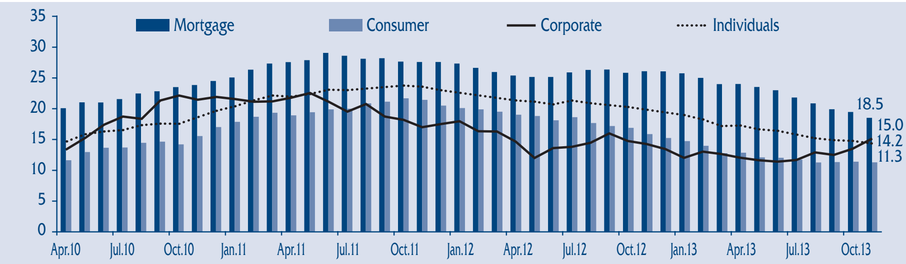
Graph 76
CREDIT TO THE PRIVATE SECTOR
(12 months % change)



Credit		Dec.09	Dec.10	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Oct.13	Nov.13
Nuevos soles	Monthly flows (Million S/.)	569	1,514	1,669	1,660	1,748	2,318	2,661	2,136	3,033
	Monthly % change	1.0	2.2	2.1	1.8	1.8	,2.3	2.4	1.9	2.7
	Annual % change	17.9	21.2	20.4	16.0	15.9	17.6	20.4	21.7	23.1
US$	Monthly flows (Million US$)	343	368	570	370	-13	326	-181	99	191
	Monthly % change	2.0	1.8	2.3	1.3	0.0	1.2	-0.6	0.3	0.7
	Annual % change	-0.1	21.3	18.2	14.7	11.8	7.1	3.9	3.6	3.5
Total	Monthly flows (Million S/.)	1,444	2,451	3,121	2,604	1,714	3,149	2,200	2,388	3,520
	Monthly % change	1.4	2.0	2.2	1.6	1.0	1.8	1.2	1.3	1.9
	Annual % change	9.3	21.2	19.4	15.4	14.2	13.1	13.3	13.9	14.7

A similar conduct is observed in the dynamics of credit by type of placements. In November, for example, mortgage loans in soles grew 36.6 percent, which offset the slowdown in the pace of growth of mortgage loans in dollars (-3.3 percent in November). Credit to businesses showed an overall rate of 15 percent (27.0 percent in soles and 4.7 percent in dollars), a higher rate than the one recorded at the close of Q3 (12.4 percent), while consumer loans remained stable with growth rates close to 11 percent.

Graph 77
CREDIT BY TYPE OF LOANS: APRIL 2010 - NOVEMBER 2013
(12 months % change)



Credit		Dec.09	Dec.10	Dec.11	Dec.12	Mar.13	Jun.13	Sep.13	Oct.13	Nov.13
Corporate	Annual % change	8.0	22.0	17.5	13.3	12.5	11.3	12.4	13.4	15.0
Individuals	Annual % change	11.8	19.7	23.1	19.4	17.1	16.3	14.8	14.6	14.2
Consumer	Annual % change	9.3	17.0	20.5	15.2	12.8	12.0	11.3	11.4	11.3
Mortgage	Annual % change	16.8	24.5	27.5	26.0	24.0	23.0	19.9	19.5	18.5

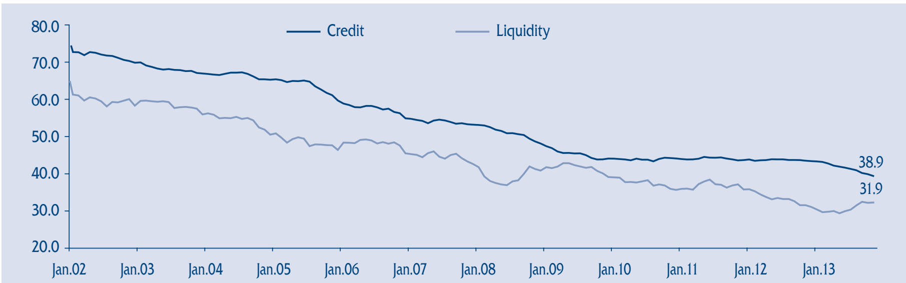
In 2014 credit is estimated to grow around 13.5 percent, driven mainly by credit in domestic currency which would continue to be more dynamic than credit in dollars. This trend in credit is consistent with the growth forecast of 6.0 percent in 2014. Should deposits in soles continue to show a slower pace of growth, the BCRP will consider the possibility of continue lowering the rate of required reserves in soles in order to provide a more permanent source for the expansion of credit in soles in order not to affect interest rates in soles in the financial system.

80. A greater preference for saving in dollars continued to be seen in Q3, which reflected in banks' high availability of liquidity in foreign currency. Thus, in Q3-2013 banks' liquidity in dollars increased by US$ 3.68 billion, of which, given the lower demand for credit in dollars, US$ 2.62 billion was held as banks' deposits at the Central Bank and US$ 1.82 billion was used to reduce banks' net short term external liabilities.

It is worth pointing out that this process in which banks substitute short-term external liabilities by local deposits is not associated with constraints in the supply of external credit, but rather with banks' lower demand for external credit due to the greater availability of liquidity in dollars in the domestic financial system, which, as previously mentioned, has reflected also in historically low short-term interest rates in dollars. In other words, the lower external credit registered in Q3 would not be associated with a capital outflow but rather with an excess of domestic liquidity in dollars.

81. The ratio of dollarization of credit fell from 40.5 percent in August to 38.9 percent in November in a context of an increased perception of risk associated with a greater strengthening of the dollar. On the other hand, the ratio of dollarization of liquidity increased from 31.1 to 31.9 percent in the same period.

Graph 78
DOLLARIZATION RATIO: 2002 - 2013
(%)



By type of credit, mortgage loans show a higher pace of dedollarization –the ratio of dollarization declined from 39.7 to 37.0 percent between August and November–, while the ratio of dollarization of credit to businesses fell from 51.0 in August to 49.1 percent in November.

Table 41
DOLLARIZATION RATIO OF CREDIT TO THE PRIVATE SECTOR 1/
(%)

	Dec.12	Mar.13	Jun.13	Sep.13	Oct.13	Nov.13
Corporate credit	53.8	53.1	51.9	50.1	49.7	49.1
Individual credit	23.9	23.6	22.8	21.6	21.2	20.8
Consumer loans	9.7	9.8	9.7	9.3	9.2	9.2
Car loans	76.5	76.9	76.9	75.4	74.5	73.8
Credit cards	6.4	6.6	6.7	6.5	6.7	6.7
Mortgage loans	44.8	43.4	41.3	38.8	37.8	37.0
TOTAL,	**43.0**	**42.3**	**41.2**	**39.7**	**39.4**	**38.9**

The flow of credit by type of loans provides additional information that confirms the faster pace of the process of de-dollarization of credit to the private sector. The ratio of dollarization of the annual flow of corporate loans fell from 28.2 percent to 16.8 percent between August and November 2013 (55.3 percent in December 2012).

The flow of mortgage loans in domestic currency accumulated between December 2012 and November 2013 amounted to S/. 4.45 billion, while on the other hand mortgage loans in foreign currency showed a negative flow of US$ 167 million. This would be indicating that banks no longer place loans in foreign currency in this segment and that the existing ones have not been renewed.

Table 42
MORTGAGE LOANS BY CURRENCY
(% change and % by Non-performing portfolios)

	Nov.12	Dec.12	Mar.13	Jun.13	Sep.13	Nov.13
Mortgage loans						
Domestic currency (12 month % change)	31.7	33.2	33.7	37.1	37.0	36.6
Foreign currency (12 month % change)	19.9	18.2	13.2	7.3	0.1	-3.3
Total (12 month % change)	**26.0**	**26.0**	**24.0**	**23.0**	**19.9**	**18.5**
Non-performing portfolios (% Total)						

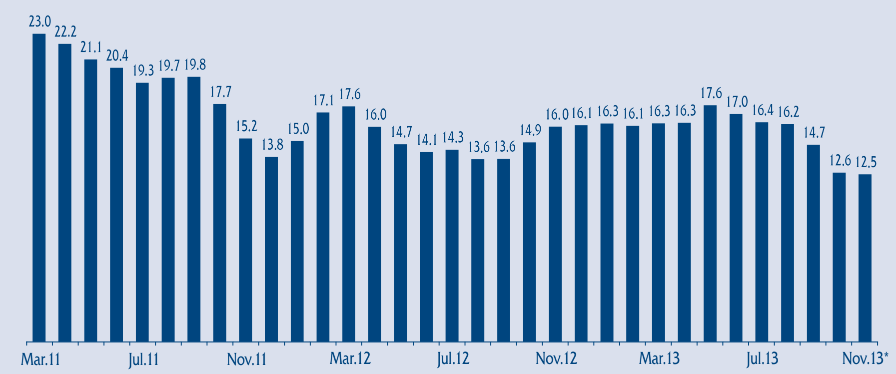
Credit to the private sector as a percentage of GDP grew significantly above the trend observed between Q3-2008 and Q2-2010 as a result of the strong capital inflow registered in the Peruvian economy in that period. After the international financial crisis, the credit-to-GDP ratio has remained close to its trend, reflecting the effect of the preventive measures taken by the BCRP in a context of capital inflows. At September 2013, the balance of credit to the private sector of depository institutions was equivalent to 32.5 percent of GDP.

Graph 79
RATIO:CREDIT/GDP
(Annual ratios of quaterly data, %)

Currency in circulation and deposits

82. Recording in the last two months the lowest growth rates observed in the last 24 months, mean currency grew at an annual rate of between 12.5 and 14.7 percent between September and November 2013, which reflects the slowdown of economic activity registered in Q3. The pace of growth of currency in circulation is expected to recover in the following quarters, in line with the greater dynamism foreseen in economic activity.

