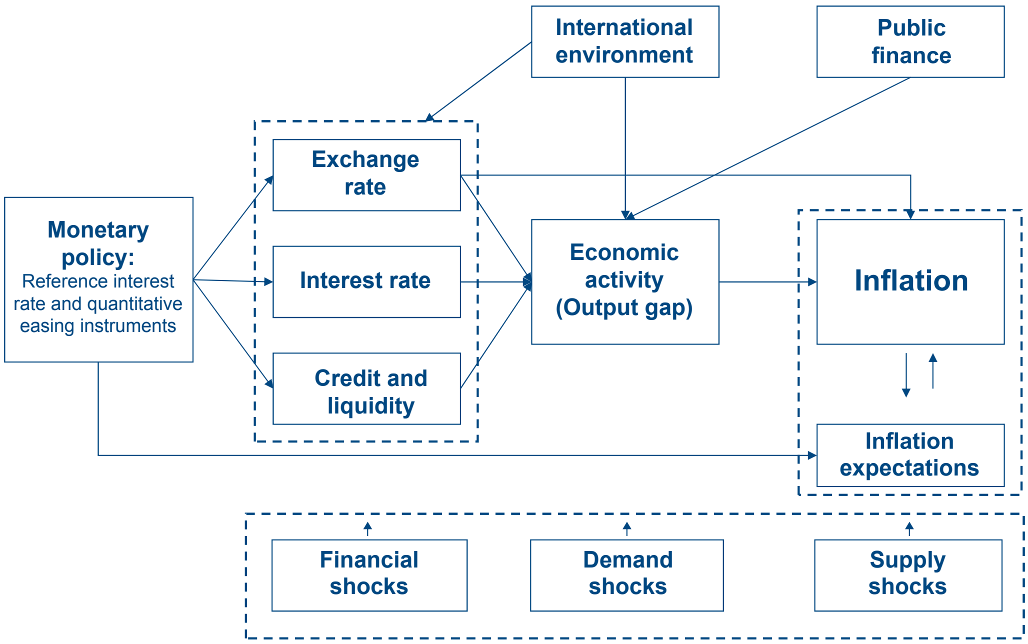
INFLATION REPORT:

Recent trends and macroeconomic forecasts 2013-2014

March 2013



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INFLATION REPORT
Recent trends and macroeconomic forecasts

CENTRAL RESERVE BANK OF PERU

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BOXES

This ***Inflation Report*** was drawn up using data on the balance of payments as of Q4-2012, data on the gross domestic product as of January 2013, and data on the operations of the non-financial public sector, monetary accounts, inflation, financial markets, and the foreign exchange rate as of February 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, 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 as well as preventing the excessive growth of credit.

- 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 BCRP will publish its next Inflation Report in June 2013.

Summary

i. The international environment between December and February continued to be favored by the measures adopted by the central banks of developed economies as well as by evidence of stability in the emerging economies. However, since the end of February, some events such as the political situation in Italy and the absence of an agreement to raise the limit on the public debt of the United States have increased again global uncertainty, affecting consumers and investors' confidence. In response, most of the central banks in the major developed economies have reiterated their commitment to maintain low interest rates and monetary expansion programs.

   In this context, the forecasts on global growth in 2013 remain unchanged. The world economy is estimated to grow 3.2 percent in 2013 and 3.8 percent in 2014, showing in 2014 a similar growth rate to the one registered before the financial crisis.

ii. The growth of Peru's economy has stabilized around its long-term sustainable level. In 2012, the Peruvian economy grew 6.3 percent as a result of a greater dynamism of domestic demand, particularly of private and public investment. The central forecast scenario for 2013 and 2014 considers GDP growth rates at stable levels close to the economy's potential level, with the momentum of demand factors prevailing in an environment in which uncertainty about the international context persists.

iii. In 2012 the current account of the balance of payments recorded a deficit of 3.6 percent of GDP (US$ 7.1 billion) –higher than the one registered in 2011 (1.9 percent of GDP)– as a result of the deterioration of the terms of trade, the slower growth observed in the volume of exports, and the high growth of imports in a context of a higher rate of expansion of domestic demand. However, external funding widely exceeded the requirements of the current account deficit due to a significant inflow of long-term private capital which amounted to US$ 16.3 billion.

   The current account deficit of 3.7 percent of GDP estimated for 2013 in our previous report is revised to 4.0 percent of GDP in this report, in line with the upward revision of the estimated growth of domestic demand. This increased deficit considers the lower trade surplus expected for the year due mainly to lower exports of gold and non-traditional products, offset in part by lower outflows for factor income as a result of the lower profits expected in the mining sector. The current account deficit would show a downward path and register a rate of 3.9 percent of GDP in 2014 due to the onset of major projects.

iv. In 2012 the non-financial public sector showed an economic surplus of 2.1 percent of GDP, slightly higher than the surplus of 1.9 percent recorded in 2011. This increase is mainly explained by the increase in the general government current revenue, which was partially offset by the real growth of the general government non-financial expenditure (8.0 percent), associated with increased spending in gross capital formation.

The economic balance for 2013 and 2014 has been revised slightly downwards from 1.1 percent of GDP (December Report) to 1.0 percent of GDP since lower revenues are foreseen due to the lower-than-expected regularization of the income tax and higher current expenditure of the general government is estimated in line with higher salary rises in the public sector as well as with increased staff engagement, as approved in the 2013 budget.

v. As expected, the rate of inflation in the last twelve months continued to decline and fell from 2.65 percent in December 2012 to 2.45 percent in February 2013, remaining within the target range reflecting the reversal of the supply factors that affected food prices since mid-2012.

vi. In this context, the Board of Directors of the Central Bank decided to maintain the monetary policy reference rate at 4.25 percent, the rate level registered since May 2011. In this period, the monetary policy communiqués of BCRP highlighted that these decisions were made taking into account the partial reversal of shocks on the side of supply, a growth of the economy close to its potential level of economic growth, and a still highly uncertain external environment.

vii. The central forecast scenario considers that inflation will remain within the target range and that it will gradually converge to 2.0 percent in the following months. This scenario also considers that there would be no major inflationary pressures associated with increases in the prices of commodities and that inflation expectations would remain within the target range. Inflation in 2012 and 2013 is forecast to be within a range of 1.5 and 2.5 percent.

viii. The balance of risks is **neutral** for the inflation rate projected at end 2014. The information available to date indicates that there's the same probability that inflation will fall below or above the baseline scenario forecast.

INFLATION FORECAST 2013 - 2014
(12 month % change)

ix. The **downward risk** scenarios in the inflation forecast are external factors associated with the potential unfolding of an international financial crisis.

a. Uncertainty about the world economy.

Even though a growth rate of global economic activity similar to the one forecast in our December Inflation Report is considered in the baseline scenario, this estimate could be conservative given growing uncertainty in international markets due to the lack of agreement on fiscal policy in the United States, to the worsening of the debt problem in the Eurozone, and to the economic deceleration observed in some emerging economies. A deepening of these risk conditions would bring about a lower global growth and a weakening in external demand, which would affect the Peruvian economy through financial and trade channels

A drop in global economic activity coupled by a reduction in the terms of trade would take place in this adverse international scenario. In addition, the increase of global uncertainty could generate panic among investors and trigger a sudden stop –a sudden capital reversal– with a real depreciation and an increase in the country risk. In this context, international interest rates are expected to remain low for a longer period of time than the one considered in the baseline scenario.

Should these risks occur and materialize, the Central Bank would use the significant amount of the international reserves it has available as well as various liquidity injection mechanisms, both in national currency and in foreign currency, to offset the impact of this shock on domestic financial conditions. Should it be required, the Central Bank would respond by easing monetary conditions.

It should be pointed out that the expected impact of this hypothetical scenario of international economic downturn is the same as that considered in our December Inflation Report. This revision considers recent information indicating a more moderate growth in the United States and signs of a recovery of growth in China. Notwithstanding, the negative impact of this scenario is still latent as long as the persistence of the problems in the Eurozone continue affecting uncertainty and market volatility.

x. On the other hand, there are scenarios of **upward risk** for inflation associated mainly with an increase in capital inflows and a rise in commodity prices.

b. Increased capital inflows.

The high availability of liquidity in international markets due to the aggressive expansion of the balance sheets of central banks in developed countries, on the one hand, together with few attractive investment options in a context of high global uncertainty, on the other hand, could attract foreign capital inflows to emerging economies such as the Peruvian economy. A greater capital inflow would accelerate the expansion of credit, stimulating aggregate demand and inflation, on the one hand, but on the other hand, this would generate appreciatory pressures on the exchange rate, which would translate into lower domestic inflation.

In this scenario, the Central Bank would adjust its monetary position and its macro prudential policy instruments, such as the rates of reserve requirements. This scenario of higher capital inflows has a similar expected impact to that considered in our December Inflation Report.

c. Imported inflation and adverse climate conditions.

Like in the December Inflation Report, the risk of higher international prices of oil crude and oil derivatives is also considered in this report due to market fears regarding a deepening of international geopolitical tensions. Should this risk occur, global inflationary pressures would be more persistent than what they are currently expected to be.

The risk of weather conditions that could affect the normal development of the production and supply of food products remains in the domestic arena.

In this scenario, the Central Bank would adjust its monetary position only if these supply shocks were to "contaminate" or affect economic agents' expectations of inflation. It should be pointed out, however, that the impact of this scenario of internal and external shocks is lower than the impact considered in our December Inflation Report, which reflects the reversal of supply shocks observed recently.

SUMMARY OF INFLATION REPORT FORECASTS

	2011	2012	2013 1/		2014 1/	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
Real % change						
1. GDP	6.9	6.3	6.0 - 6.4	6.0 - 6.5	6.0 - 6.5	6.0 - 6.5
2. Domestic demand	7.2	7.4	6.3	6.8	6.3	6.6
a. Private consumption	6.4	5.8	5.7	5.7	5.7	5.7
b. Public consumption	4.8	10.6	7.6	10.1	6.2	6.6
c. Fixed private investment	11.7	13.6	8.2	8.8	8.2	8.2
d. Public investment	-17.8	20.9	15.2	15.0	11.7	11.4
3. Exports (goods and services)	8.8	4.8	7.7	5.1	9.1	7.9
4. Imports (goods and services)	9.8	10.4	7.5	7.8	8.9	8.9
5. Economic growth in main trading partners	3.6	2.7	2.7	2.7	3.3	3.3
Memo:						
Output gap 2/ (%)	0.8	0.5	-0.5 ; +0.5	-0.5 ; +0.5	-0.5 ; +0.5	-0.5 ; +0.5
% change						
6. Forecast inflation	4.7	2.6	1.5-2.5	1.5-2.5	1.5-2.5	1.5-2.5
7. Average price of crude oil	19.8	-0.9	-4.6	-1.7	0.0	-0.5
8. Nominal exchange rate 3/	-4.2	-4.8	-1.0	-2.0	-1.0	-1.3
9. Real multilateral exchange rate 3/	-5.8	-7.3	-1.0	-3.3	-0.5	-1.1
10. Terms of trade	5.4	-4.9	-0.5	0.3	1.0	0.0
a. Export price index	20.0	-3.3	-1.9	-1.0	1.9	0.7
b. Import price index	13.8	1.7	-1.5	-1.3	0.9	0.7
Nominal % change						
11. Currency in circulation	12.9	18.3	13.4	15.5	13.2	13.2
12. Credit to the private sector 4/	19.6	15.1	14.5	14.5	13.0	12.0
% GDP						
13. Gross fixed investment	24.1	26.7	27.5	27.5	28.1	28.2
14. Current account of the balance of payments	-1.9	-3.6	-3.7	-4.0	-3.4	-3.9
15. Trade balance	5.3	2.3	1.8	1.3	2.3	1.2
16. Gross external financing to the private sector 5/	6.9	9.5	6.2	8.1	5.6	5.9
17. Current revenue of the general government	21.0	21.6	21.7	21.6	21.7	21.6
18. Non-financial expenditure of the general government	18.1	18.7	19.5	19.6	19.6	19.7
19. Overall balance of the non-financial public sector	1.9	2.1	1.1	1.0	1.1	1.0
20. Total public debt balance	21.2	19.8	18.6	18.2	17.2	17.2

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.

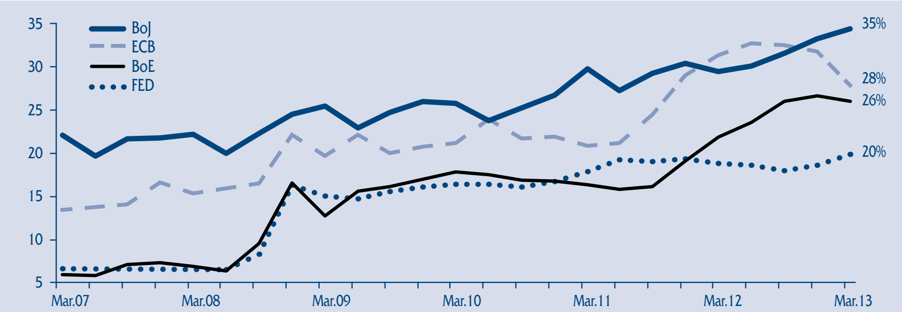
I. International Environment

1. From December, when our last Inflation Report was published, until February, the international environment continued to be favored by the measures adopted by the central banks of developed economies as well as by evidence of some stability in the emerging economies. However, since the end of February, some events have increased again global uncertainty, affecting consumers and investors' confidence.

   Two events stand out among these factors: the political situation in Italy and the banking crisis in Cyprus, both of which could affect funding conditions for other Eurozone economies with debt problems. Another factor worth pointing out is the lack of definition in the U.S. Congress regarding automatic spending cuts and the lack of agreement to raise the debt limit.

   Most of the central banks of the major developed economies have reiterated their commitment to maintaining low interest rates and their monetary expansion programs. In the particular case of the United States (USA), the FED announced that it would maintain its stimulus policies as long as the rate of unemployment is over 6.5 percent and inflation expectations remain anchored and the Bank of Japan made explicit a 2 percent inflation target. However, a reaction of international capital flows and markets is expected anticipating the reversal of the expansionary monetary policies.

Graph 1
CENTRAL BANKS: TOTAL ASSETS
(% of GDP)



Source: Bloomberg.

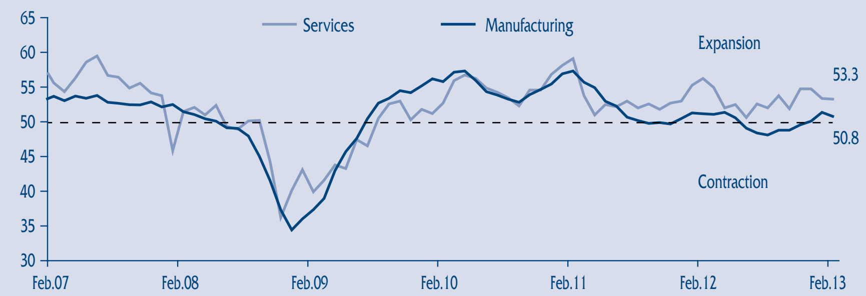
   In this context, the projections on world growth in 2013 remain unchanged, but the risks are still present. It is estimated that the world economy would grow 3.2 percent in 2013 and 3.8 percent in 2014.

This greater uncertainty has affected the price of the major commodities which corrected downwards towards the end of February. The spreads in most emerging economies showed an upward correction in line with greater risk aversion. In contrast, stock markets have had so far this year a positive evolution due to the portfolio restructuring from fixed-income to variable-income securities.

Global growth

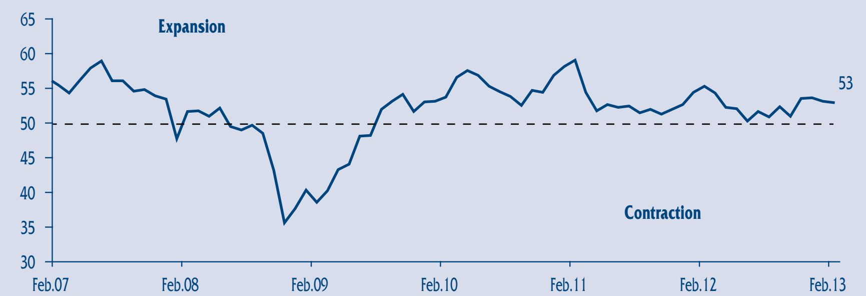
2. In 2012 the world economy recorded a growth rate of 3.1 percent, lower than that observed in the previous year (3.9 percent). In the months of January and February of this year, global activity has shown a tendency to stabilize. The global indicator of activity recorded a positive trend: while activity in the sector of services remained almost unchanged, the indicator of manufacturing declined slightly, but remained within the expansion area.

Graph 2
JP MORGAN GLOBAL PMI MANUFACTURING AND SERVICES
(January 2007- February 2013)



Source: Bloomberg.

Graph 3
GLOBAL INDICATOR OF ACTIVITY (JP MORGAN)
(January 2007- February 2013)



Source: Bloomberg.

However, this behavior is not uniform at the country level. In line with other indicators, a moderate recovery is being observed in the United States, an almost generalized contraction in seen in the Eurozone, and a stabilization of growth is observed in the emerging economies.

3. The growth forecast for 2013 remains at 3.2 percent. The emerging economies would grow 5.3 percent while developed economies would grow 1.3 percent. China stands out among the former with a growth rate of 8 percent, while in the case of the latter the low rate of growth is explained by the developments in the Eurozone, where the expectation of a contraction has increased this year.