Graph 80
AVERAGE CURRENCY IN CIRCULATION
(% change respect to the similar period of previous year)

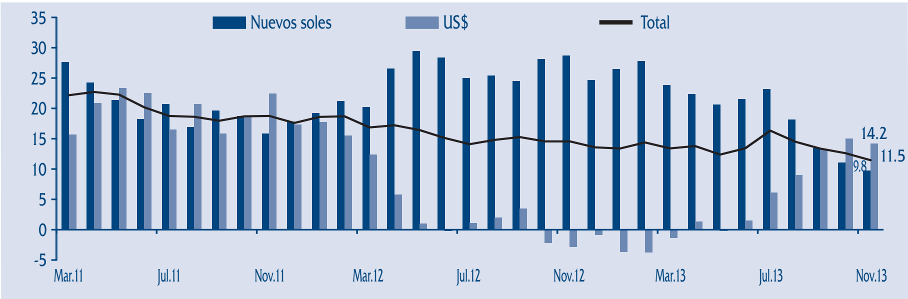


* Preliminary.

Private sector deposits

83. So far in Q4, private sector deposits have continued declining. In November private sector deposits grew 11.5 percent (versus 13.4 percent in June and 13.6 percent in 2012). This evolution of deposits reflects the slowdown in the growth of deposits in domestic currency, whose growth rate fell from 21.5 percent in June to 9.8 percent in November. On the other hand, deposits in foreign currency increased their pace of growth from 1.5 to 14.2 percent in the same period. This faster pace of growth of deposits in dollars reflects institutional investors' preference for foreign currency due to the increased uncertainty registered in international financial markets.

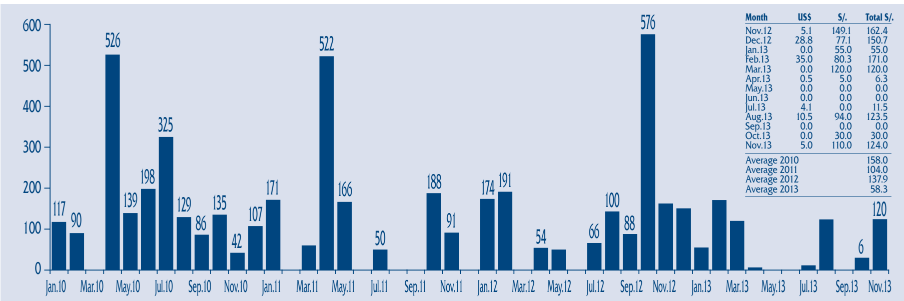
Graph 81
DEPOSITS IN THE PRIVATE SECTOR
(12 months % change)



Capital Market

84. Between August and November, non-financial firms issued bonds for a total of S/. 154 million, of which 91 percent was bonds issued in domestic currency. On average, the securities issued in 2013 are lower by S/.80 million than those issued in 2012.

Graph 82
BONDS ISSUED BY NON-FINANCIAL FIRMS*
(Million S/.)



Month	US$	S/.	Total S/.
Nov.12	5.1	149.1	162.4
Dec.12	28.8	77.1	150.7
Jan.13	0.0	55.0	55.0
Feb.13	35.0	80.3	171.0
Mar.13	0.0	120.0	120.0
Apr.13	0.5	5.0	6.3
May.13	0.0	0.0	0.0
Jun.13	0.0	0.0	0.0
Jul.13	4.1	0.0	11.5
Aug.13	10.5	94.0	123.5
Sep.13	0.0	0.0	0.0
Oct.13	0.0	30.0	30.0
Nov.13	5.0	110.0	124.0
Average 2010			158.0
Average 2011			104.0
Average 2012			137.9
Average 2013			58.3

* Emissions are measured in dollars at the rate of change of last month. Includes titulization bonds.

In September 2013, Peruvian companies issued bonds again in the international market at higher interest rates than those observed before May, in line with the increase of risk in emerging countries and the evolution of the yield of sovereign bonds. Thus, bonds for a total of US$ 5.74 billion were issued at coupon rates of between 2.25 and 9.0 percent between January and April, while bonds for a total of US$ 515 million at rates between 7.5 and 11.0 percent were issued between September and November.

The bond issuances announced for 2013 that are still pending include those of Nexus Capital Partner II and Chinalco which would amount to US$ 630 million.

Table 43
BONDS ISSUED IN THE INTERNATIONAL MARKET

BUSINESS	Amount (Million US$)	Maturity (years)	Rate
Year 2012	**2,960**		
Non-financial sector	**1,810**		
Volcan	600	10	5.38%
Camposol	125	5	9.88%
Terminales Portuarios Euroandinos	110	25	8.13%
Ajecorp	450	10	6.50%
Coazucar (Grupo Gloria)	325	10	6.38%
Maestro	200	7	6.75%
Financial sector	**1,150**		
BBVA Banco Continental	500	10	5.00%
Interbank	250	8	4.80%
Scotiabank Perú	400	15	4.50%
Year 2013	**6,886**		
JANUARY-APRIL	**5,741**		
Non-financial sector	**3,555**		
Copeinca	75	5	9.00%
Exalmar	200	7	7.38%
Cementos Pacasmayo	300	10	4.63%
Alicorp	450	10	3.88%
Gas Natural de Lima y Callao - Cálidda	320	10	4.38%
Compañía Minera Milpo	350	10	4.63%
Corporación Lindley	260	10	4.63%
Ferreycorp	300	7	4.88%
Transportadora de Gas del Perú	850	15	4.25%
Consorcio Transmantaro	450	10	4.38%
Financial sector	**2,186**		
BBVA Banco Continental	300	4	2.31%
Fondo MiVivienda	500	10	3.50%
BBVA Banco Continental	500	5	3.38%
Banco de Crédito (marzo)	716	10	4.25%
Banco de Crédito (abril)	170	14	6.13%
SEPTEMBER-NOVEMBER	**515**		
Non-financial sector	**350**		
Inkia Energy	150	8	8.38%
San Miguel Industrias	200	7	7.75%
Financial sector	**165**		
Andino Investment Holding	115	7	11.00%
Interbank	50	10	7.50%

85. Following the trend in the yields on the US Treasury bonds and in the country risk, the yields of sovereign bonds dropped 44 basis points on average compared to August. Thus, between August and November the yields on the US Treasury bonds declined on average 11 basis points, while the rates of global bonds declined 33 basis points. The yield of the short-term Peruvian BTP (PERU 2015) dropped 69 basis points and continues to register lower levels than the BCRP policy rate. The yield of the 2020 BTP and 2023 BTP bonds dropped the most in the middle section of the curve (between 5 and 10 years). Moreover, the yield of the long-

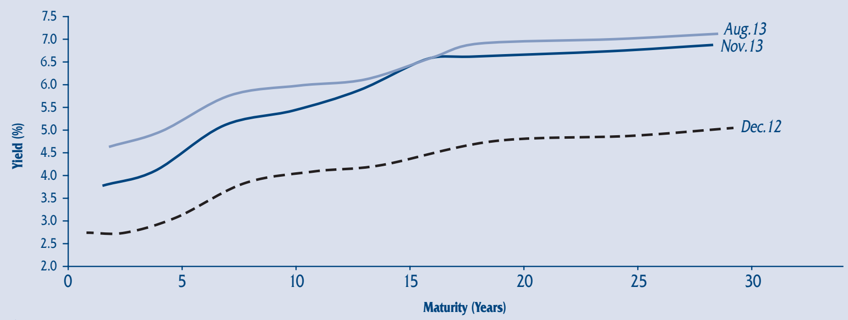
term sovereign bonds PERU 2037 fell by 26 basis points, while the yield of global bonds PERU 2037 remained stable.

Table 44
PERU GLOBAL AND SOVEREIGN BOND YIELDS AND US TREASURY BONDS BY MATURITY
(At the end of period, in percentage points)

	Dec.12 (3)	Aug.13 (2)	Nov.13 (1)	Variation (In bps) Nov.13 / Aug.13 (1)-(2)	Nov.13 / Dec.12 (1)-(3)
Sovereign bonds (S/.)					
PERU 2013	2.70	2.80			
PERU 2015	2.71	4.46	3.78	-69	107
PERU 2017	3.05	4.89	4.12	-77	107
PERU 2020	3.80	5.74	5.11	-63	131
PERU 2023	4.09	5.96	5.47	-49	138
PERU 2026	4.24	6.04	5.94	-11	170
PERU 2031	4.79	6.99	6.65	-34	186
PERU 2037	4.90	7.04	6.78	-26	188
PERU 2042	5.10	7.16	6.90	-26	180
Global bonds (US$)					
PERU 2015	0.82	0.69	0.30	-39	-52
PERU 2016	1.10	2.07	1.50	-57	40
PERU 2019	1.84	3.29	2.98	-31	114
PERU 2025	3.00	4.69	4.40	-29	140
PERU 2033	3.64	5.51	5.42	-8	178
PERU 2037	3.70	5.52	5.51	0	181
US Treasury					
2 Years bond	0.25	0.40	0.28	-12	4
3 Years bond	0.35	0.78	0.55	-24	20
5 Years bond	0.71	1.64	1.37	-27	66
10 Years bond	1.70	2.79	2.75	-4	104
30 Years bond	2.87	3.70	3.81	11	94

Even though the yield curve at November has declined relative to August, it still shows higher levels than the ones observed at end 2012.

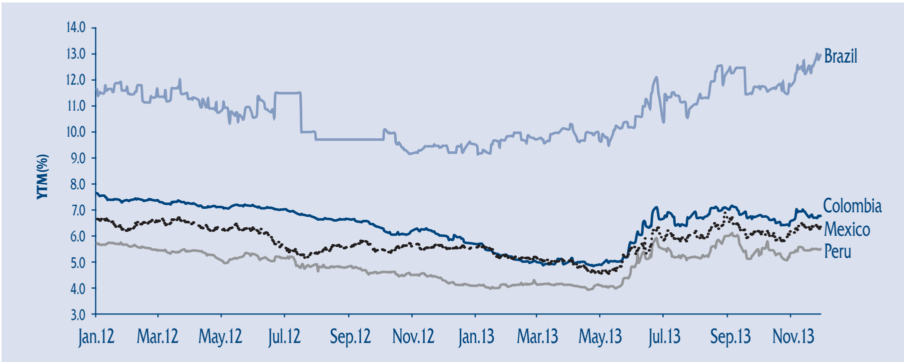
Graph 83
YIELD CURVE OF SOVEREIGN BONDS IN THE SECONDARY MARKET 1/



1/ End of month yield.

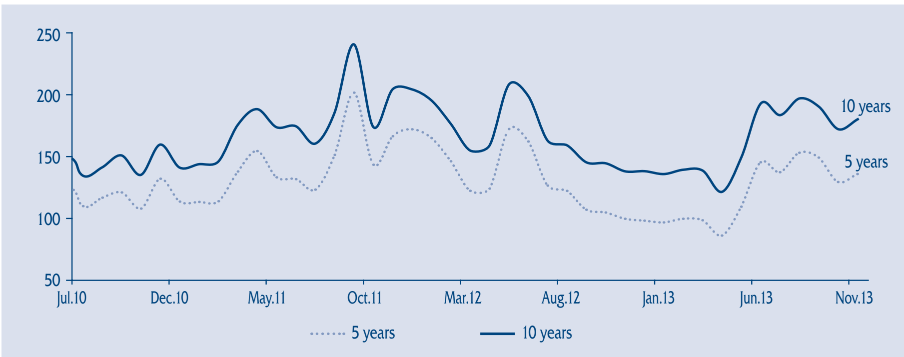
It should be pointed out that the yields on Peruvian Treasury Bonds (BTP) are the lowest yields in the region and also the ones that have increased the least since May 2013. Thus, the yield on Peru's 10-year bond has increased by 132 basis points, while the yields on the Sovereign Bonds of Brazil, Colombia, and Mexico have increased by 325, 186, and 176 basis points, respectively. Despite the increase observed recently, the levels of the yields on these bonds are similar to the ones registered in mid- 2011.

Graph 84
LATAM YIELD CURVE OF 10 YEAR SOVEREIGN BOND
(%)



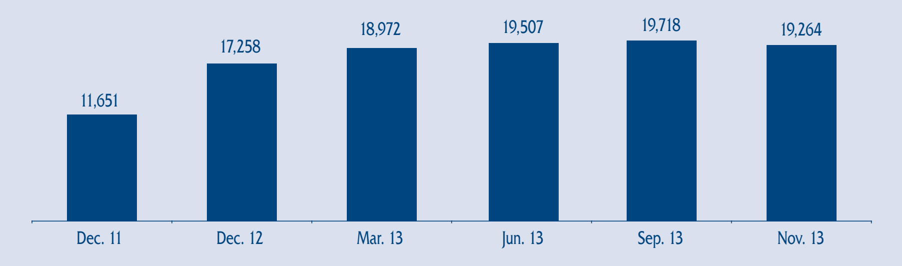
86. The upward trend of the spreads of Peru's 5-year to 10-year sovereign debt, measured by the credit default swaps (CDS), stabilized in November. Thus, between August and November, the 5-year CDS has fallen 17 basis points and the 10-year CDS has fallen 17 basis points.

Graph 85
CREDIT DEFAULT SWAPS OF SOVEREIGN PUBLIC DEBT
(Basis points)



Non-residents' holdings of sovereign bonds have declined from S/. 19.72 billion in September 2013 to S/. 19.26 billion in November, but still show a higher level than the one registered in March 2013 (S/. 18.97 billion).

Graph 86
NON-RESIDENTS' HOLDINGS OF SOVEREIGN BONDS
(Million S/.)



87. The administrators of private pension funds (AFPs) have increased their investments abroad by US$ 642 million compared to the end of Q3-2013 and by US$ 1.25 billion compared to December 2012. With this, the percentage of AFPs' investment abroad has increased from 29.4 percent in December 2012 to 34.8 percent in November 2013 (below the operative limit of 36 percent). The rest of their investments in dollars have increased by US$ 108 million between September and October 2013.

In October the investment portfolio showed a slight transfer of investments from domestic investments (shares of non-financial companies and BCRP certificates of deposit) to investments abroad (government bonds and securitization companies).

Table 45
PORTFOLIOS MANAGED
BY FINANCIAL INSTRUMENTS AND AFP
(Million S/.)

	Dec.11		Dec.12		Oct.13	
	Amount	%	Amount	%	Amount	%
I. DOMESTIC INVESTMENT	**58,185**	**71.1**	**68,055**	**70.3**	**65,905**	**65.4**
1. Government	**13,915**	**17.0**	**16,939**	**17.5**	**14,329**	**14.2**
Certificates and term deposits of BCRP (1)	886	1.1	2,830	2.9	3,212	3.2
Bonds of Central Government	13,029	15.9	14,109	14.6	11,117	11.0
2. Financial entities	**14,333**	**17.5**	**16,268**	**16.8**	**21,530**	**21.4**
Shares and Securitised Shares	5,294	6.5	5,572	5.8	3,868	3.8
3. Non-financial firms	**23,175**	**28.3**	**26,058**	**26.9**	**20,495**	**20.3**
Shares and Securitised Shares	16,881	20.6	19,272	19.9	14,335	14.2
4. Fund managers	**3,000**	**3.7**	**3,680**	**3.8**	**4,118**	**4.1**
5. Securitization companies	**3,763**	**4.6**	**5,111**	**5.3**	**5,433**	**5.4**
II. FOREIGN INVESTMENTS	**23,437**	**28.6**	**28,512**	**29.4**	**35,123**	**34.9**
1. Government	**949**	**1.2**	**1,705**	**1.8**	**1,366**	**1.4**
2. Financial entities	**2,738**	**3.3**	**2,640**	**2.7**	**3,607**	**3.6**
3. Non-financial firms	**8,220**	**10.0**	**6,249**	**6.5**	**6,656**	**6.6**
4. Fund managers	**11,529**	**14.1**	**17,918**	**18.5**	**23,493**	**23.3**
5. Securitization companies	**-**	**-**	**-**	**-**	**-**	**-**
III. OPERATIONS IN TRANSIT	**260**	**0.3**	**286**	**0.3**	**(290)**	**-0.3**
TOTAL	**81,881**	**100.0**	**96,853**	**100.0**	**100,738**	**100.0**
Foreign investment / Portfolio managed	**28.6%**		**29.4%**		**34.8%**	

1/ Includes Overnight deposits and BCRP Certificates of Deposit with Restricted Negotiation (CDBCRP-NR).

The Central Bank has recently approved a schedule of increases in the limit of the AFPs' investment abroad according to which this limit will be increased by 0.5 percent on a monthly basis since December 2013 until it reaches a limit of 40 percent of the investment portfolio managed.

Table 46
AFP INVESTMENT
(Million US$)

Date	Total			
	Abroad		In US$	
	Amount	% Portfolio	Amount	% Portfolio
Dec.12	11,177	29.4	19,646	51.7
Jan.13	11,814	30.6	20,113	52.1
Feb.13	11,937	31.1	19,979	52.0
Mar.13	12,230	31.6	20,684	53.4
Apr.13	12,891	33.9	20,784	54.7
May.13	12,689	35.4	20,473	57.0
Jun.13	12,091	35.2	19,841	57.6
Jul.13	12,080	34.6	20,626	59.0
Aug.13	11,594	33.8	20,013	58.3
Sep.13	11,874	33.7	20,478	58.1
Oct.13	12,661	34.8	21,226	58.4

88. In the variable-income market, the General Index of the Lima Stock Exchange (IGBVL) fell 4.5 percent in November relative to September, in line with the main exchange indices in the region. By sectors, the mining, industrial, and agriculture shares were negatively affected by the international context, especially due to the lower prices of precious metals (gold and silver) and copper. On the other hand, the stocks of companies in the sector of services registered a recovery in the last quarter.

Graph 87
LSE: GENERAL INDEX
(January 2, 2012=100)

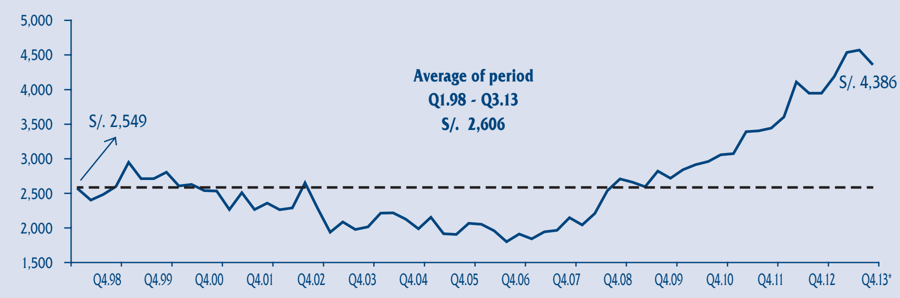
Table 47
LSE: CHANGE IN SECTORIAL INDICES
(%)

	Agriculture and livestock	Banks and financial entities	Diverses	Industry	Mining	Services	General Index
Nov.13/Dec.12	-40.6	-5.2	2.5	-11.2	-44.9	18.3	-26.3
Nov.13/Sep.13	-4.3	-2.3	-0.4	-3.7	-10.5	5.5	-4.5

Real estate market

89. In Q4-2013, the prices per square meter of property in the five districts of the sample (La Molina, Miraflores, San Borja, San Isidro, and Surco) in constant soles fell slightly compared to the previous quarter. The graph below shows the evolution of median quarterly sale prices of apartments per square meter in constant soles of 2009.