Table 1
WORLD GDP GROWTH
(Annual % change)

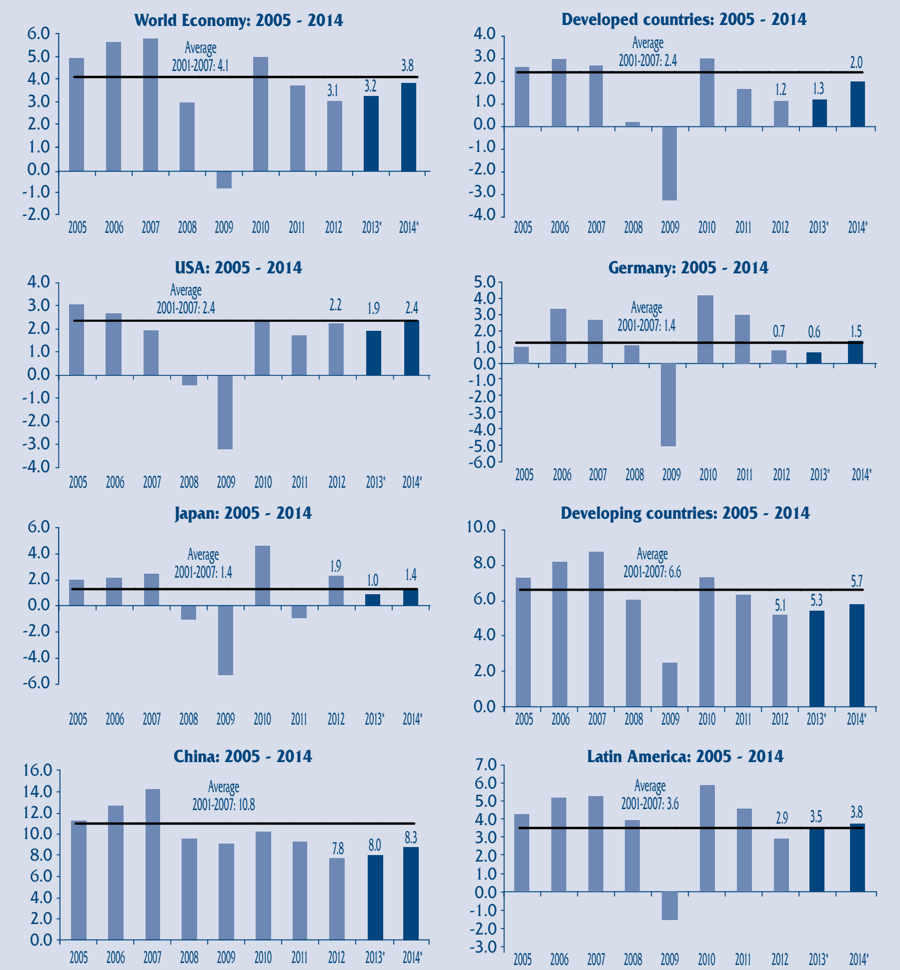
	PPP weighted	Executed		2013 *		2014 *	
	2011	2011	2012	IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
Developed countries	**51.1**	**1.6**	**1.2**	**1.2**	**1.3**	**2.0**	**2.0**
Of which							
1. United States	19.1	1.8	2.2	1.9	1.9	2.4	2.4
2. Eurozone	14.3	1.4	-0.6	-0.1	-0.3	1.2	1.1
Germany	3.9	3.0	0.7	0.7	0.6	1.5	1.5
France	2.8	1.7	0.0	0.0	-0.2	1.0	1.0
Italy	2.3	0.4	-2.4	-0.6	-1.0	0.5	0.5
Spain	1.8	0.4	-1.4	-1.5	-1.5	0.8	0.4
3. Japan	5.6	-0.7	1.9	0.2	1.0	1.4	1.4
4. United Kingdom	2.9	0.7	0.2	1.1	1.1	1.5	1.5
Developing countries	**48.9**	**6.3**	**5.1**	**5.4**	**5.3**	**5.7**	**5.7**
Of which							
1. Developing Asia	25.0	8.0	6.8	7.1	7.0	7.5	7.4
China	14.3	9.3	7.8	8.0	8.0	8.5	8.3
India	5.6	7.9	5.3	6.6	6.3	7.0	6.9
2. Central and Eastern Europe	3.5	5.3	1.6	2.5	2.3	2.9	3.1
3. Latin America and the Caribbean	8.7	4.5	2.9	3.7	3.5	3.9	3.8
Brazil	2.9	2.7	0.9	3.8	3.2	4.0	3.8
World Economy	**100.0**	**3.9**	**3.1**	**3.2**	**3.2**	**3.8**	**3.8**
Memo:							
Peru's trading partners 1/		3.6	2.7	2.7	2.7	3.3	3.3
BRICs 2/		7.7	6.0	6.7	6.6	7.1	7.0

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

This central forecast may be affected by various risks, most of which have been discussed in our previous Inflation Report. In the Eurozone, the risks on the downside are associated with the recent events in Cyprus and with the political situation in Italy which could hinder the implementation of fiscal measures and affect other peripheral economies (particularly Spain). In the U.S., the lack of agreement on fiscal measures could continue for a longer period of time with the consequent risk that the disorderly adjustment will continue and may start affecting consumer confidence.

On the other hand, there is the possibility that Japan will grow at higher rates than those considered in the central scenario as a result of the implementation of monetary and fiscal stimulus.

Graph 4
GDP GROWTH

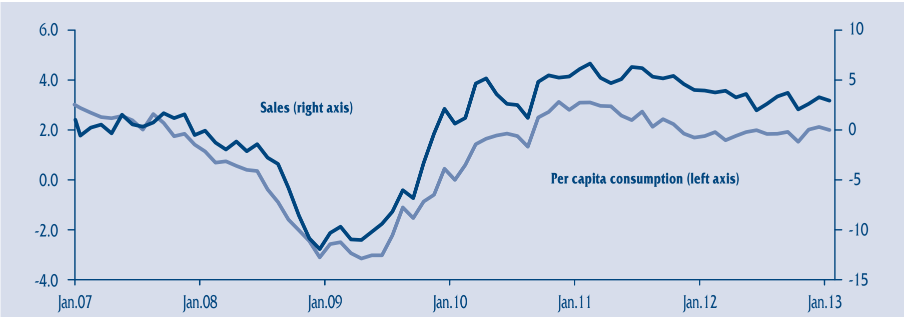


* Forecast.
Source: BCRP.

4. In the **United States** growth registered a rate of 0.1 percent in Q4-2012 (annual quarterly rate), showing a moderate growth in consumption and an increased rate in fixed investment and net exports. This evolution was partially offset by a drop in the costs of defense and a reduction in business inventories. Thus, in 2012 the U.S. economy grew 2.2 percent.

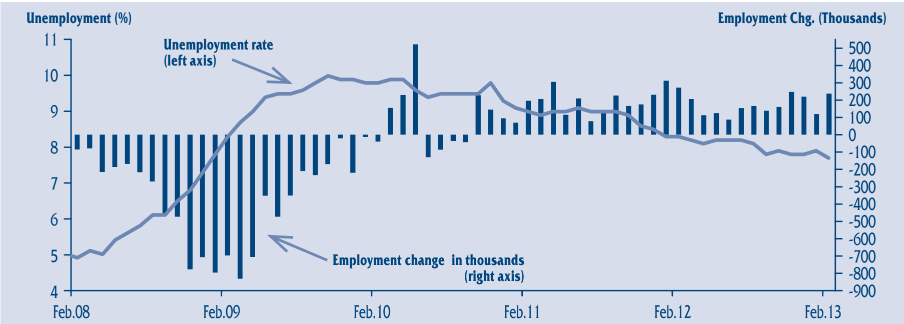
The indicators in the first months of the year show an improvement of consumption in Q1-2013, despite the lower available income given the increase in the income tax effective since January 2013 and the recent rise in the prices of gasoline registered in February. However, the slight acceleration of new jobs in recent months, the reduction of unemployment to 7.7 percent in February, and the downward trend in applications for unemployment benefits observed in the last months point to a recent improvement in the labor market.

Graph 5
REAL PER CAPITA CONSUMPTION AND RETAIL SALES IN REAL TERMS
(12 months % change)



Source: Bloomberg.

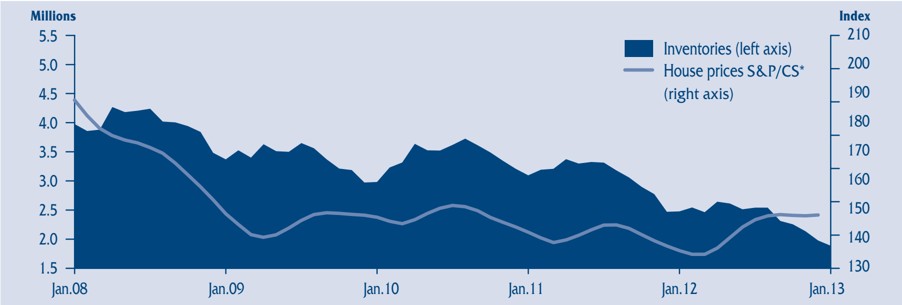
Graph 6
USA: EMPLOYMENT AND UNEMPLOYMENT RATE



Source: Bloomberg.

Residential investment continues to improve in a context of rising housing prices as a result of pressures generated by the drop in the level of inventories of homes for sale available which has reached historic lows. Construction indicators point to a drop in activity at the beginning of the year due to weather-related factors, but the increase in construction permits indicates a recovery in the sector.

Graph 7
USA: HOUSE PRICES (S&P/CS) AND INVENTORIES



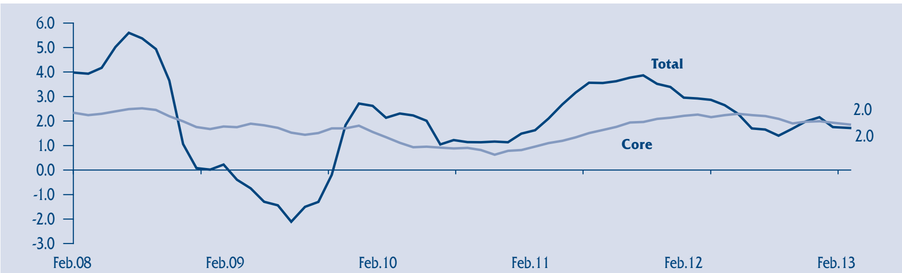
Source: Bloomberg. * S&P/CS: S&P/Case-Shiller Home Price Indices.

Graph 8
USA: RESIDENTIAL CONSTRUCTION

Source: Bloomberg.

In this context of moderate recovery, in its March policy meeting the FED announced that it would continue with its asset-purchase program –US$ 85 billion per month– and that it would keep rates low as long as the unemployment rate is above 6.5 percent, expected inflation 2-years ahead is below 2 percent with a margin of 0.5 percent, and inflation expectations are controlled. Inflation at end 2012 recorded a rate of 1.7 percent, while core inflation recorded a rate of 1.9 percent.

Graph 9
USA: CPI
(12 month % change)



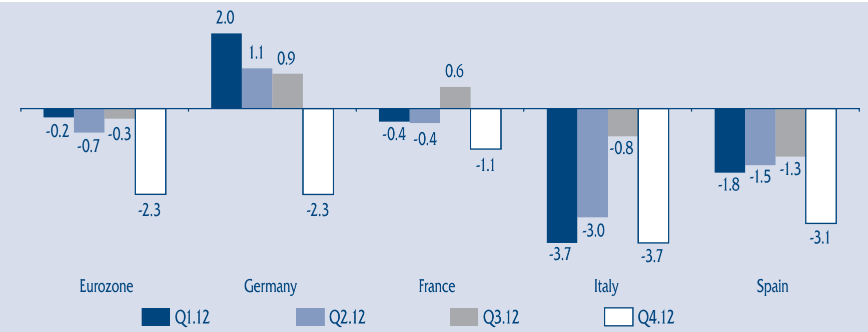
Source: Bloomberg.

In line with the data of Q4-2012 and consumption indicators, the forecast on growth in the United States in 2013 is maintained at 1.9 percent. As in our previous Inflation Report, one of the factors considered to be a downside risk in this forecast is the lack of agreement on fiscal policy, which is already having an impact on consumers and investors' confidence.

Several fiscal policy issues still require to be solved today. On the one hand, a new debt limit has to be approved given that the current limit was suspended until May 18 and, on the other hand, an agreement has to be reached to stop the automatic expenditure cuts initiated on March 1, 2013 (approximately 50 percent of these cuts, which would amount to US$ 85 billion in this fiscal year, would be cuts in defense and another 12 percent would be cuts in Medicare). It is estimated that the impact of such adjustment this year would be between 0.3 and 0.5 percentage points of GDP.

5. After showing some signs of economic stabilization, in Q4 the **Eurozone** recorded a contraction of 2.3 percent, the largest contraction since Q1-2009 (-10.7 percent). In terms of spending, the region's contraction is explained by the fall of private fixed investment, private consumption, and government spending. With this, the variation in the GDP growth rate in 2012 was -0.6 percent (1.4 percent in 2011).

Graph 10
EUROZONE: QUARTERLY GROWTH
(Seasonally adjusted annualized quarterly rates)



Source: Bloomberg.

The indicators published between December and January show some improvement since Q1. However, the indicators of February –the PMI indices of manufacturing and services– and the deterioration of corporate confidence after the results of the elections in Italy show that the risks of a recession persist. By countries, France, Spain, and Italy register the worst levels of activity, while Germany continues to show the least deterioration due to its greater commercial link to economies outside the Eurozone and due to the better credit conditions observed since November.

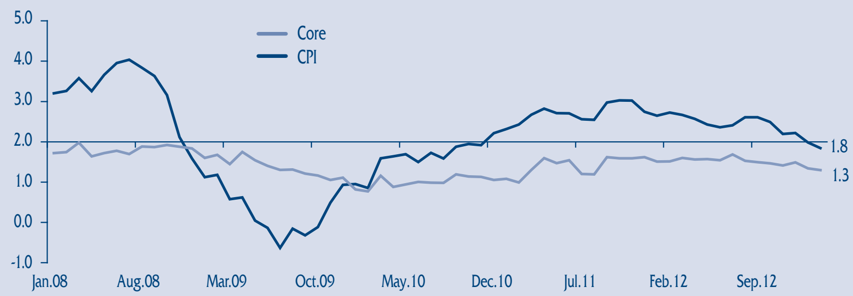
Table 2
PURCHASING MANAGERS INDEX

Eurozone	Dec.10	Dec.11	Mar.12	Jun	Sep	Oct	Nov	Dec	Jan.13	Feb
Composite	**55.5**	**48.3**	**49.1**	**46.4**	**46.1**	**45.7**	**46.5**	**47.2**	**48.6**	**47.9**
Services	**54.2**	**48.8**	**49.2**	**47.1**	**46.1**	**46.0**	**46.7**	**47.8**	**48.6**	**47.9**
Germany	59.2	52.4	52.1	49.9	49.7	48.4	49.7	52.0	55.7	54.7
France	54.9	50.3	50.1	47.9	45.0	44.6	45.8	45.2	43.6	43.7
Italy	50.2	44.5	44.3	43.1	44.5	46.0	44.6	45.6	43.9	43.6
Manufacturing	**57.1**	**46.9**	**47.7**	**45.1**	**46.1**	**45.4**	**46.2**	**46.1**	**47.9**	**47.9**
Germany	60.7	48.4	48.4	45.0	47.4	46.0	46.8	46.0	49.8	50.3
France	57.2	48.9	46.7	45.2	42.7	43.7	44.5	44.6	42.9	43.9
Italy	54.7	44.3	47.9	44.6	45.7	45.5	45.1	46.7	47.8	45.8

Source: Bloomberg.

In this context, the President of the European Central Bank (ECB), Mario Draghi, ruled out an immediate withdrawal of stimulus given the climate of increased political uncertainty due to the election results in Italy and to lower inflationary pressures (1.8 percent in February). In March, the ECB maintained its rate at 0.75 percent. However, the markets estimate a rate reduction of 25 basis points in the ECB upcoming meetings.

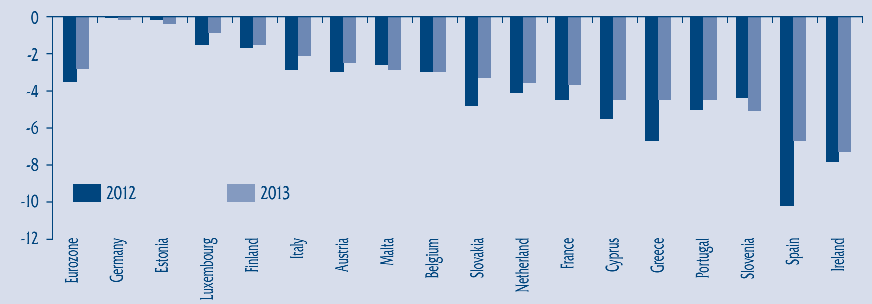
Graph 11
EUROZONE: CPI (12 MONTHS % CHANGE)
(January 2008 - February 2013)



Source: Bloomberg.

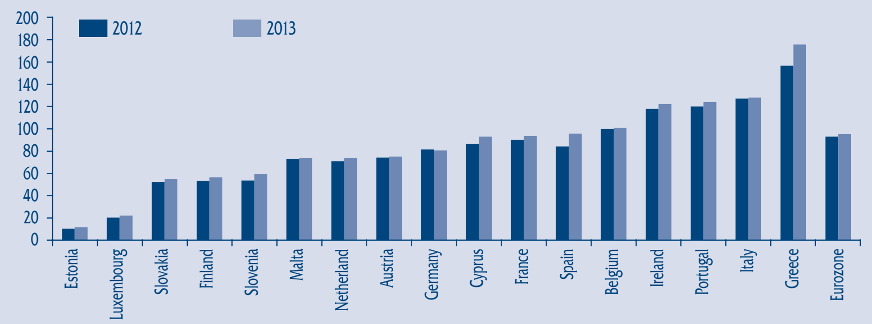
The central forecast scenario estimates that production in the Eurozone will decline 0.3 percent this year and that the economies with fiscal problems will register a contraction of over one percent. This group of economies would be affected by the magnitude of the fiscal adjustment needed to reduce the levels of fiscal deficit to rates below 3 percent in a period of 2 to 4 years. Despite the significant expenditure adjustments implemented by the authorities, the debt and deficit levels still persist.

Graph 12
FISCAL DEFICIT
(% of GDP)



Source: European Commission projections 2012-2013 (February 2013). Some countries have released data for 2012.

Graph 13
PUBLIC DEBT
(% of GDP)



Source: European Commission projections 2012-2013 (February 2013). Some countries have released data for 2012.

The Eurozone's delicate position has worsened due to events associated with the sovereign and banking bailout program for Cyprus. At the Eurogroup meeting of March 15, the European leaders agreed to provide funds for a total of €10 billion for the bailout deal, with funding for €7 billion remaining to be obtained. The proposal to finance this gap included a tax on the country's bank deposits, but the measure was rejected by the Cyprus Parliament. Thus, uncertainty about how to finance the rescue program without increasing the public debt remains (the public debt of Cyprus is currently close to 90 percent of its GDP).

6. After declining for two consecutive quarters, the economy in **Japan** recovered in Q4 recording a growth rate of 0.2 percent (annualized quarterly rate). Consumption grew 2.0 percent while residential construction grew 14.9 percent, driven by an improvement in demand for homes in anticipation of the sales tax increase that will be implemented in April 2014. The growth in construction was also influenced by the increase in public expenditure associated with the reconstruction of the

areas that were affected by the earthquake. This dynamism was offset by a drop in business investment of 5.7 percent and in net exports, with imports falling 9 percent and exports falling 14 percent. The latter is explained by the appreciation of the yen in Q2 and Q3 and by lower growth in Japan's trading partners.

The Japanese economy would grow 1 percent in 2013. Our previous estimate has been revised upwards due to the recent weakening of the currency and to the announcements of expansionary policies made by the new administration. Recent indicators of retail sales and consumers and investors' confidence are showing a better evolution than expected.

7. Within the **emerging economies**, **China** stands out with a growth rate of 7.8 percent in 2012. Although activity in this country slowed down during most of the year due to the exhaustion of the massive macroeconomic stimulus package implemented after the international financial crisis and due to the deterioration of international trade, the economy showed a gradual recovery in Q4-2012 associated in part with government spending in infrastructure as a result of the infrastructure program initiated by the government in 2012.