Graph 88
MEDIANS OF QUARTERLY SALE PRICES PER SQUARE METER OF APARTMENTS 1998-2013
La Molina, Miraflores, San Borja, San Isidro, and Surco (Base 2009=100)



* To November.

Sale price-to-income for annual rent ratio (price to earnings ratio - PER):

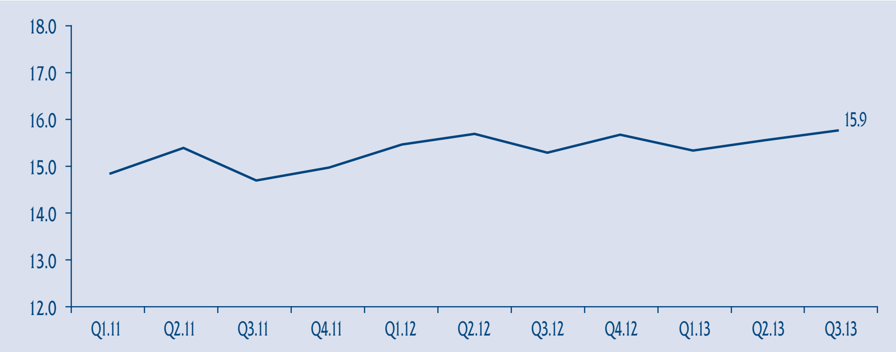
The price-to-earnings ratio (PER), which shows the number of years of rent required to recover the purchasing value of a property, has shown stable values of 15 and 16 over the last years and has remained within the ranges considered as normal, according to the criteria taken into account by Global Property Guide.

Table 48
PER: PRICE TO EARNING RATIO

	Q1.12	Q2.12	Q3.12	Q4.12	Q1.13	Q2.13	Q3.13
Jesús María	13.0	15.7	15.5	14.9	15.0	15.6	15.7
La Molina	12.7	10.7	12.4	11.6	13.7	14.7	15.5
Lince	13.9	14.2	14.2	16.4	14.1	14.6	15.4
Magdalena	14.5	14.1	13.1	16.0	14.0	14.5	15.1
Miraflores	19.0	17.0	15.3	15.0	14.8	16.5	16.3
Pueblo Libre	15.4	16.5	15.2	16.0	14.1	14.3	15.3
San Borja	15.3	19.5	16.8	18.2	18.6	17.5	17.1
San Isidro	19.7	17.7	17.2	18.4	18.0	17.2	17.3
San Miguel	14.8	15.3	16.1	15.6	14.4	14.8	14.7
Surco	16.6	16.7	17.1	15.0	16.8	16.3	16.5
Aggregated							
Average	15.5	15.7	15.3	15.7	15.3	15.6	15.9

Memo: Rates have been calculated using the sale price median and rent of each district.
According to the PER index, Global Property Guide classifies the real estate market in properties with Undervalued Prices (5.0-12.5), Normal Prices (12.5-25.0), and Overvalued Prices (25.0-50.0).
Source: BCRP.

Graph 89
PER: PRICE TO EARNING RATIO

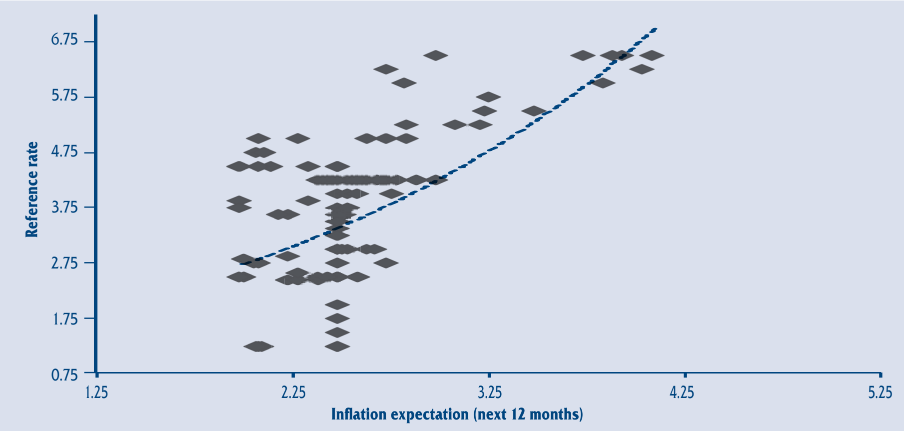


Box 4
THE MONETARY POLICY INTEREST RATE AND RESERVE REQUIREMENTS

This article discusses the use of the reference or policy interest rate and the use of the rate of reserve requirements by the BCRP. In the inflation targeting regime, the reference interest rate is the operational target of the Central Bank. Any adjustment in this rate is aimed at maintaining inflation under control. The following graph illustrates the role of the reference rate of the BCRP. When the level of expected inflation increases, this rate is raised as a signal that induces expectations to return to the target[7].

7 The slope of the relationship between the reference rate and expectations of inflation in the next 12 months is 1.57.

REFERENCE INTEREST RATE AND INFLATION EXPECTATION
(%)



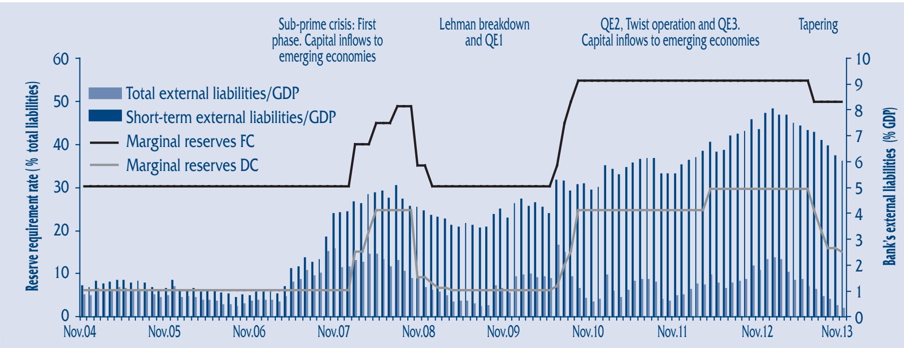
Changes in the reference rate are passed-through to the economy mainly via this rate's influence on:

i) How people's economic expectations are formed;
ii) The term structure of interest rates in the market, and
iii) Changes in the relative valuations of assets in national currency and in foreign currency.

Thus, managing the reference rate, the Central Bank establishes a level of interest rates that is consistent with price stability. Once the level of the reference rate is established, the Central Bank adjusts monetary conditions through open-market operations to anchor the interbank interest rate to the reference or policy rate.

The BCRP inflation targeting scheme also uses other monetary policy instruments, such as interventions in the foreign exchange market and the rate of reserve requirements with the aim of reducing the risks associated with dollarization. Recently, several central banks have increased the use of other monetary policy instruments in order to enhance their effectiveness and reduce the risk of vulnerabilities in the financial system.

DOMESTIC AND FOREIGN RESERVE REQUIREMENTS
AND BANKS' EXTERNAL LIABILITIES



Reserve requirements are mainly used to prevent a disorderly evolution of credit arising from sudden movements in the sources of external and domestic financing. Thus, for example, an increase in reserve requirements offsets the expansions of credit financed by strong capital inflows and also allows the Central Bank to accumulate international reserves preventively.

The use of reserve requirements takes into account the different sources of macro risks associated with the structure of the obligations of financial institutions. For example, the rate of required reserves for deposits in national currency is currently 15 percent, 50 percent for domestic obligations in foreign currency, 50 percent for short-term external liabilities, and 20 percent for long-term and foreign trade obligations, and 120 percent for non-resident financial investors' deposits in domestic currency.

The BCRP has been actively using reserve requirements both in soles and in dollars with the aim of contributing to an orderly evolution of liquidity and credit in a context of strong volatile capital inflows. Thus, from 2011 until April 2013, the rates of required reserves both in soles and in dollars were raised and new reserve requirements were established to reduce banks' incentives to give loans in dollars and especially to discourage banks from granting loans in dollars to households since families are more strongly exposed to foreign exchange credit risk.

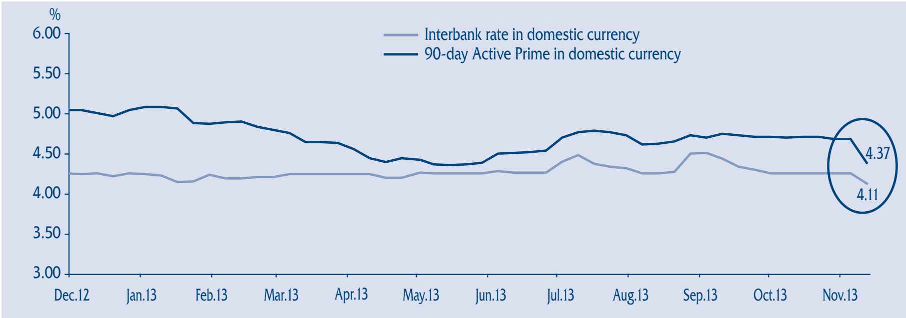
This strategy of making adjustments in reserve requirements and raising the rates of required reserves on the obligations of the financial entities that operate in the domestic market local (quantitative tightening - QT) has been used to offset the effects of quantitative easing (QE) in developed economies.

These measures have strengthened banks' level of international liquidity while offsetting their exposure to short-term capitals and thus enhancing the financial system's capability to face a reversal of these capital flows. The reserve requirement measures adopted during this period have prevented an excessive growth of credit and extraordinarily low interest rates in dollars, all of which has contributed to make the level of 4.25 percent of the reference rate during this period consistent with maintaining inflation within the target range in the forecast horizon.

Since May 2013, the increased likelihood that the Fed would cut quantitative easing measures brought about a significant correction in the value of the currencies and in the yields of sovereign bonds of emerging economies. The measures that had been taken previously allowed the Peruvian economy to face this period of greater volatility in financial markets without compromising the evolution of credit. On the other hand, since May 2013 the BCRP reduced the rate of reserve requirement in nuevos soles by 5 percentage points, from 20 to 15 percent, which released enough liquidity to meet the increased demand for credit in nuevos soles, which had increased its pace of growth and grown from a rate of 16.8 percent in April to 21.7 percent in October, replacing the demand for credit in dollars.

This contributed to accelerate the process of de-dollarization of credit without generating upward pressures on interest rates in soles. In order to reinforce this process, additional reserve requirements were established in August for banks when the growth of credit exceeded 5 percent relative to September 2013.

90-DAY CORPORATE PRIME RATE VERSUS INTERBANK OVERNIGHT RATE IN DOMESTIC CURRENCY: DEC.12 - NOV.13
(%)



This orderly evolution of credit and monetary and credit conditions has also contributed to the immediate pass-through of the recent reduction of the reference interest rate in November to both the lending and deposit prime interest rates in the financial system, which enhances the transmission channel of changes in the reference rates.

The experience of central banks in dealing with the global financial crisis has evidenced the need of using a broader range of instruments and taking preventive actions that offset the formation of risks in the financial system. The BCRP's combined use of reserve requirements and the interest rate is an example of this new approach of risk management and preventive measures. The results of this approach in terms of inflation as well as the evolution of credit conditions during the international financial crisis and more recently in the context of greater turbulence generated by the possibility that the Fed will start tapering its asset purchase program show the effectiveness of this scheme.

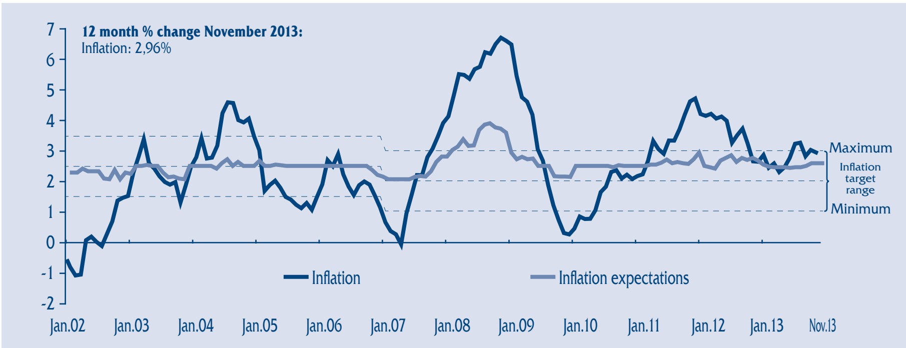
VI. Inflation

90. Inflation reached an annual rate of 3.28 percent in August. Some domestic supply shocks that had affected the evolution of the prices of some food products, such as fish and potatoes, began to subside since September. In addition to this, the prices of goods that depend on international prices, like chicken meat and sugar, showed a similar behavior and fell in the last months of the year.

This contributed to reduce the annual rate of inflation, which declined to 2.96 percent between September and November. As a result of this, the rate of inflation returned again to be within the monetary policy target range.

The variation in the foreign exchange rate –depreciation of 10 percent between January and August 2013– has had lagging effects on inflation, but these effects are expected to disappear in the following months. This would also be reinforced by the slowdown in the pace of growth of domestic spending.

Graph 91
INFLATION AND INFLATION EXPECTATIONS
(Last 12 month % change)



91. The main factors that contributed to slow down the pace of inflation between September and November included some domestic supply shocks, which account for a drop of 0.4 percentage points in inflation associated with better climate conditions. This is reflected in the lower prices of potatoes (13.3 percent) and fish (12.4 percent). This effect contrasts with the impact of domestic supply shocks in the period of January-September 2013, when these shocks caused by adverse climate and anomalous sea conditions explained an increase of 0.6 percentage points in inflation.

Table 49
WEIGHTED CONTRIBUTION TO INFLATION BY PERIODS

	Weight	January-August		September-November		January-November	
		% Chg.	Contribution	% Chg.	Contribution	% Chg.	Contribution
INFLATION	**100.0**	**2.8**	**2.76**	**-0.1**	**-0.07**	**2.7**	**2.69**
1. Foodstuffs	**37.8**	**3.4**	**1.34**	**-0.7**	**-0.28**	**2.7**	**1.06**
a. International prices shocks	10.0	-0.4	-0.04	-0.9	-0.09	-1.3	-0.13
Of which:							
Poultry meat	3.0	1.7	0.05	-4.4	-0.14	-2.8	-0.09
Sugar	0.5	-16.1	-0.11	-0.8	0.00	-16.8	-0.11
b. Domestic supply shocks	4.95	11.1	0.58	-6.9	-0.39	3.4	0.18
Of which:							
Potato	0.9	17.0	0.17	-13.3	-0.15	1.4	0.01
Fresh and frozen fish	0.7	46.6	0.32	-12.4	-0.12	28.4	0.19
c. Other vegetables	11.7	3.5	0.45	1.3	0.17	4.9	0.62
d. Fresh legumes	11.1	3.1	0.35	0.3	0.03	3.4	0.39
2. Meals outside the home	**14.3**	**2.8**	**0.39**	**0.5**	**0.06**	**3.2**	**0.46**
a. Fuels	2.8	4.6	0.14	-0.8	-0.02	3.8	0.12
b. Urban fare	8.5	1.2	0.10	0.9	0.07	2.1	0.18
c. Electricity rate	2.9	5.5	0.15	0.6	0.02	6.1	0.17
3. Related to exchange rate	**4.5**	**5.9**	**0.23**	**0.0**	**0.00**	**5.9**	**0.23**
a. Purchases of vehicles	1.6	8.7	0.12	-0.5	-0.01	8.2	0.11
b. House rent	2.4	3.0	0.06	0.4	0.01	3.4	0.07
c. Airplane fare	0.4	12.5	0.04	-0.5	0.00	11.9	0.04
4. Education	**9.85**	**4.5**	**0.46**	**0.1**	**0.01**	**4.6**	**0.47**
5. Rest	**33.58**	**1.0**	**0.33**	**0.4**	**0.14**	**1.5**	**0.47**

Another factor that contributed to slow down inflation was the dollar-nuevo sol exchange rate. After accumulating a depreciation of 9.1 percent between January and August 2013, it rose slightly by 0.1 percent between September and November. Thus, the increase in prices associated with the exchange rate, such as vehicles, house rents, and airfare, contributed with 0.2 percentage points to inflation in the period January-August of 2013, but remained stable in the following months.

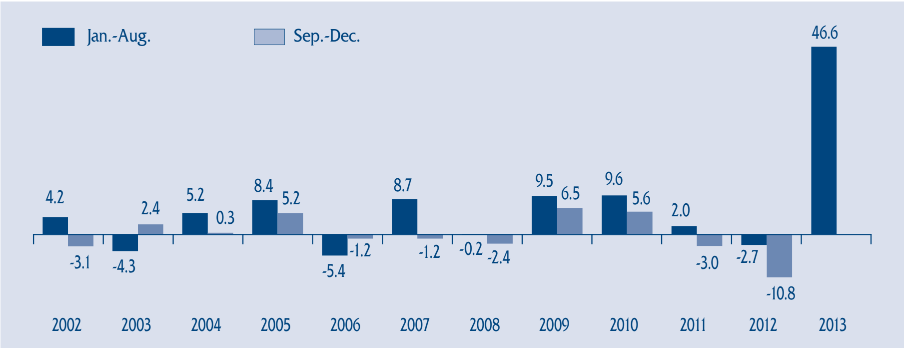
Components of inflation at November 2013

92. Among the components of inflation influenced by international prices, the fall in the price of food items with a high imported component was associated with the lower international prices of their major inputs. For example, in the case of **poultry**, the lower international prices of maize –which dropped from US$ 281.9/ ton in December 2012 to US$ 160.2 in November 2013– and by the increase in placements of baby chicken –up 6 percent in September-November compared to the same period of the previous year– contributed to offset the upward pressures generated by the lower supply and higher prices of fish.

93. As regards the prices associated with domestic supply shocks, the supply of perishable food products like potatoes and fish were affected by weather anomalies

until the month of August. The highest price increase was observed in **fish** (28.4 percent). The prices of fish products recorded an increase of 47 percent in the period January – August and fell 12.4 percent between September and November. The supply of fish was affected by weather anomalies and its price recorded successive increases from March to August. Better marine conditions in the following months contributed to reverse these price increases, except in the month of October when anomalous waves and variable weather conditions affected again the availability of species.

Graph 92
FISH PRICE
(%)



The prices of **potatoes** also showed a high rise in the period January-August (17.0 percent), especially in the months of July (18.7 percent) and August (8.8 percent), due to lower production in the regions of Pasco and Huancavelica, affected by heavy rains at the beginning of the year, as well as by climate variations in Huánuco. Better weather conditions thereafter and greater cultivation in Lima and Huánuco contributed to improve the supply in the following months, leading the prices to decline in the period September-November (-13.3 percent).