In this line, the purchasing managers index (PMI) has remained above 50 points in the first months of 2013 and new bank loans have seen a considerable increase after being stagnated for several months. Trade indicators have been recovering, which suggests an improvement in the international context and an increase in private investment. The Central Bank announced a prudent monetary policy after inflation rose to 3.2 percent in February.

Table 3
CHINA'S ECONOMIC INDICATORS

	2011	2012				2013
	Dec	Mar	Jun	Sep	Dec	Feb
Manufacturing PMI index (50: neutral level)	50,3	53,1	50,2	49,8	50,6	50,1
Industrial Production (12 month % change)	12,8%	11,9%	9,5%	9,2%	10,3%	9,9%
Investment in fixed assets (Annual % change)	23,8%	20,9%	20,4%	20,5%	20,6%	21,2%
Retail sales (12 month % change)	18,1%	15,2%	13,7%	14,2%	15,2%	12,3%
Exports(12 month % change)	13,4%	8,9%	11,3%	9,9%	14,1%	21,8%
Imports (12 month % change)	11,8%	5,3%	6,3%	2,4%	6,0%	-15,2%
New loans (Billions of yuan)	641	1,010	920	623	454	620
CPI (12 month % change)	4,1%	3,6%	2,2%	1,9%	2,5%	3,2%

* Jan-Feb.
Source: Bloomberg.

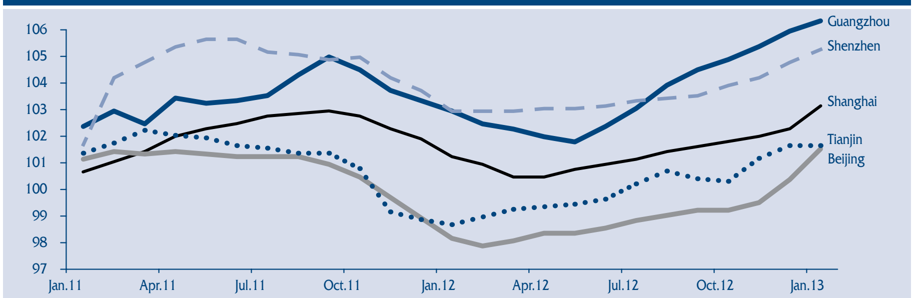
In this context, China is expected to grow 8.0 percent in 2013 and 8.3 percent in 2014. The authorities have reiterated their intention to rebalance the economy in favor of consumption, to liberalize interest rates to improve the allocation of resources, and to gradually open the capital market in the medium term, emphasizing particularly the role that the urbanization process will have in the following years.

Box 1

CHINA: MEASURES IN THE REAL ESTATE MARKET

Over the past few years the Chinese government has implemented measures to prevent the potential formation of a bubble in the real estate market. The measures implemented, which included increasing cash payments and mortgage restrictions, were initially effective in offsetting the rise of property prices. However, an upsurge of real estate prices has been observed in the major cities of China since the first half of 2012.

CHINA: REAL STATE
(Price index)



Source: NDRC.

In this line, on Friday March 1, the government reinforced these measures to control the price rises in this market. The Central Bank branch offices in cities with a real estate overheating must raise cash payment requirements (currently at 60 percent) and the interest rates on purchases of a second property. In addition to this, a 20 percent tax on capital gains has been activated (this tax existed, but was not effective until now).

There is the possibility that the government will complement this sector measures with monetary policy measures, such as raising interest rates or increasing the rate of reserve requirements, if the pressures in the real estate market are coupled by a rise in inflation.

8. On the other hand, **India** grew 5.3 percent in 2012, less than initially estimated. The decline in external demand was aggravated by a slowdown in consumption and a deterioration of the business climate in a context of domestic uncertainty associated with persistent inflationary pressures, with a depreciation of the rupee, and with political disputes over the fiscal consolidation (it is estimated that the deficit in the consolidated public sector amounted to 8.6 percent of GDP in 2012). In 2013 India would grow 6.3 percent. This growth would be supported by a recovery in consumer confidence as well as by a gradual improvement in the pace of growth of this country's most important trading partners.

9. The estimates of growth in **Eastern Europe** countries have been revised downwards again due to the lower GDP growth rates registered in 2012 (1.6 percent). Despite this, the indicators suggest that the economies in the region will tend to stabilize or initiate a recovery process in the first half of 2013, in line with

the evolution of some commercial partners such as Germany. In 2013 Eastern Europe countries are estimated to grow 2.3 percent.

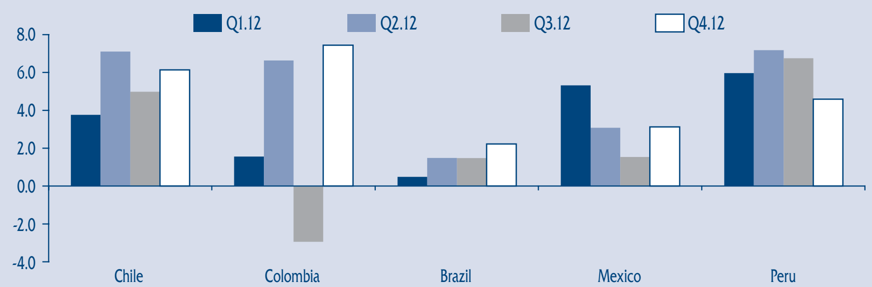
10. In 2012, the pace of economic growth continued to decline in most **Latin American** countries, in line with the slowdown of exports and domestic demand, even though the latter continued to lead growth. The deceleration of growth was higher in Brazil and Colombia. On the other hand, economic activity in Chile, despite the moderation observed recently, continued to grow at high rates.

During the year, Brazil grew 0.9 percent, recording the lowest rate of growth observed since 2009, due mainly to the unfavorable conduct of private investment and exports. Moreover, as various analysts have suggested, several structural factors would also account for this economic slowdown. Growth in Colombia slowed down from 6.6 to 4.0 percent due to the decline of construction and investment, as well as due to an irregular schedule for the implementation of infrastructure projects in Q3. On the other hand, countries like Chile and Mexico maintained their dynamism. In the case of Chile, this dynamism was higher than expected, especially in the second half of 2012, when growth was boosted by private investment.

This differentiated conduct continues to be observed in the first two months of the year. In Brazil, since the monthly indicators of activity show no clear signs of recovery, the prospects for growth are lower especially in a context in which rising rates and inflation expectations are reducing the space for policy responses. On the other hand, Chile continues to show better than expected indicators while the recovery in Colombia is being offset both by external factors (fears of a lower demand from Venezuelan) and by internal factors (strikes of coffee producers and groups associated with coal mining).

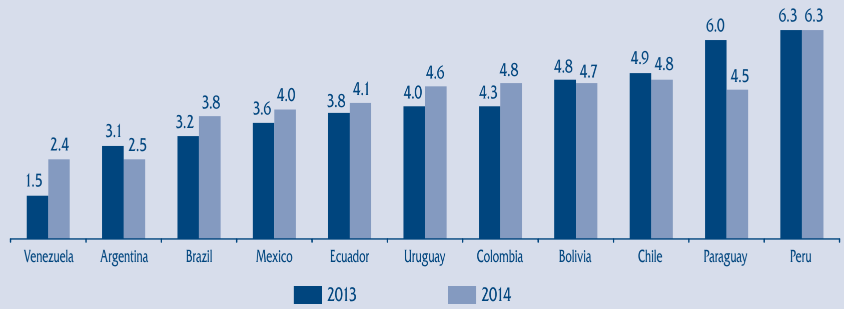
The region is expected to grow at a rate of 3.5 percent this year and to record a higher growth rate of 3.8 percent in 2014, in line with the recovery of the global economy and with still high commodity prices.

Graph 14
LATIN AMERICA: QUARTERLY GROWTH
(Seasonally adjusted annualized quarterly rates)



Source: Central banks and statistical institutes.

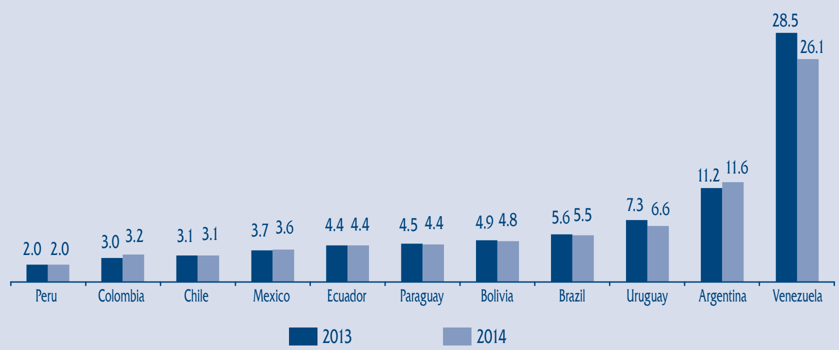
Graph 15
LATIN AMERICA: GDP GROWTH FORECAST



Source: Consensus Economics and BCRP (Peru).

As regards **inflation**, in most of the countries in the region with the exception of Brazil, inflation rates corrected downwards since December due to the evolution of food prices, the moderation of growth, and the appreciation of local currencies, reversing in this way the upward trend observed until Q3-2012 as a result of the increase in international food prices and demand pressures. At the end of the year, the rates of inflation in two of the major countries with inflation targeting regimes reached levels outside their target ranges: on the one hand, Uruguay registered an inflation rate of 7.5 percent –above the 4-6 percent target range– whereas, on the other hand, Chile registered a rate of 1.5 percent –below the lower band of its target range (2-4 percent). In all of the countries in the region, inflation in 2012 was lower than in 2011.

Graph 16
LATIN AMERICA: INFLATION FORECAST*



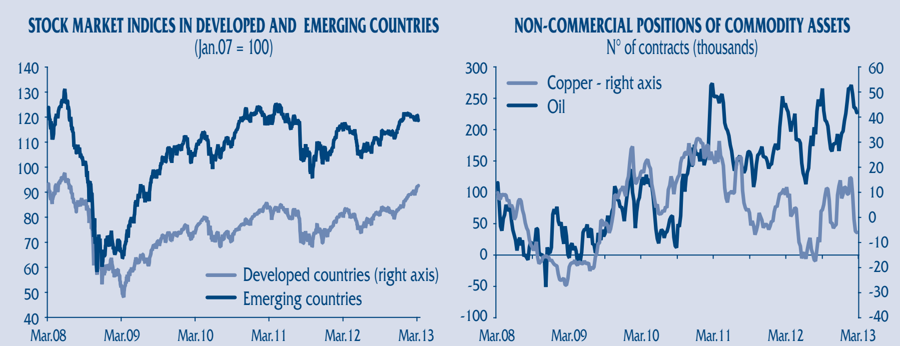
Source: Consensus Economics and BCRP (Peru).

Financial markets

11. Until mid-February, favorable conditions were observed in financial markets given that the major central banks of developed countries (such as the FED and the ECB) announced that they would maintain monetary stimulus and given that there was less uncertainty regarding the economy of Eurozone peripheral countries. Factors worth pointing out in the case of the latter included Greece's debt repurchase plan and the approval of the new terms of the program for Greece, the beginning of the restructuring process of Spanish banks, and the issuance of long-term debt securities by Spain and Italy, both of which had a good acceptance in markets.

    In a context of abundant international liquidity (see Graph 1), this better-than-expected evolution has reflected in a better risk perception in financial markets. The implied volatility index (VIX) has dropped significantly to levels unheard of since 2007 and a greater preference for risky assets, particularly variable income assets, has been observed, generating a positive impact on the evolution of stock market indices both in developed and in emerging countries. In contrast, on the other hand, a liquidation of non-commercial positions of commodity assets has been observed since the second half of February, which could be explained by fears of a lower demand of China after the measures implemented in its real estate sector.

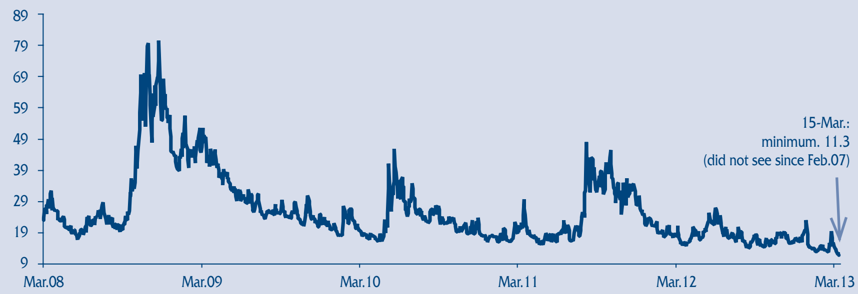
Graph 17



Source: Bloomberg. Source: Bloomberg.

However, since the last week of February, with the inconclusive results of the parliamentary elections in Italy and the recent events in Cyprus, uncertainty has increased again in Europe. Moreover, uncertainty due to the fiscal problem in the United States (which had also affected markets towards the end of December) and the measures adopted in China in order to offset the increase in real estate prices have added onto this.

Graph 18
RISK AVERSION COEFFICIENT: VIX (S&P'500)
(March 2008 - March 2013)



Source: Bloomberg.

12. **European money markets** continued showing a stable trend mainly as a result of measures such as the ECB's 3-year liquidity injections (carried out at the end of last December and in February) and the maintenance of low policy interest rates through which the conditions of illiquidity observed until October 2012 have been able to be corrected. Moreover, European banks' prepayments of the ECB loans, announced in January and February, 2013, would be pointing to a better financial position of European banks. The spread between the 3-month Euribor and the market overnight index swap (OIS) rate, which measures the tensions in money markets, has remained stable since mid-October, 2012, at around 12 basis points.

Graph 19
SPREAD BETWEEN THE 3-MONTH EURO-LIBOR RATE AND O/N OF SWAP MARKET (OIS)
(March 2008 - March 2013)

Source: Bloomberg.

13. Tensions in **developed sovereign debt markets** have declined, particularly after the better outcomes observed in the European economies with debt problems during the month of January and in the first weeks of February. In this period, the European sovereign spreads showed a clear downward trend while the yields in the U.S., the United Kingdom, and Germany showed a rising trend, in line with

expectations of more support through the monetary stimulus of the major central banks.

Table 4
SOVEREIGN SPREADS OF DEVELOPED COUNTRIES

	End of period						Difference in basis points		
	Dec. 08	Dec. 09	Dec. 10 (4)	Dec. 11 (3)	Dec. 12 (2)	Mar. 13 (1)	Dec. 10 (1)-(4)	Dec. 11 (1)-(3)	Dec.12 (1)-(2)
CDS (bps)									
USA	67	38	42	49	38	38	-3	-11	0
United Kingdom	107	82	74	98	41	44	-30	-54	2
Germany	46	26	59	102	42	34	-25	-68	-8
France	54	32	108	220	93	70	-38	-150	-24
Spain	101	114	350	380	300	275	-75	-106	-25
Italy	157	109	240	484	289	273	33	-212	-16
Greece 1/	232	286	1,010	8,786	4,265	3,890	2,880	-4,896	-375
Portugal	96	92	501	1 082	443	369	-132	-713	-74
Ireland	181	158	609	724	220	170	-439	-555	-50
10 Year Treasury yields (%)									
USA	2.21	3.84	3.29	1.87	1.76	1.99	-130	12	23
United Kingdom	3.02	4.02	3.40	1.98	1.83	1.94	-146	-4	11
Germany	2.95	3.39	2.96	1.83	1.32	1.46	-151	-37	14

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.

Since March, however, this trend has been partially offset by political uncertainty in Italy and by the recent events in Cyprus. Credit spreads have registered significant reductions, except for the spread in Italy, which has even surpassed the spread in Spain, even though the latter country has a financial rescue program.

In Latin America, the CDS spreads in most countries have declined, reflecting the lower tensions observed in international financial markets until mid-February.

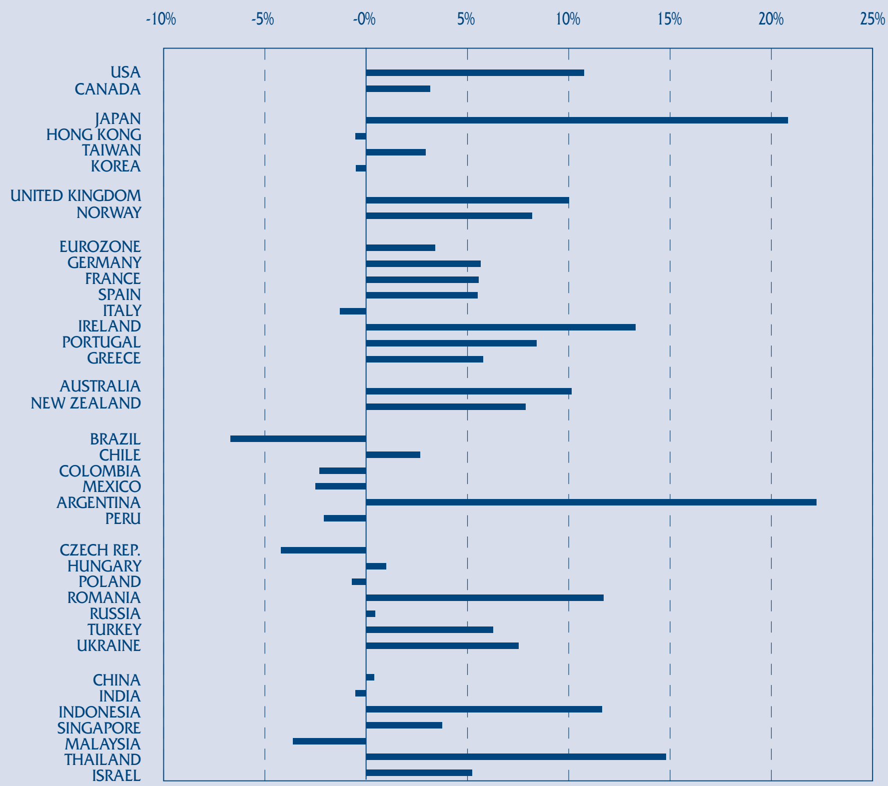
Table 5
SOVEREIGN SPREADS OF LATIN AMERICA ECONOMIES

	End of period						Difference in basis points		
	Dec. 08	Dec. 09	Dec. 10 (4)	Dec. 11 (3)	Dec. 12 (2)	Mar. 13 (1)	Dec. 10 (1)-(4)	Dec. 11 (1)-(3)	Dec. 12 (1)-(2)
Spreads CDS (bps)									
Argentina	3,905	961	610	923	1,401	2,715	2,106	1,792	1,315
Brazil	299	123	111	161	108	131	20	-30	22
Chile	203	69	84	132	72	63	-21	-70	-9
Colombia	308	144	113	154	96	89	-24	-65	-7
Mexico	292	134	113	153	97	90	-23	-63	-7
Peru	303	124	113	172	97	89	-25	-83	-8

Source: Bloomberg.