The prices of "**other vegetables**" rose 9.3 percent in January-August and fell 8.2 percent in September-November. The prices of these products were affected not only by a greater seasonal demand in Q1, but also by anomalous climate conditions in the central coast areas which delayed the production of crops, such as lettuce, and reflected in a price rise in the month of July. The normalization of temperatures in the following months contributed to improve the supply of goods afterwards. The production of lettuces increased from a daily production of 95 tons between January and August to a daily production of 107 tons between September and November.

In the case of **sugar**, the price of this product was strongly influenced by lower international prices –the price of sugar in contract 5 dropped from US$ 527/ton in December 2012 to US$ 467/ton in November 2013– and by an increase of domestic production (2 percent in the period September-November).

The price of **fresh legumes** increased 8.4 percent on average in the period January-August and fell 20.6 percent in the period September-November. The hike in the price of peas, main component of this category, was associated with a lower cultivation of this crop in the regions of Junin and Huancavelica in the first months of the farming year due to lack of rain. Lower sowing in Huanuco in March was a factor that contributed also to the rise in prices in July (17.3 percent). Declining price changes were observed since August due to better weather conditions and greater sowing in Huánuco and Junín.

Core inflation

94. The annual rate of core inflation, which excludes the most volatile items from the calculation of the CPI index, was 3.7 percent at the month of November. Inflation without food and energy rose from 1.9 percent in December 2012 to 2.9 percent in November, reflecting increases in the prices of services, particularly meals outside the home and education, and increases in some prices influenced by the depreciation of the nuevo sol.

95. The non-core component of inflation rose slightly from an annual rate of 1.5 percent in December 2012 to 1.6 percent in November 2013. Rises were observed in the prices of gasoline (which increased from -5.0 percent in December 2012 to 1.6 percent in November 2013), electricity rates (from 2.2 percent in December 2012 to 5.3 percent in November 2013), and urban fares (from 2.3 percent in December 2012 to 3.8 percent in November 2013).

Table 50
INFLATION
(%)

	Weight 2009=100	2006	2007	2008	2009	2010	2011	2012	2013 Jan.-Nov.	2013 12 month
I. INFLATION	**100.0**	**1.14**	**3.93**	**6.65**	**0.25**	**2.08**	**4.74**	**2.65**	**2.69**	**2.96**
II. CPI WITHOUT FOOD AND ENERGY	**56.4**	**1.28**	**1.49**	**4.25**	**1.71**	**1.38**	**2.42**	**1.91**	**2.48**	**2.89**
III.CORE INFLATION	**65.2**	**1.37**	**3.11**	**5.56**	**2.35**	**2.12**	**3.65**	**3.27**	**3.50**	**3.68**
Goods	32.9	0.97	3.30	5.32	2.17	1.53	3.17	2.56	2.87	2.99
Services	32.2	1.85	2.88	5.86	2.56	2.72	4.13	3.97	4.12	4.37
IV.NON-CORE INFLATION	**34.8**	**0.83**	**5.07**	**8.11**	**-2.54**	**2.00**	**6.79**	**1.52**	**1.18**	**1.59**
Foods	14.8	2.06	7.25	10.97	-1.41	1.18	11.50	2.36	0.09	-0.08
Fuels	2.8	-1.50	6.45	-0.04	-12.66	12.21	7.54	-1.48	3.80	3.45
Transportation	8.9	1.12	0.82	5.86	0.19	1.94	3.61	1.99	1.49	3.84
Utilities	8.4	-3.22	0.24	7.48	-4.56	0.01	1.50	0.54	1.99	1.72
Foodstuffs	**37.8**	**1.8**	**6.0**	**9.7**	**0.6**	**2.4**	**8.0**	**4.1**	**2.7**	**2.8**

96. When we analyze the correlations between the exchange rate and consumer prices, we find that house rents and the new vehicles have the higher correlation with the exchange rate. At November, the nuevo sol has depreciated 9.02 percent relative to its level of December 2012. In this period, rents rose 3.4 percent and the price of new vehicles rose 8.2 percent.

Recent estimates show that the pass-through effect of fluctuations in the foreign exchange rate to inflation is fast and small[8]. It is estimated that a nominal depreciation of 1 percent would push inflation up by about 0.1 percent in a period of 6 months. Therefore, it is estimated that the depreciation pressures on the nuevo sol registered by mid-2013 –particularly, the depreciation of about 10 percent observed between May and July– account for approximately 1 percent of the rate of inflation registered at the end of the year.

Table 51
PRICES WITH A HIGH CORRELATION WITH THE EXCHANGE RATE

	Weight	Maximum correlation 1/	Correlation Dec.11-Nov.13
Goods			
Electric appliances	1.3	0.96	0.10
Recreation and culture items	0.9	0.93	0.22
Jewelry	0.1	0.92	-0.11
Purchases of vehicles	1.6	0.89	0.60
Recreational item	0.7	0.86	-0.13
Car replacement part	0.2	0.69	0.09
Services			
House rent	2.4	0.99	0.97
Hotel expensives	0.1	0.74	0.21
Airplane fare	0.4	0.71	0.34

1/ Highest correlation taking moving windows of 24 months since January 1995 to November 2013.

Fuel and food prices

a. Fuels

97. The price of **WTI** oil fell 12.0 percent in the past three months as it dropped from US$ 106.55 per barrel in August –the maximum level observed in the year– to US$ 93.81 per barrel in November. However, the price of crude oil still shows an increase of 6.4 percent so far this year.

The declining trend in the price of oil was associated with a greater production of crude in the United States where it reached levels not seen since January 1989 due to the rise of non-conventional crude oil, whose production increase exceeded projections. Other countries not members of OPEC also contributed to the growth of the global production of crude oil, but to a lesser extent. Moreover, Canada and Russia's production of crude oil from also showed significant growth. In addition to this, downward pressures on the price of crude were also observed after a

8 Winkelried D. (2012), "Traspaso del tipo de cambio y metas de inflación en el Perú", Banco Central de Reserva del Perú, Revista Estudios Económicos, 23, 9-24.

temporary agreement was reached between Iran and the G-5 countries that are members of the UN Security Council and Germany.

This higher production of crude offset the lower supply of OPEC countries associated with the temporary suspension of some OPEC members (particularly, Iraq and Libya), as well as the decline in the production of Saudi Arabia during the year in response to a well-supplied global market.

Table 52
OIL AND LIQUID FUELS: SUPPLY AND DEMAND
(Million barrels per day)

	2012	2013*	2014*
Supply	89.31	90.10	91.54
OPEP	36.64	35.87	35.84
Non-OPEP	52.67	54.22	55.70
Consumption	89.17	90.25	91.39
OECD	45.91	45.82	45.64
Non-OECD	43.26	44.42	45.75
Market balance	0.14	-0.15	0.15
Inventories at the end of period (million barrels)			
Inventories USA	1,113	1,087	1,097
Inventories OECD	2,649	2,587	2,614

* Forecast.
Source: Short Term Energy Outlook, November 2013.

Because of this scenario of a well supplied market, the price of WTI oil is expected to show lower levels than the ones estimated in our September Inflation Report. However, risk factors remain both on the upside and downside. The likelihood of price increases remains high due to the recurring political tensions observed in the Middle East and to the new infrastructure that will reduce the oversupply in Oklahoma oil storage facilities. At the same time, a quick return of Iran's production of crude oil to the market and a higher-than-estimated production of crude oil in the United States could push prices downwards.

Graph 93
WTI OIL: JANUARY 2007 - DECEMBER 2015
(US$/bl)

b. Imported food products

Maize

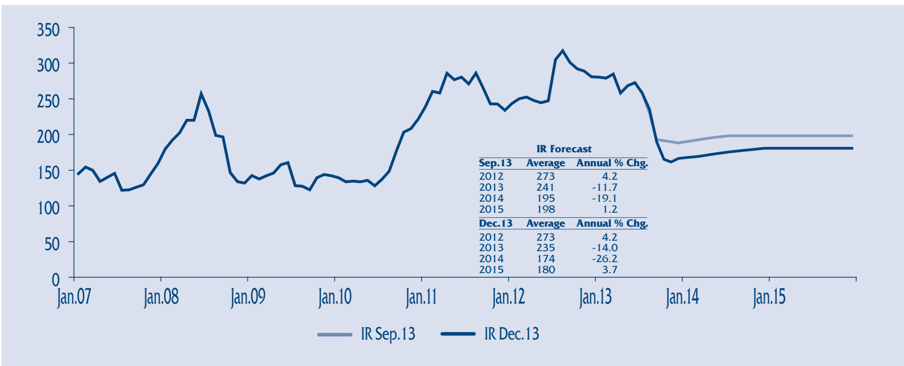
98. In the last three months, the average international price of **maize** dropped 32 percent, from US$ 235/metric ton in August to US$ 159/metric ton in November, and thus accumulated a decline of 43 percent so far this year.

The sharp decline in the price of maize was associated with a greater harvest of this crop in the United States, which would be reaching historic highs. This production of maize has relieved fears of a fairly tight market due to the inadequate harvest of the last farming season caused by the worst drought observed in over 50 years. Favorable climate conditions this year have resulted in better yields, which have reached the second highest level in history (surpassed only by the yield obtained in the 2009-2010 farming season). The world production of this grain would also reach a historical peak due to the strong increase obtained in the harvest of other producing countries –i.e. Russia, India, and other European countries– with yield rates that exceed the growth in demand.

Additionally, the price of maize was also pushed downwards by the possibility that the U.S. Government will lower the use of ethanol in 2014, which would reduce the demand for the grain. This decision is associated with the increase of crude oil production in the United States.

The excess supply in the 2013/2014 season will result in an increase in the global final inventories of maize and adds onto the unexpected increase in final inventories in the 2012/2013 season, which ended in August, and surprised the USDA which expected a drop in inventories. In these circumstances, in the forecast horizon the price of maize is expected to fall relative to the price foreseen in our September Inflation Report.

Graph 94
MAIZE: JANUARY 2007 - DECEMBER 2015
(US$/MT)



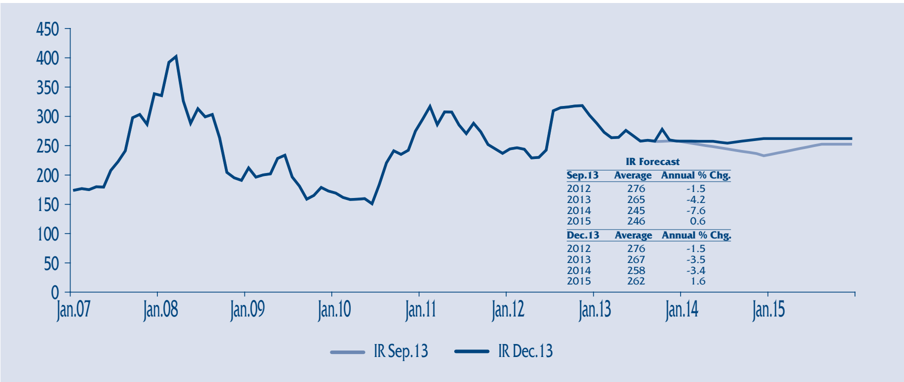
Wheat

99. At November the international price of **wheat** shows an accumulated decrease of 14.1 percent, having closed November with an average international price of US$ 259 per ton. During the last three months, however, the price of wheat has remained close to the average level recorded in August, although showing significant fluctuations.

    The price of wheat has been facing downward pressures due to the resumption of wheat cultivation in winter in Russia and in Ukraine after a period of heavy rains and due to higher inventories in the United States. An increase in the world production of wheat this season is anticipated due to better climate conditions this year.

    Together with a low growth in demand, this would boost the growth of inventories and keep prices low next year. In line with this, it is estimated that prices would fall slightly in the forecast horizon compared to the level estimated in our last report.

Graph 95
WHEAT: JANUARY 2007 - DECEMBER 2015
(US$/MT)



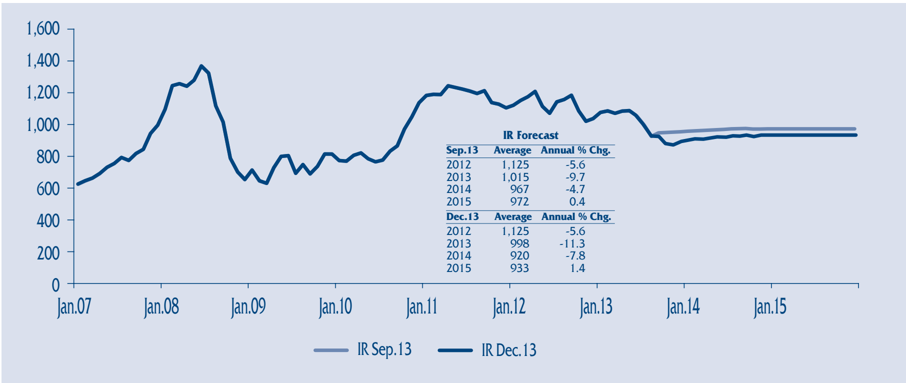
Soybean oil

100. The average price of **soybean oil** was US$ 873/ton in November, 6.4 percent lower than the average price in August and 15.8 percent lower than the price at December 2012.

     The price of soybean oil was affected by an increase in the world production of soybean which recorded a new all-time high, the better outlook for the production of soybean and soybean oil in South America standing out. The price is also being subject to pressures as a result of the proposal of the US Environmental Protection

Agency to reduce the target of biofuels by 16 percent in 2014. In line with these developments, it is estimated that the prices of soybean will remain below the prices considered in our previous report.

Graph 96
SOYBEAN: JANUARY 2007 - DECEMBER 2015
(US$/MT)



Expectations of inflation

101. Economic agents' expected levels of inflation in the forecast horizon continue to be within the target range.

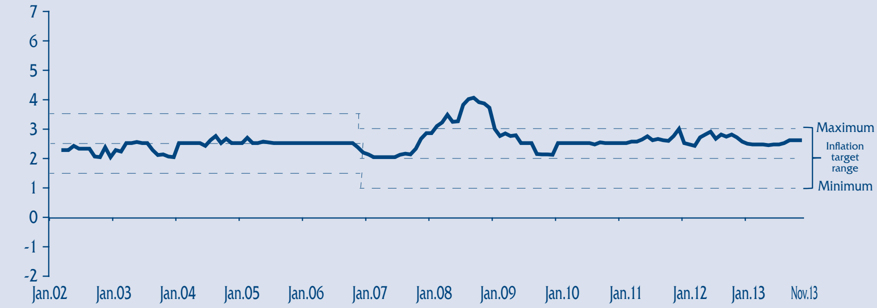
Table 53
SURVEY ON MACROECONOMIC EXPECTATIONS: INFLATION AT END OF PERIOD
(%)

	Expectations about:		
	IR Jun.13	IR Sep.13	IR Dec.13*
Financial entities			
2013	2.5	2.8	3.0
2014	2.5	2.5	2.6
2015	2.5	2.5	2.6
Economic analysts			
2013	2.5	2.7	3.0
2014	2.4	2.5	2.6
2015	2.3	2.4	2.5
Non-financial firms			
2013	2.7	3.0	3.0
2014	2.8	3.0	3.0
2015	2.8	3.0	3.0

* Survey conducted during November 30, 2013.
IR: Inflation Report.

According to the BCRP survey on macroeconomic expectations, inflation expectations for next year have also been stable in recent months and remain within the target range.

Graph 97
INFLATION EXPECTATIONS FOR THE NEXT YEAR*
(%)



* Corresponds to the average of the expectations of the financial system and economic analysts.

102. In November, inflation in the last 12 months returned to the inflation target range, in line with what was forecast in our previous report. In the central forecast scenario, inflation is expected to remain within the target range and to converge towards the middle point of 2.0 percent. No major inflationary pressures are foreseen in this scenario since economic growth is slowing down at rates below the economy's potential level of growth. This scenario also considers that inflation expectations will remained anchored within the target range.

Forecast on non-core inflation

103. **Non-core inflation** would record a rate of 1.5 percent in 2013 as a result of better climate conditions and a favorable evolution in the international prices of food products. In 2014 the energy components would continue to show higher price levels due to rises in the prices of LPG and electricity rates.

In 2014 the prices of food products are expected to continue showing downward corrections which, together with normal climate conditions, would result in a price increase of about 2 percent. With this increase, inflation would still continue to be within the inflation target range.

Table 54
INFLATION 2009 - 2014
(Last 12 month % change)

	Weight	2009	2010	2011	2012	2013*		
						November	IR Sep.13	IR Dec.13
CPI	**100.0**	**0.2**	**2.1**	**4.7**	**2.6**	**3.0**	**2.9**	**2.9**
Food and energy	**43.6**	**-0.9**	**3.0**	**7.7**	**3.6**	**3.0**	**3.3**	**3.0**
a. Food	37.8	0.6	2.4	8.0	4.1	2.8	2.8	2.5
b. Energy	5.7	-10.4	6.8	6.0	0.2	4.3	6.8	6.1
CPI without food and energy	**56.4**	**1.7**	**1.4**	**2.4**	**1.9**	**2.9**	**2.6**	**2.9**

IR: Inflation Report.
* Forecast.

The forecasts on the imported components of non-core inflation, such as fuels and food, show a slightly declining trend due to the favorable supply conditions foreseen and the still gradual sustainable recovery of the global economy.

Forecast on core inflation

104. On the other hand, the main factors affecting the path of **core inflation** are the output gap, imported inflation, and expectations of inflation.

The central scenario considers a recovery of economic activity which would grow to reach its potential level in the forecast horizon, which is equivalent to a neutral economic cycle. Therefore, no major demand pressures are expected on inflation in this period. Moreover, no major inflationary pressures associated with imported inflation are foreseen and inflation expectations are expected to remain anchored within the target range in the forecast horizon, as has been reflected in the survey on macroeconomic expectations.

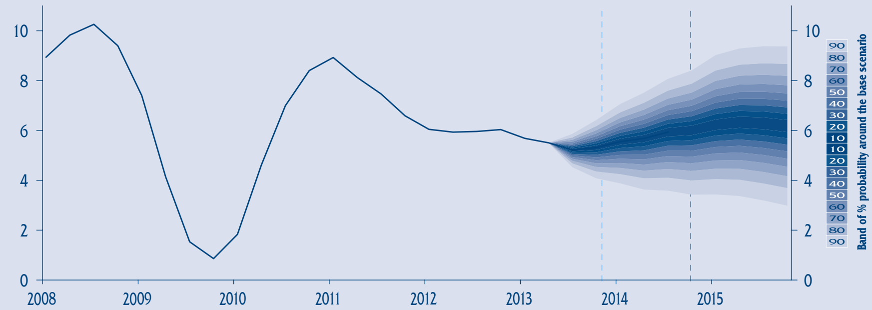
105. The central forecast scenario for 2013 considers that the **Peruvian economy would grow 5.1 percent**, registering a lower growth rate than the one forecast in our Report of September (5.5 percent). This downward revision is explained by the slowdown of private economic activity, together with a deterioration of terms of trade, partially offset by a more dynamic government spending. In 2014 and 2015 Peru's GDP is forecast to grow between 5.5 and 6.5 percentage points.

106. Every growth forecast is subject to the occurrence of unanticipated events that may divert it from its central scenario. In this context of uncertainty, the materialization of some risks could imply a different rate of growth of GDP than the one projected originally.