14. These better conditions in the markets also reflected in slight gains in the major stock markets, where the gains were also favored by a portfolio re-composition as fixed income securities were replaced by variable income securities. Except for Italy, almost all the stock exchanges in the developed markets accumulate earnings so far this year. In Latin America, the major stock exchanges have been slightly affected by the correction in commodity prices. In the case of Brazil, the stock exchange has also been affected by the deterioration of inflation expectations and by the growth outlook for 2013.

Graph 20
STOCK MARKETS
(End of period; % chg. Mar.13 respect to Dec.12)



Source: Bloomberg.

Foreign exchange rate

15. Relative to the close of December, the dollar has appreciated 1 percent against a basket of the major currencies. This would be basically reflecting greater risks in European countries with debt problems after the Italian political crisis and the recent events in Cyprus, as well as the worsening of conditions for growth in Europe (compared to conditions in the USA).

Graph 21
US DOLLAR INDEX*
(March 2008 - March 2013)

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

Table 6
EXCHANGE RATE
(End of period)

	Dec.08	Dec.09 (5)	Dec.10 (4)	Dec.11 (3)	Dec.12 (2)	Mar.13 (1)	Mar.13 % chg. compared to: Dec.09 (1)/(5)	Dec.10 (1)/(4)	Dec.11 (1)/(3)	Dec.12 (1)/(2)
Canada	1.22	1.05	1.00	1.02	0.99	1.02	-3.1	2.3	0.0	2.8
Japan	90.60	92.90	81.15	76.94	86.74	95.28	2.6	17.4	23.8	9.8
United Kingdom (US$/c.u.)	1.46	1.62	1.56	1.55	1.63	1.51	-6.5	-3.1	-2.7	-7.0
Eurozone (US$/c.u.)	1.40	1.43	1.34	1.30	1.32	1.31	-8.7	-2.3	1.0	-0.9
Switzerland	1.07	1.04	0.93	0.94	0.92	0.94	-9.3	0.6	0.1	2.5
Brazil	2.31	1.74	1.66	1.86	2.05	1.98	13.7	19.4	6.4	-3.2
Chile	636	507	468	519	478	472	-7.0	0.8	-9.2	-1.4
Colombia	2,246	2,040	1,915	1,936	1,766	1,806	-11.5	-5.7	-6.7	2.3
Mexico	13.65	13.06	12.36	13.95	12.86	12.43	-4.8	0.6	-10.9	-3.4
Argentina	3.454	3.799	3.979	4.302	4.915	5.089	34.0	27.9	18.3	3.5
Peru	3.136	2.890	2.808	2.697	2.552	2.592	-10.3	-7.7	-3.9	1.6
Hungary	188.30	187.96	208.15	243.28	220.21	233.44	24.2	12.1	-4.0	6.0
Poland	2.96	2.86	2.96	3.44	3.08	3.17	10.8	7.3	-7.8	2.8
Russia	30.53	30.31	30.57	32.19	30.55	30.62	1.0	0.2	-4.9	0.2
Turkey	1.54	1.50	1.54	1.88	1.78	1.81	21.2	17.9	-3.8	1.9
China	6.82	6.83	6.59	6.29	6.23	6.21	-9.0	-5.7	-1.3	-0.3
India	48.58	46.40	44.70	53.01	54.99	54.02	16.4	20.9	1.9	-1.8
Israel	3.78	3.79	3.52	3.81	3.73	3.68	-2.7	4.6	-3.3	-1.2
FED basket	107.40	101.60	99.17	100.64	99.21	100.40	-1.2	1.2	-0.2	1.2

Source: Bloomberg and Reuters.

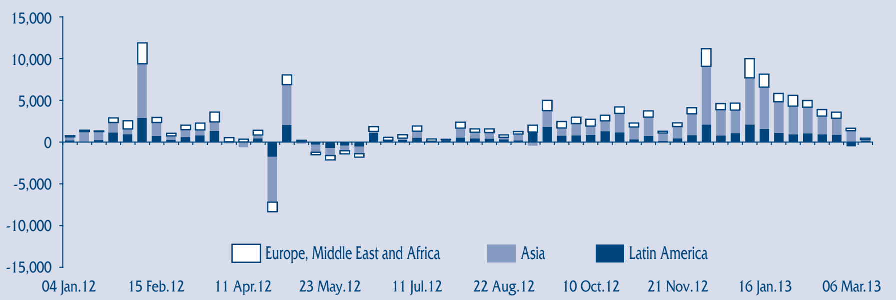
Thus, between December and March, the dollar has appreciated 0.9 percent against the euro and 7.0 percent against the pound. In addition, maintaining the trend observed in the last months of 2012, which responds to expectations that the Bank of Japan will loosen its monetary policy, the dollar has appreciated 9.8 percent against the yen.

Graph 22
EXCHAGE RATE OF EURO (US$ PER €)
(March 2012 - March 2013)

Source: Reuters.

Most **Latin American currencies** have appreciated in the last three months in a context of net capital inflows to the region. This trend was offset by temporary events of higher global risk aversion and falling commodity prices. The currencies of Brazil, Chile, and Mexico have appreciated relative to their values at the end of last year, whereas the currencies of Argentina and Colombia have depreciated. It should be also pointed out that the Government of Venezuela devalued the official exchange rate by 32 percent (from 6.3 to 4.3 bolivars per dollar) in early February.

Graph 23
PORTFOLIO CAPITAL INFLOWS TO EMERGING ECONOMIES*
(Weekly flows, millions of US$)



* Includes dedicated and non-dedicated funds.
Source: Barclays.

Interest rate decisions

16. Continuing with the trend discussed in previous inflation reports, so far this year most central banks have maintained their interest rates unchanged. Of a sample

of 32 central banks, only five –Israel, Colombia, Hungary, India, and Poland– have lowered their rates by 25 basis points and only one central bank –Serbia– has raised it, also by 25 basis point

Table 7
MONETARY POLICY INTEREST RATE

							Acummulated variation (bps.)			
	Sep.12	Oct.12	Nov.12	Dec.12	Jan.13	Feb.13	Dec.12	Nov.12	Dec.11	Sep.08
Serbia	10.50	10.75	10.95	11.25	11.50	11.75	25	30	150	-450
South Korea	3.00	2.75	2.75	2.75	2.75	2.75	0	0	-50	-250
ECB	0.75	0.75	0.75	0.75	0.75	0.75	0	0	-25	-350
Chile	5.00	5.00	5.00	5.00	5.00	5.00	0	0	-25	-325
USA	0.25	0.25	0.25	0.25	0.25	0.25	0	0	0	-175
Indonesia	5.75	5.75	5.75	5.75	5.75	5.75	0	0	-25	-350
Mexico	4.50	4.50	4.50	4.50	4.50	4.50	0	0	0	-375
Philippines	3.75	3.50	3.50	3.50	3.50	3.50	0	0	-100	-250
United Kingdom	0.50	0.50	0.50	0.50	0.50	0.50	0	0	0	-450
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0	0	0	-40
Uruguay	9.00	9.00	9.00	9.25	9.25	9.25	0	25	50	200
South Africa	5.00	5.00	5.00	5.00	5.00	5.00	0	0	-50	-700
Pakistan	10.50	10.00	10.00	9.50	9.50	9.50	0	-50	-250	-350
Peru	4.25	4.25	4.25	4.25	4.25	4.25	0	0	0	-225
Switzerland	0.25	0.25	0.25	0.25	0.25	0.25	0	0	0	-250
Thailand	3.00	2.75	2.75	2.75	2.75	2.75	0	0	-75	-100
Taiwan	1.88	1.88	1.88	1.88	1.88	1.88	0	0	0	-163
Turkey	5.75	5.75	5.75	5.50	5.50	5.50	0	-25	-25	-1 125
China	6.00	6.00	6.00	6.00	6.00	6.00	0	0	-56	-120
Canada	1.00	1.00	1.00	1.00	1.00	1.00	0	0	0	-200
Brazil	7.50	7.25	7.25	7.25	7.25	7.25	0	0	-375	-650
Australia	3.50	3.25	3.25	3.00	3.00	3.00	0	-25	-125	-400
Iceland	5.75	5.75	6.00	6.00	6.00	6.00	0	0	125	-950
Malaysia	3.00	3.00	3.00	3.00	3.00	3.00	0	0	0	-50
Norway	1.50	1.50	1.50	1.50	1.50	1.50	0	0	-25	-425
New Zealand	2.50	2.50	2.50	2.50	2.50	2.50	0	0	0	-500
Sweden	1.25	1.25	1.25	1.00	1.00	1.00	0	-25	-75	-375
Israel	2.25	2.00	2.00	2.00	1.75	1.75	-25	0	-75	-225
Colombia	4.75	4.75	4.50	4.25	4.00	3.75	-25	-25	-50	-575
Hungary	6.50	6.25	6.00	5.75	5.50	5.25	-25	-25	-125	-275
India	8.00	8.00	8.00	8.00	7.75	7.75	-25	0	-50	-100
Poland	4.75	4.75	4.50	4.25	4.00	4.00	-25	-25	-25	-175

Source: Reuters and Bloomberg.

This has taken place in a context of low inflationary pressures in most developed economies, which facilitates that monetary stimuli be maintained. In the largest emerging economies, on the other hand, particularly in Brazil and China, inflation has shown a rebound relative to the rates observed towards the end of 2012.

Table 8
INFLATION IN MAIN COUNTRIES
(12 Months % change)

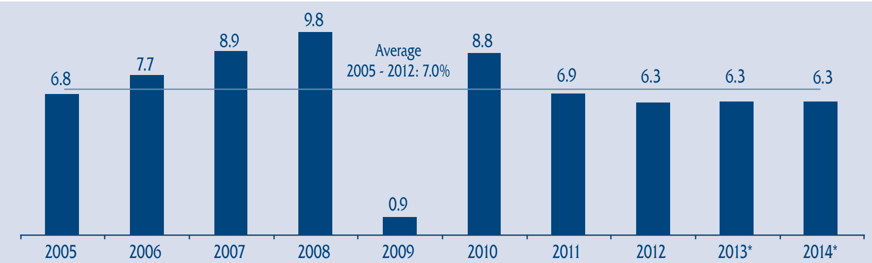
	Dec.10	Dec.11	Dec.12	Jan.13	Feb.13
Developed countries					
1. United States	1.5	3.0	1.7	1.6	2.0
2. Eurozone	2.2	2.7	2.2	2.0	1.8
Germany	1.9	2.3	2.0	1.9	1.8
France	1.5	2.7	1.5	1.4	1.2
Italy	2.1	3.7	2.6	2.4	2.0
Spain	2.9	2.4	3.0	2.8	2.9
3. Japan	0.0	-0.2	-0.1	-0.3	n.d.
4. United Kingdom	3.7	4.2	2.7	2.7	2.8
Developing countries					
1. China	4.6	4.1	2.5	2.0	3.2
2. India	9.5	6.5	7.3	6.6	6.8
3. Russia	8.8	6.1	6.6	7.1	7.3
4. Brazil	5.9	6.5	5.0	6.2	6.3
Average Inflation 1/	**3.4**	**3.6**	**2.7**	**2.4**	**3.1**

1/ Average inflation in some countries weighted by share of world GDP PPP. On December 2012 and months in 2013 were used, 2011 weights.
Source: Bloomberg; FMI, WEO october 2012 and Eurostat.

II. Economic Activity

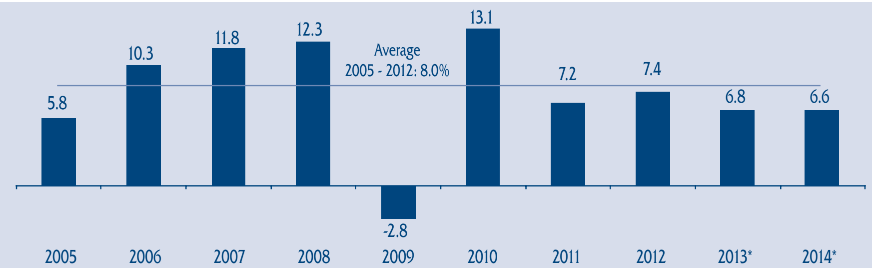
17. The growth of the Peruvian economy has stabilized around its long-term sustainable level. In 2012, economic activity in Peru grew 6.3 percent as a result of a greater dynamism in domestic demand, particularly in private and public investment. In this context, the growth of domestic demand increased from a rate of 6.2 in the first half of the year to a rate of 8.6 percent in the second half, while economic activity grew 6.2 and 6.3 percent in the same periods, respectively. For 2013 and 2014, the central projection scenario considers that GDP will grow at stable levels close to the level of the economy's potential output, with the greater impulse of domestic demand prevailing over a context in which weak indicators of global growth would persist.

Graph 24
GDP: 2005-2014
(Real % change)



* Forecast.

Graph 25
DOMESTIC DEMAND: 2005 - 2014
(Real % change)



* Forecast.

18. The growth of domestic demand accelerated in Q3 and in Q4 registering an expansion of 9.8 and 7.6 percent in these quarters, respectively, and showing higher rates than the growth rates recorded by the GDP in the same periods. Based on this trend of domestic demand, the forecast for 2013 considers a lower slowdown in this variable than the one estimated in our December inflation report due to the recent evolution of private investment as well as to optimistic consumer and business expectations.

In this line, the forecast of GDP growth in 2013 has been revised upwards from 6.2 percent (Inflation Report of December) to 6.3 percent, while in 2014 GDP is estimated to grow 6.3 percent (the same rate forecast in our previous inflation report).

Forecast of expenditure components

19. The growth forecast of the domestic demand in 2013 has been revised upwards from 6.3 percent (Inflation Report of December) to 6.8 percent in this report, which still considers a slowdown in the domestic demand compared to the previous years. This upward revision is explained by the greater dynamism of both private and public spending, both of which account for a contribution of 0.3 percentage points to the increased growth of domestic demand relative to our previous forecast.

Table 9
GDP AND DOMESTIC DEMAND
(Real % change)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
1. DOMESTIC DEMAND	**7.2**	**7.4**	**6.3**	**6.8**	**6.3**	**6.6**
a. Private consumption	6.4	5.8	5.7	5.7	5.7	5.7
b. Public consumption	4.8	10.6	7.6	10.1	6.2	6.6
c. Private investment	11.7	13.6	8.2	8.8	8.2	8.2
d. Public investment	-17.8	20.9	15.2	15.0	11.7	11.4
2. Exports	**8.8**	**4.8**	**7.7**	**5.1**	**9.1**	**7.9**
3. Imports	**9.8**	**10.4**	**7.5**	**7.8**	**8.9**	**8.9**
4. GDP	**6.9**	**6.3**	**6.2**	**6.3**	**6.3**	**6.3**
Memo:						
Government expenditure	*-4.2*	*14.1*	*10.4*	*11.9*	*8.3*	*8.3*

IR: Inflation report.
* Forecast.

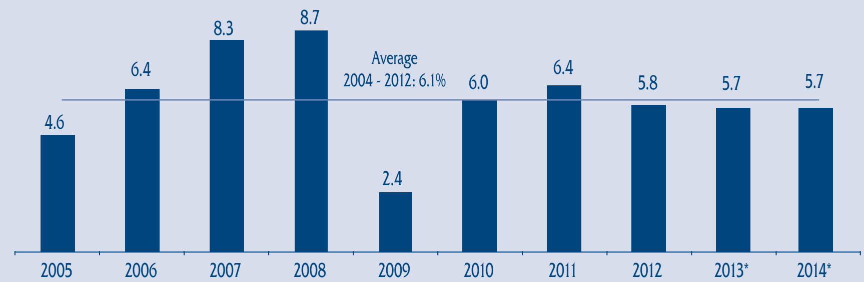
Table 10
GDP AND DOMESTIC DEMAND
(Contributions to the real % change)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
1. DOMESTIC DEMAND	**7.5**	**7.7**	**6.6**	**7.2**	**6.7**	**7.0**
a. Private consumption	4.2	3.9	3.7	3.7	3.7	3.7
b. Public consumption	0.5	1.0	0.7	1.0	0.6	0.7
c. Private investment	2.5	3.1	2.0	2.1	2.0	2.0
d. Public investment	-1.1	1.0	0.8	0.8	0.7	0.7
e. Inventory variation 1/	1.4	0.3	-0.4	-0.2	-0.6	-0.3
2. Exports	**1.6**	**0.9**	**1.4**	**0.9**	**1.7**	**1.4**
3. Imports	**2.1**	**2.3**	**1.7**	**1.8**	**2.1**	**2.1**
4. GDP	**6.9**	**6.3**	**6.2**	**6.3**	**6.3**	**6.3**
Memo:						
Government expenditure	*-0.7*	*2.0*	*1.6*	*1.8*	*1.3*	*1.3*

1/ Percentage of GDP.
IR: Inflation report.
* Forecast.

20. **Private consumption** in 2012 had a lower dynamism than in 2011 and registered a growth rate of 5.8 percent (6.4 percent in 2011). This would be confirming a gradual moderation in the growth of consumption compared to the previous two years, but more stable rates are expected in the next years in line with the GDP growth foreseen for those years. The expansion of consumption in a context of consumer optimism is reflected in several indicators, such as the sales of new family vehicles which grew 34.8 in Q4 and accumulated a rate of 37.9 percent in the year, and the increase in consumer loans, which climbed 15.2 and 13.9 percent in December 2012 and in February.

Graph 26
PRIVATE CONSUMPTION: 2005 - 2014
(Real % change)

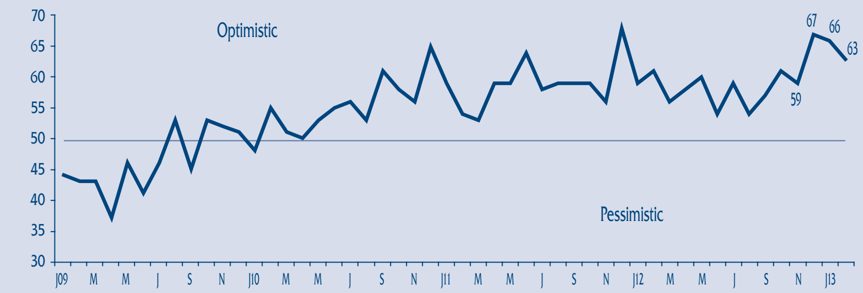


* Forecast.

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

a. The Consumer Confidence Index continues to be on the optimistic side. This indicator maintained an average level of 62 points in Q4 (vs. 57 points in Q3). Although it registered a slight deterioration in the first two months of this year, it still shows a higher level than the average level it had in 2012 (58 points).

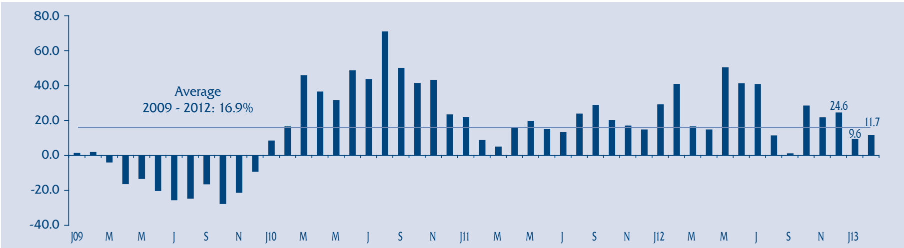
Graph 27
CONSUMER CONFIDENCE INDEX: 2009 - 2013
Households' economic situation



Source: Ipsos APOYO.
Elaboration: BCRP.

b. The volume of imports of durable consumer goods continued to grow at high rates –at around 10 percent in the last two months–, even though showing a slower pace of growth than in Q4 (25.0 percent).

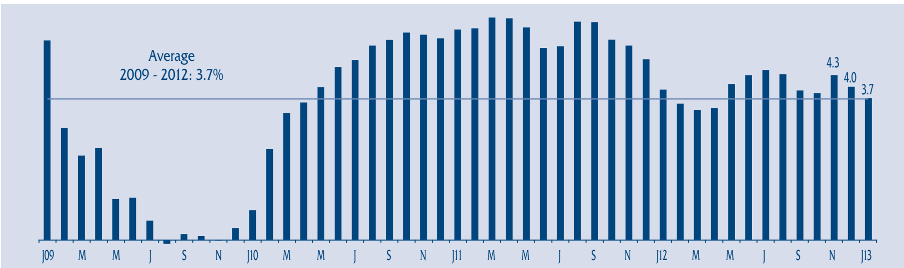
Graph 28
VOLUME OF IMPORTS OF DURABLE CONSUMER GOODS: 2009 - 2013
(12 month % change)



Source: SUNAT.

c. Recording a similar rate to the average rate in 2009-2013 but showing a more moderate growth rate than in 2011 and 2012, urban employment in firms with 10 and more workers grew 3.7 percent in January 2013.

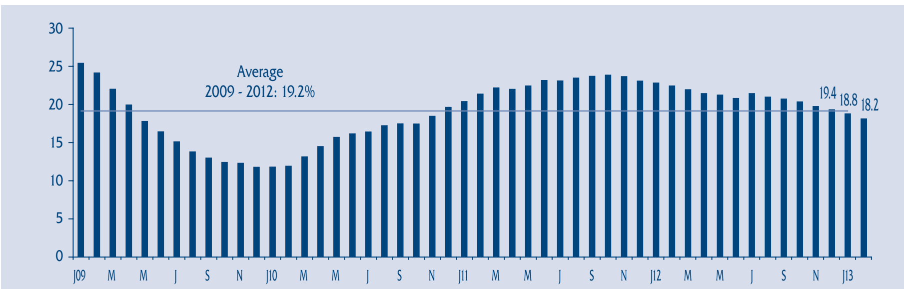
Graph 29
URBAN EMPLOYMENT IN FIRMS WITH 10 OR MORE WORKERS: 2009 - 2013
(12 month % change)



Source: MTPE.

d. The growth of personal credit, which includes consumer loans and mortgages, has moderated compared to the rates observed in 2012.

Graph 30
PERSONAL CREDITS: 2009 - 2013
(12 month % change)



Based on these indicators, the growth forecast of consumption in 2013 remains unchanged at 5.7 percent. Consumption is foreseen to stabilize around this rate and to show a similar growth in 2014.

21. Showing two-digit quarterly expansion rates with a slight slowdown in Q4, **private investment** grew 13.6 percent in 2012, reaching in this way ratios of over 20 percent as a percentage of GDP. This rising trend is associated with the recovery of business confidence, as reflected in the surveys on macroeconomic expectations during this period. Several indicators reflect the evolution of private investment:

   a. Business expectations on the situation of the economy in the three months ahead continue to be on the optimistic segment and registered 66 points in February, a higher level than the ones recorded in 2012.

Graph 31
EXPECTATIONS ABOUT THE ECONOMY IN THE NEXT 3 MONTHS: 2009 - 2013

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

   b. Economic agents have raised their expectations of GDP growth in 2013. In 2014 GDP is expected to grow between 6.0 and 6.5 percent.

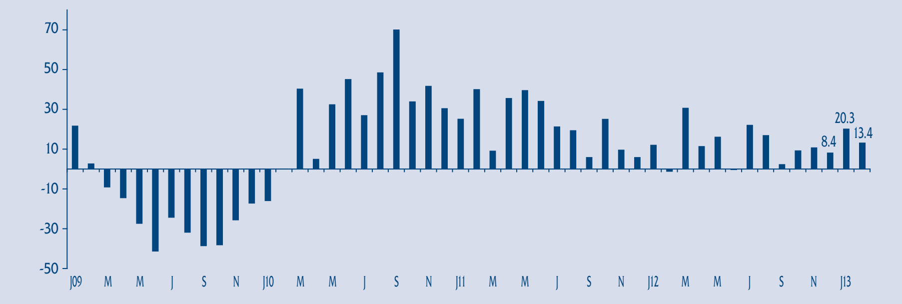
Table 11
SURVEY ON MACROECONOMIC EXPECTATIONS : GDP GROWTH
(%)

	Expectations about:		
	RI Sep.12	**IR Dec.12**	**IR Mar.13**
Financial entities			
2013	6.0	6.0	6.3
2014	6.0	6.0	6.1
Economic analysts			
2013	5.9	6.0	6.3
2014	6.0	6.0	6.5
Non-financial firms			
2013	6.0	6.0	6.1
2014	6.0	6.0	6.0

IR: Inflation report.
Source: Survey conducted during the second fortnight of February 2013.

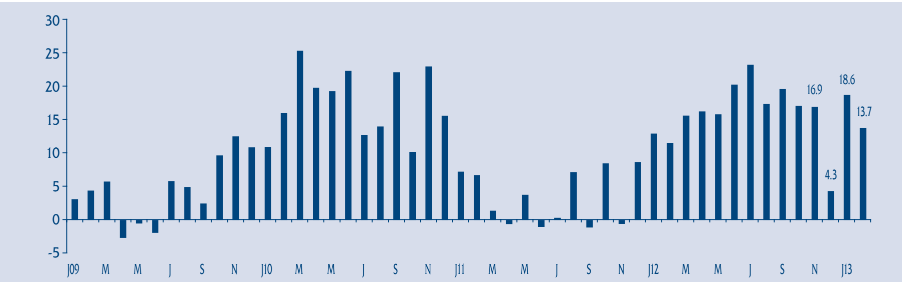
c. The volume of imports of capital goods, indicator of investment demand, has been showing two-digit rates in recent months.

Graph 32
VOLUME OF IMPORTS OF CAPITAL GOODS: 2009 - 2013
(12 month % change)



d. The domestic consumption of cement showed a two-digit growth rate in the first two months of 2013.

Graph 33
DOMESTIC CONSUMPTION OF CEMENT: 2009 - 2013
(12 month % change)



Source: ASOCEM and cement companies.

e. The production of electricity continues to show a significant dynamism with rates of over 5 percent on average in the last months.

Graph 34
PRODUCTION OF ELECTRICITY: 2009 - 2013
(12 month % change)

Source: COES.

22. It should be pointed out that the evolution of these indicators in the first quarter of 2013 would be affected by the calendar effect on the number of working days in this period given that there were fewer working days in Q1-2013 than in Q1-2012. Two factors account for this: on the one hand, since 2012 was a leap year, the month of February in 2012 had an additional day, and, on the other hand, the Easter holidays this year will take place in March whereas in 2012 they took place in April.

23. Investment projects announced for the period 2013 - 2014 amount to US$ 32.0 billion, a figure higher by US$ 0.9 billion than the one considered in our Inflation Report of December.

Table 12
INVESTMENT PROJECTS ANNOUNCED
(Millions of US$)

	2013	2014	2013 - 2014
Mining	7,756	7,037	14,793
Hydrocarbons	3,020	1,972	4,992
Electricity	2,379	1,447	3,826
Industry	971	838	1,809
Infrastructure	1,112	585	1,697
Other sectors	3,315	1,604	4,919
Total	**18,553**	**13,483**	**32,036**

Source: Information companies.

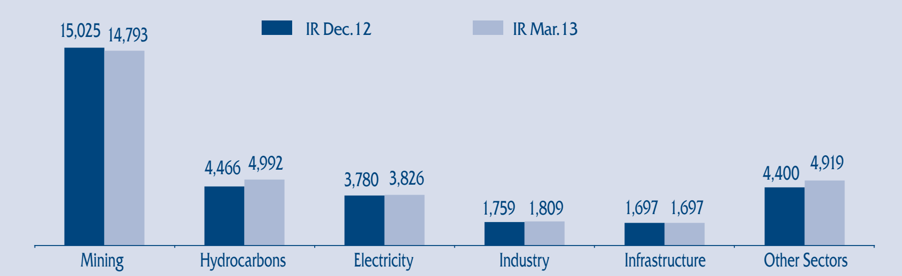
This increase is explained in part by the higher number of investment projects announced in the hydrocarbon sector. For example, Pacific Rubiales Energy has announced the implementation of projects in five lots: lot Z-1 in Tumbes, operated together with BPZ; lots 135 and 137 in Loreto; lot 116 in Amazonas, and lot 138 in Ucayali, where it will initiate the drilling of its first well, the Yahuish - 1X.

Table 13
INVESTMENT PROJECTS ANNOUNCED
(Millions of US$)

	2013 - 2014		
	IR Dec.12	IR Mar.13	Differences
Mining	15,025	14,793	-232
Hydrocarbons	4,466	4,992	526
Electricity	3,780	3,826	46
Industry	1,759	1,809	50
Infrastructure	1,697	1,697	0
Other sectors	4,400	4,919	519
Total	**31,127**	**32,036**	**909**

Source: Information companies.

Graph 35
INVESTMENT PROJECTS ANNOUNCED: 2013-2014
(Millions of US$)

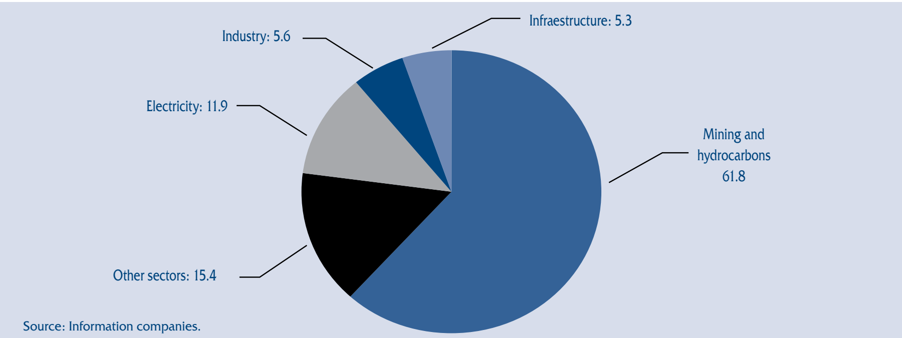


Source: Information companies.

Investments in the mining sector would increase in 2013, as reflected in the announcement of projects whose implementation has been confirmed. Mining company Toromocho has announced that it will increase its investment by US$ 1.3 billion and the Constancia project has already issued the purchase orders for the equipment required for the provision of energy and automation needed to start up the project. However, the implementation of projects is still somewhat slowed down by the existence of unresolved social conflicts and by delays in the procedures to be followed to obtain permits for exploration and exploitation, which causes the execution of the investment portfolio to be rescheduled. The investment flows in the mining and hydrocarbons sectors considered here include the reference amounts in the different stages of project implementation (studies, exploration and exploitation, plant construction, among others) in the case of projects with preliminary or approved environmental impact studies.

The sectors associated with the construction sector, such as the real estate, hotel, and health sectors continue making important investment announcements which include both the implementation of new projects and the expansion and refurbishment of already existing facilities, both in Lima and in the provinces. The retail sector will continue to grow in 2013 given that the main operators of shopping centers have announced that they will invest more than US$ 350 million in the construction of ten new shopping centers in the country.

Graph 36
FORESEEN INVESTMENT PROJECTS: 2013-2014
(% participation)



Source: Information companies.

Table 14
ANNOUNCED MAIN INVESTMENT PROJECTS: 2013-2014

SECTOR	COMPANIES	PROJECT NAMES
Mining	Xstrata Copper	Las Bambas
	Freeport-Macmoran Copper	Expansion:Cerro Verde
	Aluminium Corp of China Ltd. (Chinalco)	Toromocho
	Norsemont Mining Inc., HudBay Minerals Inc.	Constancia
	Antares Minerals Inc.	Haquira
	Anglo American Plc.	Quellaveco
	China Minmetals Corporation y Jiangxi Copper Company Ltd.	El Galeno
	Cumbres Andinas, Korea Resources Corp.	Mina Justa
	Bear Creek Mining Corporation	Corani
	Grupo Milpo	Expansion: Cerro Lindo and El Porvenir
	Hochschild Mining International Minerals Corporation	Inmaculada
	Shougang Corporation	Expansion: Marcona
	Minera Gold Corp.	Expansion: Lagunas Norte
	Grupo Buenaventura	Expansion: Colquijirca
	Grupo México S.A.B. de C.V.	Expansion: Cuajone
Hydrocarbons	Pluspetrol Perú Corp. S.A.	Expansion of Pisco and Malvinas plants
	Savia Perú S.A.	Lot Z-2B: Perforation, exploration and other investments
	Pacific Rubiales Energy	Lots: Z1-135 - 137 - 116 - 138
	Transportadora de Gas del Perú S.A.	Expansion of gas and capacity of transportation
	Petrobras	Lot 58 and Lot X
	Cálidda Gas Natural del Perú	Expansion of main grid
	Perenco	Exploration Lot 67 and pipeline
	Pluspetrol Perú Corp. S.A.	Exploration Lots 88 and 56
	SK Energy	Exploration Lot Z 46
	Repsol Exploración, Petrobras Energía Perú S.A.	Lot 57 - Kinteroni
Electricity	Odebrecht S.A.	Hydroelectric plant of Cerro de Chaglla
	Inkia Energy	Hydroelectric plant of Cerro del Águila
	Norwind	Wind energy park Cerro Chocan
	Energía Azul S.R.L.	Hydroelectric plant Santa María
	SN Power Perú S.A.	Hydroelectric plant Cheves
	Volcan Compañia Minera S.A.A.	Hydroelectric planta Belo Horizonte
	GDF Suez	Hydroelectric plant Quitaracsa I
	Inevarante	Hydroelectric plant Acco Pucará
	GDF Suez	Cold Power Generation Reserve - Ilo and Talara
	Energía de Entre Ríos S.A. - ENERSA, Grupo Cobra	Cold Power Generation Reserve - Éten
	Abengoa	Machupicchu – Quencoro – Onocora – Tintaya Transmission Line
Industry	Hochschild Mining S.A.	Phospates projects
	Siderperú	Modernization of plant
	Repsol YPF	Expansion of La Pampilla plant
	Grupo Celepsa	Expansion of rolling mill (N° 2)
	Grupo Pilkington Limited	Manufacture plant of float glasses
	Corporación JR Lindley	Expansion and new plants
Infrastructure	OAS S.R.L.	Parque Rimac express way
	Covisol	Trujillo-Sullana: Sol Highway
	APM Terminals	Modernization of North Pier
	Autopista del Norte SAC	Pativilca – Port of Salaverry Road Network No. 4
	Consorcio Transportadora Callao	Minerals Pier
	Tertir Terminais / Cosmos / Translei	Expansion: Port Paita
	Grupo Romero	Expansion: Port Matarani
Other sectors	Grupo Brescia	Real state and health centers
	Grupo Falabella	Mall Aventura: New malls
	Grupo Interbank	Expansion and constructions: Real Plaza (Lima and Provinces)
	Banmédica, Grupo Roe, Grupo San Pablo, Grupo Mapfre, Pacífico EPS	Expansion and constructions: Health centers
	Graña y Montero, Inmobiliari, Paz Centenario, Grupo San José, Rutini, Besalco, Grupo Fierro	Real state and health centers
	Ripley, Cencosud, Ekimed,Quimera	Expansion and constructions : Ripley, Almacenes Paris, and malls.

Source: Media press and Information companies.

Additionally, Proinversión has important projects which will be given in concession, including the Molloco hydroelectric power plant in Arequipa, the third stage of the Chavimochic irrigation project in La Libertad, and works to supply areas with potable water in Lima, among other projects.

Table 15
MAIN PROJECTS TO BE IMPLEMENTED THROUGH CONCESSION ARRANGEMENTS

Project	Estimated Investment (US$ Millions)
Hydroelectric Power Plant of Molloco (Arequipa)*	600
Chavimochic Stage III Irrigation Project	600
Drinking Water Works for Lima	400
Mantaro – Marcona – Socabaya – Montalvo Transmission Line (500 kV) and Associated Sub-stations	380
New International Airport of Chinchero - Cusco	356
Transmisión Moyobamba - Iquitos Transmission Line (220 KV)	345
National Fiber Optics Backbone	315
Supply System of LPG for Lima and Callao	260
Supply System of LNG for the domestic market	250
Longitudinal de la Sierra - Stretch 4	250
Expansion of the use of natural gas nationwide	205
Longitudinal de la Sierra - Stretch 2	175
Longitudinal de la Sierra - Stretch 5	127
Port Terminal General San Martín	101
Energy Supply for Iquitos (formerly Cold Reserve Project)	100
Supply of Water and Sanitation Services for Districts in the south of Lima	100
Amazon Waterway: Maranon, Amazonas, and Huallaga Rivers	74
Total	**4,638**

* Project granted in concession on March 21, 2013.
Source: Proinversión.

Moreover, major public investment projects are foreseen to be implemented at the level of regional and local governments in 2013, including the Electric Train project in Lima and Callao, the construction and equipment of primary schools, and the execution of a large number of works to improve road infrastructure at the national level, among others.