A scenario of domestic risks could include adverse demand shocks associated with obstacles that hinder private investment, which would have a negative effect on business confidence. Moreover, uncertainty about how the evolution of the global economy will contribute to deteriorate macroeconomic conditions remains high. Recent signs that point to a slowdown of growth in the emerging economies stand out together with uncertainty about the pace that the tapering of the Fed asset purchase program will have.

The balance of risks for GDP growth is biased on the downside. In other words, the probability that the growth of GDP will divert below the forecast in the baseline scenario is higher than the probability that it will divert above this forecast.

Graph 98
FORECAST OF GDP GROWTH 1/, 2013 - 2015
(Interanual % change)



Memo: The graph shows the probability of occurrence of GDP growth forecasts in the future, the values of which were established combining statistical analysis (using data as of October 2013) and the risk balance of the BCRP. Thus, in each period of the forecast horizon, each pair of bands with the same shade concentrates a probability of 10%. This can be interpreted as that 10 of every 100 possible future values of GDP growth are expected to fall within the darkest bands (located in the center), that contain the baseline scenario trajectory.
1/ GDP growth is defi ned as the percentage change of the moving average in four quarters compared to the same quarter of the previous year. Thus, the figure in Q4 coincides with the GDP growth rate in the year.

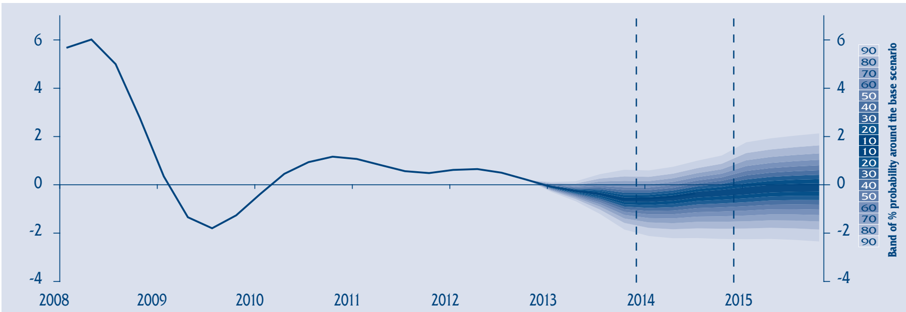
107. The **output gap** reflects cyclical fluctuations in economic activity that become inflationary pressures on the demand side. This gap is affected by various kinds of impulses: the external impulse, the fiscal impulse, the private impulse, and the monetary impulse.

On the external front, the external impulse is expected to be lower due to the decline registered in the terms of trade. Moreover, this forecast scenario also considers a positive fiscal impulse in 2014 which would in part offset the negative contribution of the external impulse on the output gap.

The baseline scenario also considers a gradual recovery in business confidence and consumer confidence, which would translate into a greater dynamism of the private impulse in the forecast horizon.

Finally, the baseline forecast scenario considers more flexible monetary conditions, especially in domestic currency due to the reduction of the policy reference rate in November 2013. A suitable monetary policy position contributes to maintain inflation expectations anchored, especially in the context of persistent significant shocks that affect sensitive products of the CPI basket. The Central Bank will continue to pay careful attention to developments in the world economy and in the domestic economy to adjust, if required, its monetary policy instruments to ensure that inflation remains within the target range.

Graph 99
OUTPUT GAP: 2008 - 2015
(% potential GDP)



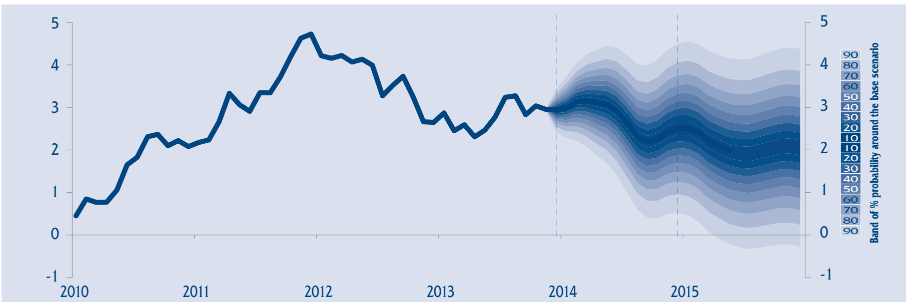
Memo: Output gap is not an observable variable and has to be estimated. Because of this, the graph shows uncertainty about its value, inclusive for periods with information of GDP (until third quarter of 2013). As in the case of the output gap, each pair of bands concentrate a probability of occurrence of 10% and total bands represent a probability of occurrence of 90%.
The risk scenario to the output gap forecast is in the chapter of balance of risk and are used for the inflation forecast (graph 100).

108. The evolution of the variables described above affect the path of inflation in the baseline scenario. However, due to uncertainty about future developments in the domestic economy and in the global economy, other scenarios that incorporate alternative projection assumptions in which inflation diverts from the path in the baseline scenario are also evaluated.

This is illustrated in Graph 100. The darker bands contain the path of inflation in the baseline scenario, which shows a probability of occurrence of about 70 percent. The alternative forecast scenarios, which are described in the section of Balance of Risks, have a total probability of occurrence of 30 percent.

Based on data available at November 2013, the probability that inflation will be within the target range in 2014 and 2015 is approximately 56 percent, while the probability that it will be below 3 percent is 68 percent.

Graph 100
INFLATION FORECAST: 2013-2015
(Last 12 months % change)



Memo: : The graph shows the probability of occurrence of inflation values in the future: These values were established combining statistical analysis and the balance of risk of BCRP. Thus, in each period of the forecast horizon, each pair of bands with the same shade concentrates a probability of 10%. This can be interpreted as that 10 of every 100 possible future values of inflation are expected to fall within the darkest bands (located in the center), that contain the baseline scenario trajectory.

VII. Balance of Risks

109 The forecast process is not free from uncertainty about future developments in the domestic and in the global economies. Therefore, in addition to the baseline scenario, other scenarios that include alternative forecast assumptions that, in the long run, divert inflation from the baseline scenario are also evaluated.

The balance of risks results from assessing the relative significance that each of the risk factors has on the inflation forecast. The expected impact of a risk factor on inflation depends on two components: first, the magnitude of deviation of the inflation forecast in the risk scenario compared to the baseline scenario, and second, the probability of occurrence assigned to each risk scenario. Together, these two factors determine the bias of the balance of risks in the inflation forecast.

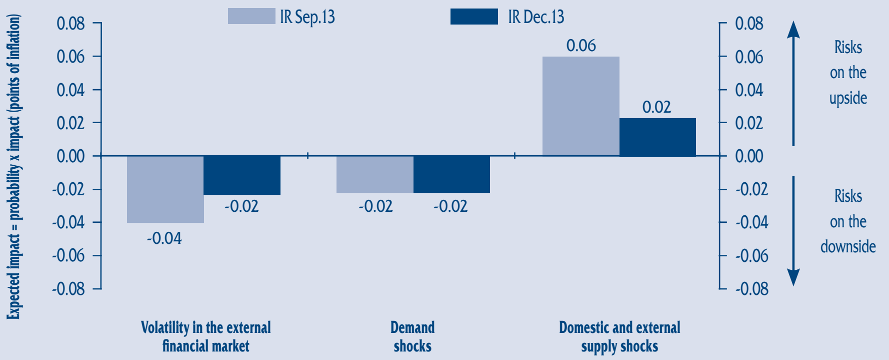
110. As in our Report of September, the main risks that could divert the rate of inflation from the baseline scenario in the forecast horizon are associated with uncertainty about the evolution of the global economy, the impact of lower terms of trade, and the slowdown of domestic demand. However, in contrast with our previous report, the balance of these risks is today biased on the downside. Graph 98 illustrates the expected impact of each of these risk factors on the inflation forecast in a 2-year horizon.

The **downward risks** in the inflation forecast are, on the one hand, external factors associated with the possibility that volatility may return to international financial markets and with a slower pace of growth in many economies, and, on the other hand, internal factors associated with a slower pace of recovery in domestic demand due to the postponement of some investment projects.

On the other hand, the **upward risk** for inflation is associated mainly with the increase in fuel prices due to geopolitical factors, although this risk has declined significantly compared to the situation in our previous report.

The **balance of these risks results in a negative bias** in the inflation forecast; therefore, the probability that inflation is lower than the projected rate of around 2 percent in the 2014 - 2015 horizon is greater than the probability of it being higher than this rate.

Graph 101
BALANCE OF RISKS ACCORDING TO THE BASELINE



Memo: The risk assessment describes how exogenous factors would affect the rate of inflation forecast for 2 years ahead if such risks materialized. Each bar in the graph illustrates the magnitude and direction of the effect of these factors, i.e., the expected impact in alternative forecast scenarios. This impact is calculated as the difference between the inflation forecast in the baseline scenario and inflation projections in several scenarios considering different assumptions, multiplying this difference by the probability of occurrence assigned to such alternative assumptions. The sum of the bars –the risk balance– indicates how these risk factors as a whole would divert inflation from the baseline scenario in the medium term.
The balance of these risks shows a downward bias for the projection of inflation: The probability that inflation will be below the forecast considered in the baseline scenario is greater than the probability that infl ation will be above the forecast level.

Conclusion

111. The faster pace observed recently in the rate of inflation was associated with transitory factors whose influence is expected to disappear in the short run. Thus, inflation is expected to converge to the target range. The balance of risks is on the downside.

GDP would continue to grow at rates not too distant from the economy's potential level of growth, with a dynamic evolution in domestic demand and with a recovery of exports in the next years.

The Central Bank will continue to pay careful attention to developments in the world economy and in the domestic economy, as well as in expectations of inflation and stands ready to adjust, if it is necessary, its monetary stance to ensure that inflation remains within the target range.