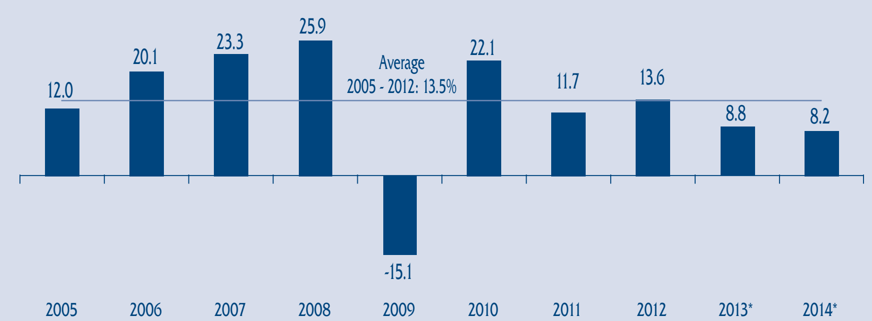
Table 16
MAIN PUBLIC INVESTMENT PROJECTS

Project	Estimated investment (US$ Millions)
Special Project Electric Train for Lima and Callao	1,172
Construction and Equipment of Primary Schools - II Cycle of Regular Basic Education	930
Rehabilitation and Improvement of the Ayacucho-Abancay Road	364
Rehabilitation and Improvement of the Chongoyape-Cochabamba Road - Cajamarca	242
Improvement of Health Services Hospital Antonio Lorena Nivel III-1-Cusco	212
Rehabilitation and Improvement of the Lima-Canta-La Viuda-Unish Road	193
Rehabilitation and Improvement of the Quinua-San Francisco Road	181
Rehabilitation and Improvement of the Juanjui-Tocache Road	175
Modernization of the Anti-Tank Defense System	172
Rehabilitation and Improvement of the Chamaya-Jaén-San Ignacio-Río Canchis Road	167
Increase the Peruvian Air Force's Operational Capacity of Surveillance of the Peruvian Amazon Air Space	152
Rehabilitation and Improvement of the Huaura-Sayán-Churín Road	137
Rehabilitation and Improvement of the Cajamarca-Celendín-Balzas Road	111
Rehabilitation and Improvement of the Trujillo-Shiran-Huamachuco Road	108
Construction and Improvement of the Camaná-Dv. Quilca-Matarani-Ilo-Tacna Road	100
Improvement of Irrigation and Hydroenergy Generation Infrastructure in Alto Piura	89
Construction and equipment of Level III-1 Hospital Victor Ramos Guardia, Huaraz, Province of Huaraz, Ancash	88
Improvement of the Satipo-Mazamari-Dv. Pangoa-Puerto Ocopa Road	78
Rehabilitation and Improvement of the Yauri-Negromayo-Oscollo-Imata Road, Stretch Dv. Imata-Oscollo-Negromayo	70
Improvement of at-sea training for navy cadets being trained by the Peruvian Navy	65
Construction and Implementation of Hospital II-2 in Jaén	60
Majes Siguas Project - Stage II	57
Total	**4,924**

Source: Presupuesto del Sector Public 2013.

Given that private investment is showing a more dynamic evolution than expected, the growth forecast of private investment in 2013 has been revised upwards from 8.2 percent (Inflation Report of December) to 8.8 percent. The forecast for 2014 remains unchanged at 8.2 percent.

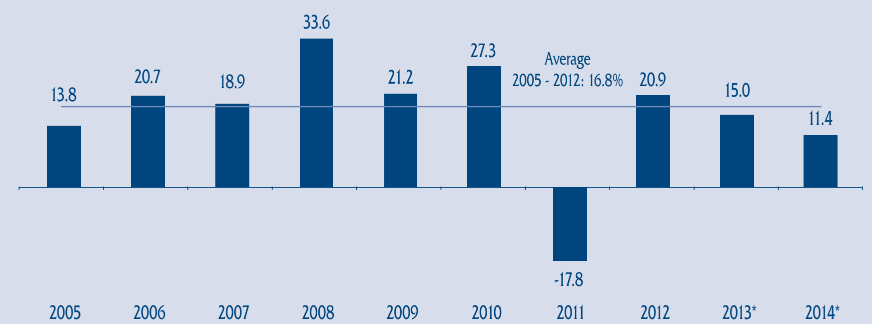
Graph 37
PRIVATE INVESTMENT: 2005 - 2014
(Real % change)



* Forecast.

24. In 2012 **public investment** grew 20.9 percent, favored by the increased spending of the regional and local governments in road and education infrastructure as well as in water and sanitation works. Investment in the case of the national government and state-owned enterprises was lower than in 2011. A downward trend was registered during the year in the pace of growth of public investment since it dropped from 39.4 percent in Q1 to 9.7 percent in Q4. Public investment would grow at quarterly rates around 15.0 percent in 2013 reaching a rate 15.0 percent at year end.

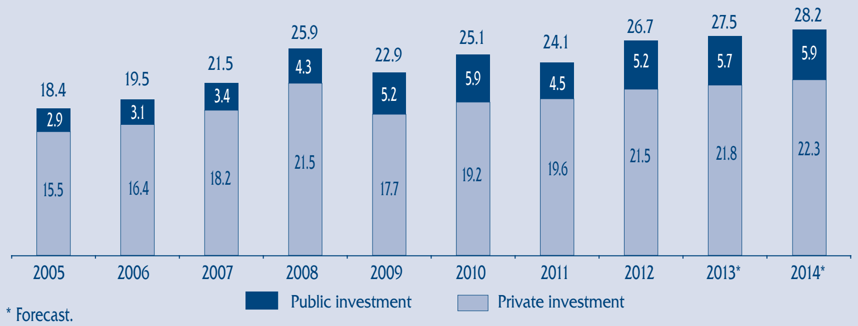
Graph 38
PUBLIC INVESTMENT: 2005 - 2014
(Real % change)



* Forecast.

25. Considering the evolution of public investment and private investment, the gross investment-to-GDP ratio would be higher than 27 percent in 2013, in line with the estimates of our previous Inflation Report.

Graph 39
GROSS FIXED INVESTMENT: 2005 - 2014
(% of GDP)



* Forecast.

The forecast considers that the increase in the ratio of investment to GDP would be financed mainly by increasing domestic savings, which would continue to show the rising trend observed in recent years. Domestic savings would grow from 23.1 percent of GDP in 2012 to 24.3 percent in 2014, in line with the growth of income.

Table 17
SAVING - INVESTMENT GAP
(% of GDP)

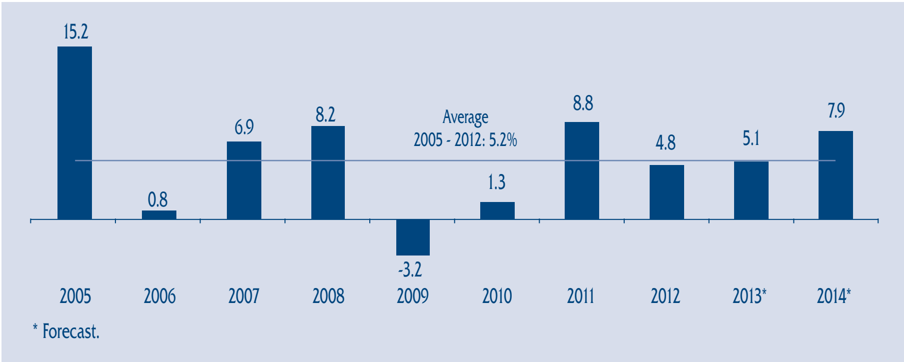
	2011	2012	2013*	2014*
1. GROSS FIXED INVESTMENT	**24.1**	**26.7**	**27.5**	**28.2**
a. Private	20.9	21.7	21.7	22.0
b. Public	4.5	5.2	5.7	5.9
2. NET DOMESTIC SAVING 1/	**22.2**	**23.1**	**23.5**	**24.3**
3. EXTERNAL SAVING	**1.9**	**3.6**	**4.0**	**3.9**

1/ Excluding inventory variations.
* Forecast.

26. In a context of slowdown in global trade, **exports** grew 4.8 percent in 2012 and registered a lower rate than in the previous year (8.8 percent). A weak evolution of exports was observed in Q4 due to a drop in exports of traditional products (-3.2 percent), especially coffee and gold, whereas non-traditional exports grew 7.0 percent in terms of volume.

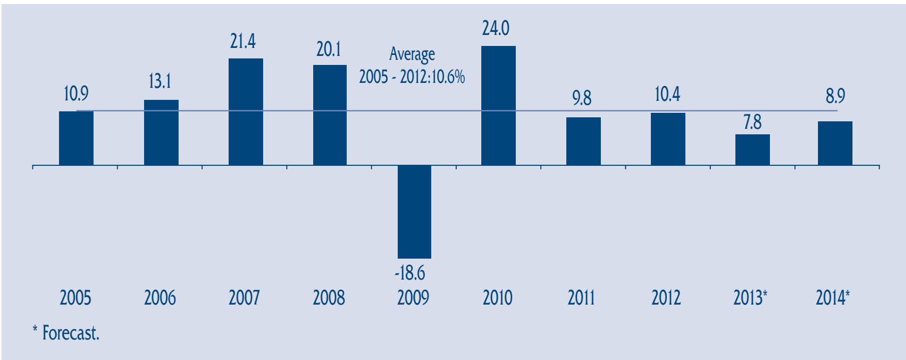
Exports are foreseen to follow a recovery path towards 2014 due mainly to the onset of operations of copper mining projects, such as Toromocho, Las Bambas, and Constancia, located in the regions of Apurimac, Junín and Cusco, respectively.

Graph 40
EXPORTS OF GOODS AND SERVICES : 2005 - 2014
(Real % change)



On the other hand, **imports** grew 10.4 percent in 2012 as a result of increased imports of consumer goods and non-financial services, which showed rates of 19.4 and 13.7 percent, respectively. In 2013 and 2014, imports would grow at lower rates than in the past three years and register growth rates of 7.8 and 8.9 percent, respectively, in line with the moderation foreseen in the growth of domestic demand.

Graph 41
IMPORTS OF GOODS AND SERVICES : 2005 - 2014
(Real % change)



GDP by production sectors

27. GDP recorded a growth rate of 6.3 percent in 2012. An acceleration of growth was observed in non-primary sectors (7.1 percent), particularly in the sectors of construction, trade, and services, in accordance with the dynamism of domestic demand.

Table 18
GROSS DOMESTIC PRODUCT BY ECONOMIC SECTORS
(Real % change)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
Agriculture and livestock	**3.8**	**5.1**	**4.3**	**3.5**	**4.2**	**4.2**
Fishing	**29.7**	**-11.9**	**2.6**	**1.1**	**1.1**	**3.3**
Mining and hydrocarbons	**-0.2**	**2.2**	**7.1**	**5.0**	**12.6**	**12.7**
Metallic mining	-3.6	2.1	6.4	3.9	12.9	12.3
Hydrocarbons	18.1	2.3	9.4	9.6	11.3	14.4
Manufacturing	**5.6**	**1.3**	**5.6**	**5.0**	**6.0**	**5.7**
Raw materials	12.3	-6.5	4.9	3.6	3.9	3.7
Non-primary industries	4.4	2.7	5.8	5.2	6.4	6.0
Non-primary industries	**7.4**	**5.2**	**5.9**	**5.9**	**6.5**	**6.1**
Electricity and water	**3.4**	**15.2**	**9.6**	**10.5**	**8.2**	**8.2**
Commerce	**8.8**	**6.7**	**5.8**	**6.4**	**5.9**	**6.0**
Other services	**8.3**	**7.2**	**6.3**	**6.6**	**5.9**	**6.1**
GDP	**6.9**	**6.3**	**6.2**	**6.3**	**6.3**	**6.3**
Memo:						
Primary GDP	4.4	1.7	5.2	4.0	6.9	6.8
Non-Primary GDP	7.4	7.1	6.4	6.7	6.2	6.2

IR: Inflation report.
* Forecast.

28. Production in the **primary sectors** in 2012 grew 1.7 percent, a lower rate than the one registered in 2011 (4.4 percent), reflecting lower growth in the sectors of livestock, fishing, and manufacturing based on raw materials. The forecast of the growth of the primary sectors in 2013 has been revised downwards from 5.2 (Inflation Report of December) to 4.0 percent.

    The **agricultural sector** grew 5.1 percent in 2012 with noteworthy high volumes of potatoes, rice, and meat, which accounted for 57 percent of the growth of the sector. Among other products for the domestic market, a historically high production of bananas, onions, tangerines, oranges, and sweet potatoes, was also observed. In 2013, the sector would grow 3.5 percent, recording a lower rate than the one estimated in our December Inflation Report, due mainly to a lower production of coffee associated with the plague called coffee rust.

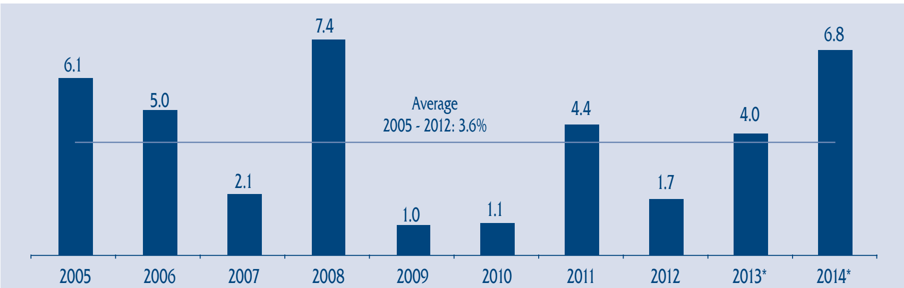
    The growth rate of the **fishing sector** in 2012 (-11.9 percent) reflects mainly the lower quota of anchovy catch allowed for industrial consumption. A lower level of anchovy catch than the one estimated in our previous report is foreseen in 2013 (3.3 million tons instead of 3.9 million tons) given that a lower quota would be established for the catch of anchovy in the North - Central zone. However, since this would be corrected by the end of 2013, the extraction of anchovy in 2014 would recover showing levels of 3.6 million tons.

Moreover, the growth of the **metal mining sector** in 2012 (2.1 percent) is explained by a higher production of copper (due to the expansion of Antamina), zinc, and silver, which offset the lesser extraction of gold from artisanal mining in Madre de Dios.

The growth forecast of this sector in 2013 has been revised downwards compared to the one estimated in our previous inflation report due to a lower expected production of gold, which has been revised down from 5.1 to 4.7 million ounces as a result of the announced reduction of up to 25 percent in the production of Yanacocha as well as of lower activity in Madre de Dios. However, this decline would be in part offset by a higher extraction of copper (1.3 million fine metric tons) resulting from a full year's operation of the Antapaccay project (160 tons) and, to a lesser extent, from the contribution of Antamina's expansion. Production in 2014 would grow 12.3 percent due mainly to a higher production of copper (1.7 million fine metric tons) associated with the onset of operations at the new projects of Toromocho, Las Bambas, and Constancia.

As regards the **hydrocarbons** subsector, a slightly higher growth rate than the one estimated in our previous report is foreseen in this sector in 2013 (9.6 percent instead of 9.4 percent). This increase would be associated with the higher production of natural gas projected in Repsol's Lot 57 in the Ucayali basin, which has reserves estimated at between 1 and 2 trillion cubic feet, with an estimated production plan of 155 million cubic feet per day. This increase would be offset by the production of lower oil of Savia Perú in Lot Z-2B in Piura relative to the production estimated in December.

Graph 42
PRODUCTION IN PRIMARY SECTORS: 2005 - 2014
(Real % change)

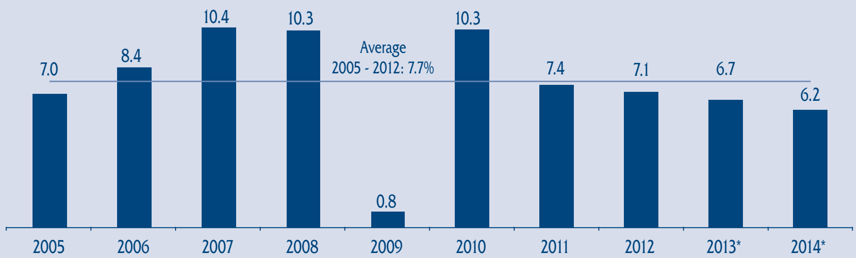


* Forecast.

29. The **non-primary sectors** grew 7.1 percent in 2012, mainly due to the evolution of services, construction, and trade. A gradual slowdown in the growth rate of the non-primary sectors is foreseen in the forecast horizon, in line with the moderation of growth in domestic demand. The growth of non-primary manufacturing would be associated with both the growth of domestic demand and the evolution of non-

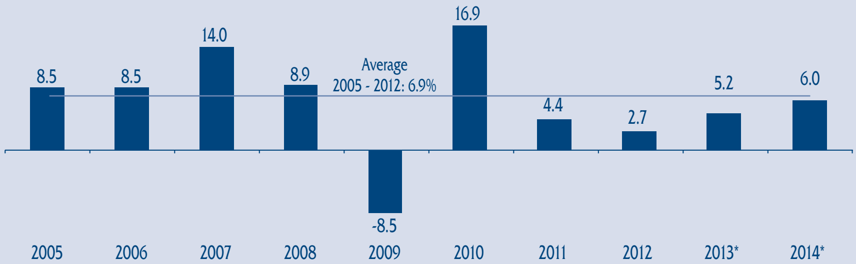
traditional exports, associated in turn with global demand which is expected to recover in 2014 with a positive effect on this sector. The lower dynamism of textile exports would contribute to moderate the growth of non-primary manufacturing. The construction sector would continue to grow, although showing more moderate rates supported by the increased construction of housing complexes, shopping malls, and road and public infrastructure works, both in Lima and in the rest of the country.

Graph 43
PRODUCTION IN NON PRIMARY SECTORS: 2005 - 2014
(Real % change)



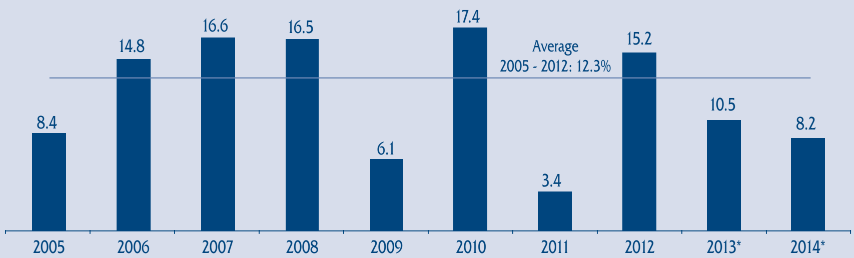
* Forecast.

Graph 44
NON-PRIMARY MANUFACTURING: 2005 - 2014
(Real % change)



* Forecast.

Graph 45
CONSTRUCTION: 2005- 2014
(Real % change)



* Forecast.

Box 2
INFRASTRUCTURE AND ECONOMIC GROWTH

There is a consensus in the literature on economic growth that one important determinant of long-term growth in a market economy is an appropriate provision of infrastructure since infrastructure improves the productivity of factors employed by the private sector. However, the magnitude of this impact is subject to a degree of uncertainty, as reflected in the wide range of different levels of elasticity estimated in the major studies on the subject.

SUMMARY OF MAJOR STUDIES

Study	Evaluated countries	Sample	Infrastructure variable	Methodology	Elasticity
Aschauer (1989)	USA	1949-1985	Public expenditure in non military capital	OLS	0.39
Munnell (1990)	USA	1947-1988	Public expenditure on infrastructure	OLS	0.34
Canning (1999)	57 developing countries	1960-1990	Telecommunications	Fixed effect panel	0.139
Easterly and Rebelo (1993)	28 developing countries	1970-1988	Transport and telecommunications expenditure	OLS	0.16
Esfahani and Ramírez (2003)	75 countries	1965-1995	Telecommunications and energy	OLS 2 stages	0.091 and 0.156
Vasquez and Bendezú (2008)	Peru	1940- 2003	Roads	Cointegration	0.218
Rivera and Toledo (2004)	Chile	1975-2000	Investment in infrastructure sector	Cointegration	0.16
Sanchez-Robles (1998)	57 countries, 19 countries in Latin America	1970-1985	Infrastructure index	OLS	0.009 0.012
Davarajan, Swaroop and Zu (1996)	43 developing countries	1970-1990	Transport and telecommunications expenditure	Fixed effect panel	-0.025
Calderón and Serven (2004b)	101 countries	1960- 2000	Infrastructure index	Fixed effect panel GMM	0.0195 0.0207
Duggal, Saltzman and Klein (1999)	USA	1960-1989	Public expenditure on roads and structures	OLS, non-linear specification	0.27
Garcia-Milá, McGuire and Porter (1996)	USA, 48 states	1971-1983	Public expenditure on water and sewage system and highways	Fixed effect panel	-0.058 and -0.029

OLS: Ordinary least squares.
GMM: Generalized method of moments.
Source: Urrunaga, R. and Aparicio, L (2012), “Infraestructura y crecimiento económico en el Perú”, Santiago de Chile, Revista CEPAL N° 107.

Another branch of the economic literature examines the distributive impact generated by access to infrastructure, mainly through two mechanisms: increasing the value of the assets poor people have (i.e., land or human capital), and reducing the transaction costs (e.g., transport and logistics costs) they incur in to have access to markets. Both factors increase the income of the poorest groups and improve income distribution, which may have additional positive effects on long-term growth. Some empirical studies have established that both the quantity and the quality of infrastructure are negatively related to income inequality and that the quantity of infrastructure is more important than the quality of infrastructure in developing countries (Estache, Foster and Wodon 2002[1], Calderón and Chong 2004[2]).

1 Estache, Foster and Wodon 2002, “Cómo hacer que la reforma de la infraestructura en América Latina favorezca a los pobres”, Santiago de Chile, Revista Cepal No. 78, December 2002.

2 Calderón, C. and Chong, A., 2004. “Volume and Quality of Infrastructure and the Distribution of Income: An Empirical Investigation.” Review of Income and Wealth 50, 87-105.

Analyzing information on 100 countries in the period 1960-2000, Calderón and Servén (2004)[3] find that both the quantity and the quality of infrastructure have a positive impact on economic growth and income distribution.

According to these authors, if Peru reached the quantity and quality of the infrastructure stock that Costa Rica has, the potential GDP per capita in Peru would increase by 3.5 percentage points, the amount of infrastructure accounting for 3.0 percentage points of this increase. Moreover, if it achieved the levels of infrastructure observed in the Republic of Korea, the potential GDP per capita would increase by 5 points, of which 4.0 points would be explained by the amount of infrastructure.

POTENTIAL INCREASES IN PER CAPITA GDP GROWTH DUE TO IMPROVEMENTS IN THE QUANTITY AND QUALITY OF INFRASTRUCTURE
(%)

	Improvement to reach the highest level in the first country in Latin America and the Caribbean (Costa Rica)			Improvement to reach the median of East Asian Tigers (South Korea)		
	Quantity	Quality	Total	Quantity	Quality	Total
Argentina	1.3	0.4	1.7	2.2	0.9	3.2
Bolivia	3.8	0.5	4.3	4.8	1.0	5.8
Brazil	1.5	1.4	2.9	2.4	1.9	4.4
Chile	1.3	0.0	1.3	2.3	0.6	2.8
Colombia	1.9	1.2	3.1	2.9	1.7	4.6
Costa Rica			0.0	1.0	0.5	1.5
Ecuador	2.0	1.0	3.0	3.0	1.5	4.5
El Salvador	1.6	0.4	2.1	2.6	1.0	3.6
Guatemala	3.3	0.4	3.7	4.2	0.9	5.2
Honduras	3.1	1.1	4.2	4.1	1.6	5.7
Mexico	1.4	0.2	1.7	2.4	0.8	3.2
Nicaragua	3.4	1.4	4.8	4.4	1.9	6.3
Panama	1.4	0.2	1.5	2.4	0.7	3.1
Peru	**3.0**	**0.6**	**3.5**	**4.0**	**1.1**	**5.0**
Dominican Republic	1.3	0.1	1.4	2.3	0.7	2.9
Uruguay	0.7	0.4	1.1	1.7	0.9	2.6
Venezuela	1.1	0.4	1.4	2.0	0.9	2.9

Source: Calderón and Servén 2004b.

In a study specifically on Peru, Vasquez and Bendezú (2008)[4] found that a 1 percent increase in road infrastructure has an impact of 0.218 percentage points on the national GDP. Furthermore, Urrunaga and Aparicio (2012)[5] analyze the regional impact of infrastructure and find that public infrastructure (roads, electricity, and telecommunications) is relevant to explain transitory differences in the regional output, even though this evidence is not conclusive in terms of the long term regional impact.

On the other hand, Richard Webb's study entitled "Conexión y despegue rural"[6] provides evidence of the progress observed in rural incomes and of the progress made in reducing the levels of isolation of rural populations since the 1990s and more significantly in the last decade as a result

3 Calderón, C. and L. Servén (2004b), "The effects of infrastructure development on growth and income distribution", Documentos de trabajo, Nº 270, Santiago de Chile, Banco Central de Chile, September.

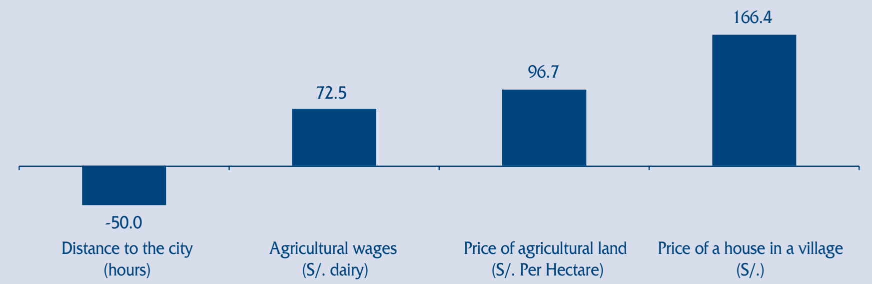
4 Vásquez, A. and L. Bendezú (2008), Ensayos sobre el rol de la infraestructura vial en el crecimiento económico del Perú, Lima, Consorcio de Investigación Económica y Social (CIES) y Banco Central de Reserva del Perú (BCRP).

5 Urrunaga, R. and Aparicio, L (2012), "Infraestructura y crecimiento económico en el Perú", Santiago de Chile, Revista CEPAL N° 107.

6 Webb, Richard (2013), Conexión y Despegue Rural, Universidad San Martín de Porres.

of the direct connection generated by the new communication platform established through the improvements made in the road networks and through the massive use of cell phones and the internet. Comparing indicators for a sample of 176 rural districts between 2001 and 2011, one can see that traveling time to the nearest city has declined by 50 percent, that agricultural wages have increased by 72.5 percent, that the price of agricultural land has increased by 96.7 percent, and that the price of a house in a village has increased by 166 percent. All of these things have contributed not only to connect territories with more dynamic markets, but also to the implementation of a more rapid electrification process, to improve literacy, and to increase people's access to a national identity document. In addition to this, indirect connection also explains the improvement observed in the quality of public education and health services.

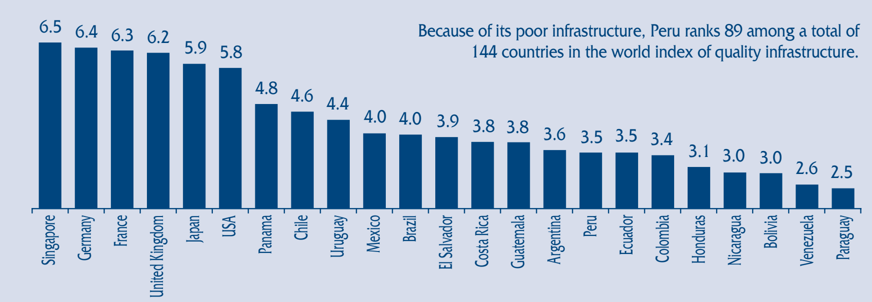
RURAL INDICATORS
(% change 2011/2001)



Source: Conexión y Despegue Rural. Richard Webb, febrero 2013. Universidad San Martín de Porres.

The provision of infrastructure in Peru has grown in the last two decades. According to PROINVERSIÓN, committed investments for infrastructure from privatization and concession processes amounted to US$ 6.87 billion in 1991-1999, while in 2000-2012 the amount of investments committed for infrastructure projects was US$ 14.01 billion (road networks, IIRSA projects, ports, airports, electricity transmission lines, hydro-electrical power plants and natural gas power plants, among others).

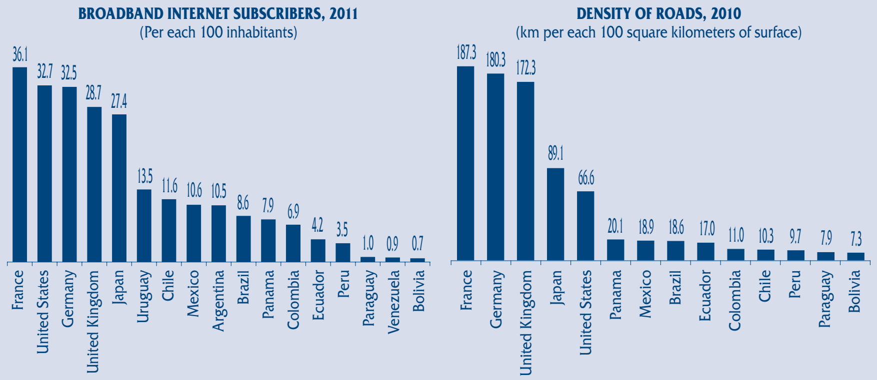
INDEX OF QUALITY INFRASTRUCTURE
(1=underdeveloped. 7=efficient)



Source: Global Competitiveness Report 2012-2013. World Economic Forum.

Despite these favorable developments, the availability of quality infrastructure in Peru is still lower than the one observed in other countries of the region. According to the World Economic Forum's index of quality infrastructure (2012-2013), with a rating of 3.5 (of a maximum score of 7 points), Peru's infrastructure is below that of several countries in the region, such as Mexico, Brazil, Uruguay, and Argentina, but above that of Colombia.

The country's infrastructure constraints are evidenced in the low penetration of broadband Internet (3.5 lines per 100 inhabitants versus 11.6 lines per 100 inhabitants in Chile or versus 36.1 lines per 100 inhabitants in France) and the low density of roads observed nationwide (9.7 km/100 square kilometers of surface). This situation constrains connectivity in the country because it limits the scope of the market and people's capacity to benefit from favorable exchanges.



Source: World Development Indicators (WDI), World DataBank.

The development of infrastructure in the country also faces specific difficulties not observed in other sectors, due either to the higher amounts that need to be invested at the beginning of a project or due to the increased time required to have a return on an investment. As a result, many projects have a long period of implementation, as well as construction risks and benefits concentrated in the medium and the long terms, risks of social disapproval in the regions involved in the projects, environmental risks, and uncertainty about the demand these projects will have.

Therefore, it is essential to promote the development of infrastructure and to continuously improve the institutional framework and institutional practices in the concessions of infrastructure projects to be carried out in the country through private-public partnerships (PPPs). According to The Economist Intelligence Unit[7], together with Chile, Brazil and Mexico, Peru offers the best conditions for the development of PPPs in the region[8].

The country should also benefit from the advantages it has in attracting capital (macroeconomic fundamentals, investment opportunities) and from the favorable external conditions (low international interest rates, abundant liquidity) to obtain low-cost international financial

7 Infrascopio 2012 América Latina y el Caribe, Published on behalf of FOMIN-BID, February 2013.

8 This assessment included the legal framework, the institutional framework, the operational maturity, the general climate for investments, and financial conditions.

resources in advantageous conditions to develop infrastructure that promotes economic growth.

Moreover, a greater participation of the private sector in the provision of infrastructure should be promoted by the sub-national governments. Co-financing infrastructure projects through PPPs, regional and local governments can make a better use of the increased resources they obtain from the mining royalty (canon) and other royalties and also improve their low budget execution. The participation of the private sector in the provision of infrastructure at the regional and local levels should also be promoted through the mechanism of works-for-taxes.

Several measures have been taken recently to promote the development of PPPs, including the publication of the regulations establishing the priority of co-financed private initiatives; the possibility of easing the legal terms on PPPs, which can now be modified in order to expedite concession processes, and reinforcing PROINVERSION as an institutional promoter of private investment. These measures are expected to facilitate the development of infrastructure and to boost concession processes through PPPs.

III. Balance of Payments

30. In 2012 the **current account** of the balance of payments recorded a deficit of 3.6 percent of GDP (US$ 7.1 billion), higher than the deficit of 1.9 percent of GDP observed in 2011. This balance reflects the decline in the surplus trade by a little over 50 percent, from US$ 9.3 billion in 2011 to US$ 4.5 billion in 2012, as a result of the decline in the terms of trade, a lower growth in the volume of exports, and a high growth of imports in a context of expansion of domestic demand.

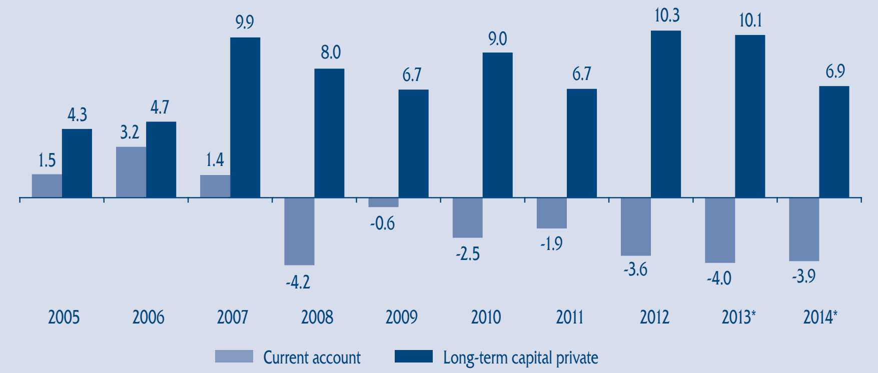
    Notwithstanding, external financing largely exceeded the requirements associated with the current account deficit because a significant inflow of long-term private capital amounting to US$ 20.6 billion was registered in the year. This substantially higher capital inflow than that observed in 2011 (US$ 12.0 billion) was associated with greater direct investment for the implementation of major investment projects as well as with local companies' increased financing in the international debt markets. Thus, in 2012 the balance of payments registered a positive balance of US$ 14.8 billion (US$ 4.7 billion in 2011).

Table 19
BALANCE OF PAYMENTS
(Millions of US$)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
I. CURRENT ACCOUNT BALANCE	**-3,341**	**-7,136**	**-7,990**	**-8,877**	**-7,983**	**-9,385**
% of GDP	*-1.9*	*-3.6*	*-3.7*	*-4.0*	*-3.4*	*-3.9*
1. Trade Balance	9,302	4,527	3,965	2,771	5,439	3,002
a. Exports	46,268	45,639	48,425	47,082	54,608	51,913
b. Imports	-36,967	-41,113	-44,460	-44,311	-49,169	-48,911
2. Services	-2,132	-2,258	-2,020	-2,063	-2,422	-2,502
3. Investment income	-13,710	-12,701	-13,415	-13,069	-14,611	-13,670
4. Current transfers	3,200	3,296	3,480	3,485	3,610	3,784
Of which: Remittances	2,697	2,788	2,959	2,964	3,073	3,218
II. FINANCIAL ACCOUNT	**8,065**	**21,963**	**12,990**	**21,377**	**11,483**	**13,385**
Of which:						
1. Private sector	7,185	20,277	12,050	21,168	11,670	13,172
a. Long term	9,620	16,349	10,545	16,999	10,115	11,072
b. Short term 1/	-2,435	3,929	1,505	4,169	1,556	2,100
2. Public sector 2/	880	1,685	940	209	-187	213
III. BALANCE OF PAYMENTS (=I+II)	**4,724**	**14,827**	**5,000**	**12,500**	**3,500**	**4,000**
Memo:						
GDP (Billions of US$)	177	200	218	221	237	240

1/ Includes erros and omissions.
2/ Includes exceptional financing.
IR: Inflation report.
* Forecast.

Graph 46
CURRENT ACCOUNT AND LONG-TERM PRIVATE CAPITAL INFLOWS 1/: 2005 - 2014
(% of GDP)



1/ Includes foreign direct investments, portfolio investment and long term disbursements.
* Forecast.

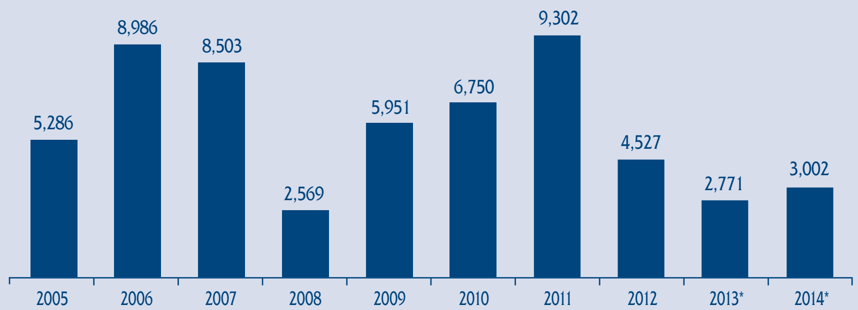
31. The current account deficit forecast for **2013** has been revised upwards from 3.7 percent of GDP in our previous report prior to 4.0 percent of GDP, in line with the revision of the growth of domestic demand. This larger deficit would be associated with the lower trade surplus foreseen in this year, partially offset by lower income factor expenditure given the lower profits expected in the mining sector. Moreover, the deficit in the current account in **2014** has also been revised upwards from 3.4 to 3.9 percent of GDP.

32. In 2012 the **trade balance** registered a balance of US$ 4.5 billion, a substantially lower balance that recorded in 2011. The trade balance was affected by the low dynamism of primary sectors which resulted in almost zero growth in the volume of traditional exports, as well as by the contraction observed in the prices of our major export metals and by the rise in the price of imported food.

    The trade surplus estimated for 2013 is revised downwards from US$ 4.0 billion (Inflation Report of December) to US$ 2.8 billion given that smaller volumes of exports, both of traditional and non-traditional products, larger volumes of imports, and a decline in the price of copper and gold are anticipated.

    Along the same lines, the estimated trade balance for 2014 is revised downwards from US$ 5.4 billion to US$ 3.0 billion as a result of a slower growth in the volume of traditional exports, especially mining products.

Graph 47
TRADE BALANCE: 2005-2014
(Millions of US$)



* Forecast.

Table 20
TRADE BALANCE
(Millions of US$)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
Exports	**46,268**	**45,639**	**48,425**	**47,082**	**54,608**	**51,913**
Of which:						
Traditional products	35,837	34,247	36,081	35,179	40,915	38,564
Non-traditional products	10,130	11,047	12,126	11,504	13,475	12,920
Imports	**36,967**	**41,113**	**44,460**	**44,311**	**49,169**	**48,911**
Of which:						
Consumer goods	6,692	8,247	9,353	9,184	10,645	10,560
Inputs	18,255	19,256	19,945	20,485	21,659	21,953
Capital goods	11,665	13,356	14,950	14,377	16,730	15,986
TRADE BALANCE	**9,302**	**4,527**	**3,965**	**2,771**	**5,439**	**3,002**

IR: Inflation report.
* Forecast.

33. **Exports** in 2012 amounted to US$ 45.6 billion, a figure lower by US$ 629 million than the one recorded in 2011, due mainly to the drop observed in gold trading companies' sales of gold as a result of the measures implemented by the government with the aim of eradicating informal gold mining and informal trading. The volume of gold exports registered through customs decreased from 6.4 to 5.7 million ounces between 2011 and 2012, this difference accounting for a value of exports close to US$ 1.2 billion. Another factor that explains the decline in exports is the lower prices of some mining commodities, such as copper, zinc and lead. This was partially offset by higher volumes of exports of traditional products, with the exception of exports of textiles and fish products to the United States and Europe which registered a major decline.

Table 21
TRADE BALANCE
(% change)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
1. Value:						
a. Exports	30.1	-1.4	5.7	3.2	12.8	10.3
Traditional products	29.5	-4.4	4.6	2.7	13.4	9.6
Non-traditional products	32.6	9.1	10.5	4.1	11.1	12.3
b. Imports	28.3	11.2	7.5	7.8	10.6	10.4
2. Volume:						
a. Exports	8.5	2.2	7.8	4.2	10.7	9.5
Traditional products	5.2	0.4	7.5	3.9	11.6	9.6
Non-traditional products	20.2	9.0	8.3	5.2	8.3	9.1
b. Imports	12.8	9.5	9.1	9.2	9.6	9.6
3. Price:						
a. Exports	20.0	-3.3	-1.9	-1.0	1.9	0.7
Traditional products	22.9	-4.6	-2.7	-1.1	1.6	0.0
Non-traditional products	10.4	0.3	2.0	-1.0	2.6	3.0
b. Imports	13.8	1.7	-1.5	-1.3	0.9	0.7

IR: Inflation report.
* Forecast.

34. In **2013** exports would amount to US$ 47.1 billion, a lower amount than the one estimated in our December report (US$ 48.4 billion) given that the growth rate of the volume of exports has declined from 7.8 percent (December report) to 4.2 percent. This decline would be associated with lower exports of gold due to the contraction expected in the production of Yanacocha, as well as with lower exports of coffee, fish meal, and with lower exports of textile products to Venezuela. It should be pointed out that the operations of the Antapaccay project, as well as the implementation of Trevali's Santander project (zinc), Minsur's Pucamarca (gold), and Volcan's Alpamarca (silver) are expected to have a positive impact on the growth of exports this year.

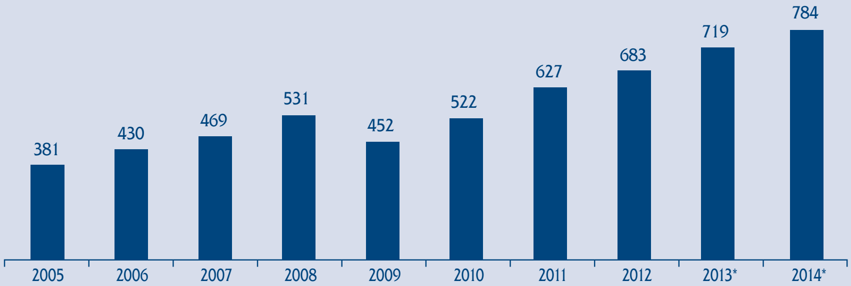
Graph 48
EXPORTS OF GOODS: 2005-2014
(Billions of US$)

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

35. Exports in **2014** would amount to US$ 51.9 billion, less than expected in our December report (US$ 54.6 billion), as a result of the expected decline in gold production due to the lower content of mineral obtained in current operations as well as a result of the drop in the price of gold. This forecast takes into account the

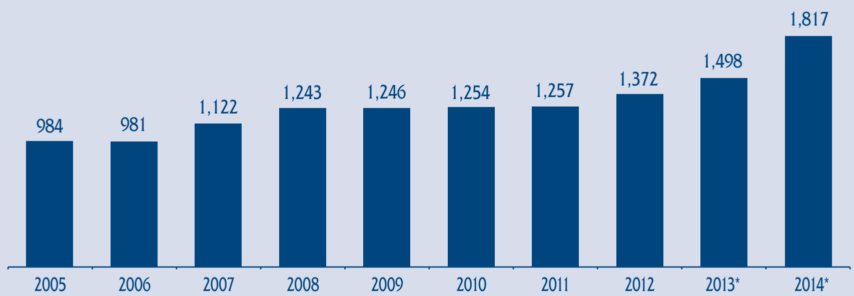
onset of operations in the projects of Toromocho (Junín), Las Bambas (Apurimac), and Constancia (Cusco), which together are projected to have a production of over 700 thousand FMT of copper when operating at full capacity.

Graph 49
NON TRADITIONAL EXPORTS VOLUME
(Index 1994=100)



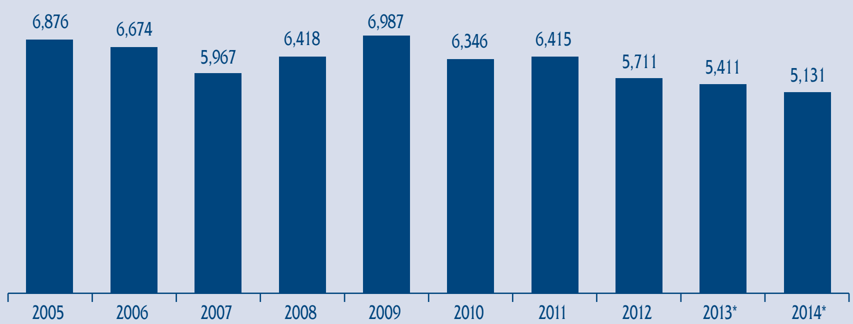
* Forecast.

Graph 50
VOLUME OF COPPER EXPORTS
(Thousands of FMT)



* Forecast.

Graph 51
VOLUME OF GOLD EXPORTS
(Thousands of ounces)

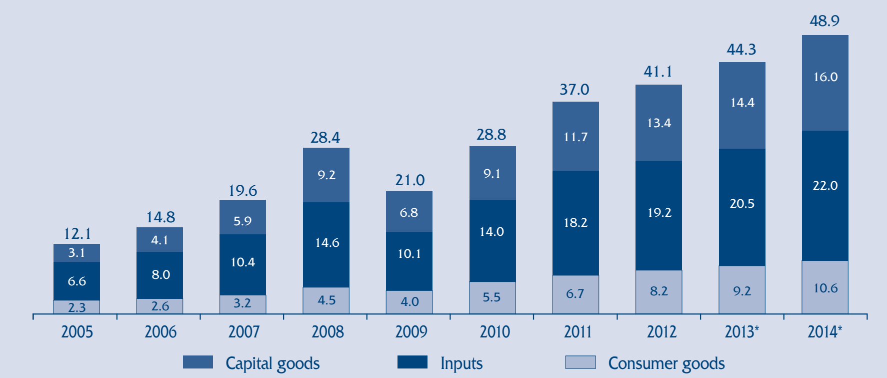


* Forecast.

36. **Imports** in 2012 totaled US$ 41.1 billion, a figure 11.2 percent higher than the value imported in 2011. This reflects the expansion of domestic demand, which encouraged particularly the volume of imports of consumer goods and capital goods.

As a result of increased dynamism in economic activity, in 2013 imports would grow 9.2 percent in terms of volume compared to 2012 –slightly higher than foreseen in December– and would amount to US$ 44.3 billion. This growth would be partially offset by a slower pace of growth in imports of inputs due to the slowdown expected in the non-primary industry. In 2014 imports are estimated to amount to US$ 48.9 billion, in line with a growth in the volume of imports of 9.6 percent, as estimated in our December report.

Graph 52
IMPORTS OF GOODS: 2005 - 2014
(Billions of US$)



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

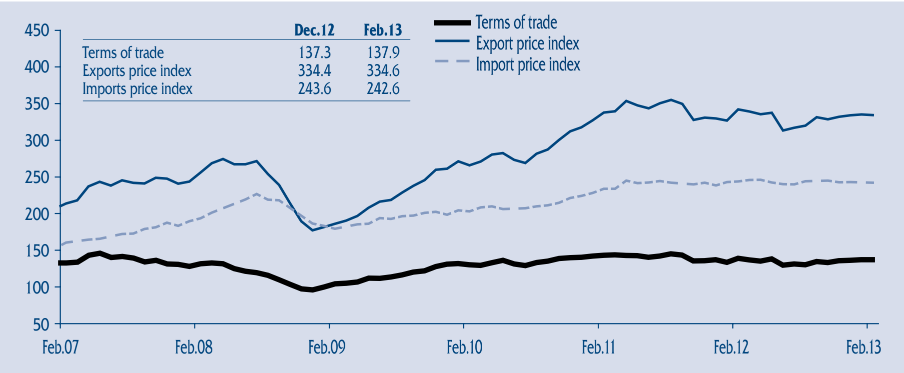
Terms of trade and commodity prices

37. In 2012, the terms of trade fell about 5 percent due to the drop registered in export prices and to the rise registered in import prices. The annual fall in the terms of trade reflected mainly the evolution of imports and exports in the first semester, when some international prices of metals dropped. In the second half of the year, the terms of trade recovered in part, in line with the downward correction observed in food prices. It is estimated that the terms of trade will increase slightly in the rest of the year and imply an increase of 0.3 percent in 2013.

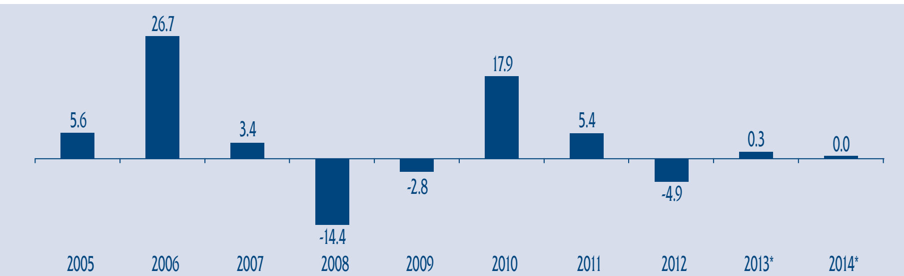
Table 22
TERMS OF TRADE: 2011 - 2014
(Annual average data)

	2011	2012	2013*			2014*	
			Jan-Feb	IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
Terms of trade	**5.4**	**-4.9**	**0.6**	**-0.5**	**0.3**	**1.0**	**0.0**
Price of exports	**20.0**	**-3.3**	**0.1**	**-1.9**	**-1.0**	**1.9**	**0.7**
Copper (US$ cents per pound)	400	361	366	365	359	366	360
Zinc (US$ cents per pound)	100	88	94	90	91	94	93
Lead (US$ cents per pound)	109	94	107	98	103	99	103
Gold (US$ per ounce)	1,570	1,670	1,650	1,720	1,608	1,720	1,600
Price of imports	**13.8**	**1.7**	**-0.5**	**-1.5**	**-1.3**	**0.9**	**0.7**
Oil (US$ per barrel)	95	94	95	90	93	90	92
Wheat (US$ per ton)	280	276	281	331	276	324	280
Maize (US$ per ton)	262	273	280	276	256	245	222
Soybean oil (US$ per ton)	1,191	1,125	1,085	1,096	1,104	1,125	1,110

Graph 53
TERMS OF TRADE, EXPORT AND IMPORT PRICE INDICES: JANUARY 2007 - FEBRUARY 2013
(1994 =100)



Graph 54
TERMS OF TRADE
(% change)



* Forecast.

During the first six weeks of 2013, commodity prices were favored by expectations of an economic recovery in the major developed economies based on positive indicators of activity in the United States and China, as well as on the favorable of stock markets after the publication of mostly favorable corporate results.

This trend reversed as from the second half of February due to uncertainty about the situation in the Eurozone following the elections in Italy, the lack of agreement on fiscal matters in the United States, and the measures implemented in China to reduce pressures in the housing market as well as due to China's announcement of targets for 2013.

Copper

38. In 2012, the price of **copper** dropped 9.9 percent, reaching an annual average price of US$ 3.60 per pound. In the first two months of 2013, the price of this metal increased 1.6 percent and closed with a monthly average price of US$ 3.66 per pound at the end of February. However, the price of copper has dropped rapidly since the second week of February, closing the month at US$ 3.55 per pound.

    The correction in the price of copper observed since the second half of February was mainly associated with the Chinese Government's decision to implement measures to curb speculation in the real estate market. This has taken place in a context of a better outlook for the production of refined copper and increased mine production that started in mid-2012, especially in Chile and Indonesia, which has reflected in an increase in global copper inventories, as evidenced in the high levels of inventories that continue to be observed in the Shanghai warehouses.

    Thus, a higher than expected surplus and high levels of inventories are foreseen in the copper market at the beginning of the year in the forecast horizon, which would offset the slight increase expected in China's demand. In line with these factors, it is estimated that the price of copper will be slightly below the level projected in our last Inflation Report.

Graph 55
COPPER: JANUARY 2007 - DECEMBER 2014
(ctv. US$/pd.)

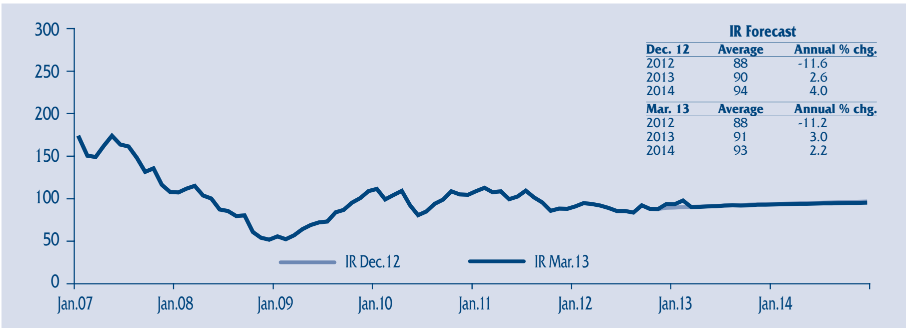
Zinc

39. Showing an annual drop of 11.2 percent, in 2012 **zinc** recorded an average price of US$ 0.88 per pound. In the first two months of 2013, the price of zinc recovered 4.4 percent and closed February with a monthly average level of US$ 0.97 per pound.

The decline in the price of zinc observed in 2012 reflected loose conditions in the world market, which showed a global surplus for the sixth consecutive year and rising global inventories, in line with the increase of mining production and the drop of demand, affected by the economic downturn in Europe and a lower demand in China. In the first months of 2013, this trend reversed anticipating a reduction in the production of refined zinc (in response to low prices). However, the prices were influenced in mid-February by the events that affected the Eurozone, the United States, and China which have been mentioned above.

The fundamentals of the zinc market continue to show loose market conditions, although it is estimated that the production of refined zinc production in the medium term will not recover at the same rate as the growth in consumption, which will generate upward pressures. In the forecast horizon the international price of zinc is expected to remain relatively stable and at similar levels to those estimated in our previous Inflation Report.

Graph 56
ZINC: JANUARY 2007 - DECEMBER 2014
(ctv. US$/pd.)



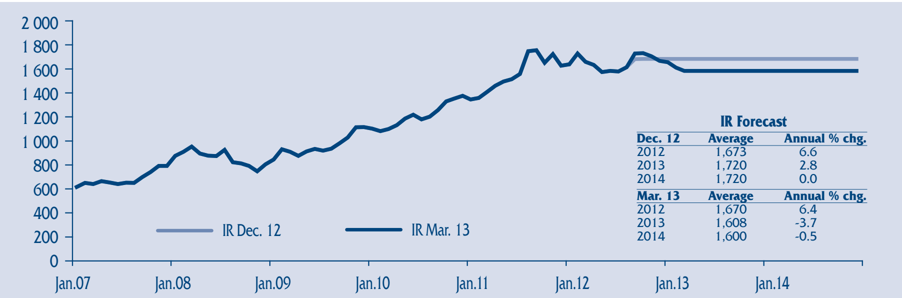
Gold

40. In 2012 the price of gold rose 6.4 percent, closing the year with an average price of US$ 1,670 per troy ounce. However, in the first two months of 2013, the price of gold fell 3.4 percent and registered a monthly average price of US$ 1,627 per troy ounce at end February.

The downward trend in the price of gold was supported by the record sales of investment funds carried out by investors that recomposed their portfolio in favor of variable income securities. This investment demand shrank after having grown 51 percent in 2012. Another factor that affected the price of gold was the lower demand of India, particularly of Indian jewelers, and the stagnation of demand from China. The demand in India would have been affected after the tax on gold imports was raised.

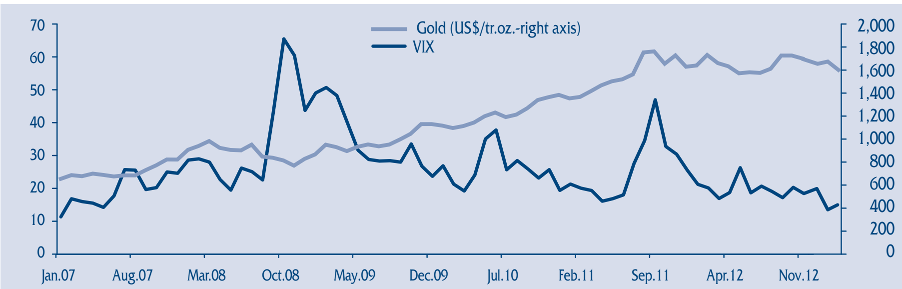
The price of gold is estimated to remain around its current levels and below the levels estimated in our previous report. In line with the data available today, this forecast is supported by expectations of low global inflation. However, risk aversion and the global demand for gold as a hedge asset could increase should some of the risk factors outlined in this report occur.

Graph 57
GOLD: JANUARY 2007 - DECEMBER 2014
(US$/tr.oz.)



Dec. 12	Average	Annual % chg.
2012	1,673	6.6
2013	1,720	2.8
2014	1,720	0.0
Mar. 13	**Average**	**Annual % chg.**
2012	1,670	6.4
2013	1,608	-3.7
2014	1,600	-0.5

Graph 58
GOLD PRICE AND S&P-500 VIX INDEX
(January 2007 - February 2013)



Source: Bloomberg.

Financial account

41. In 2012 the **long-term financial account of the private sector** amounted to US$ 16.3 billion, which represents a flow of 8.2 percent of GDP. This amount was higher than in 2011 due mainly to higher foreign direct investment in the country and to the increased funding obtained by the local non-financial sector through

bonds issued in international markets. This was in part offset by the higher capital outflows carried out by local institutional investors.

Table 23
PRIVATE SECTOR FINANCIAL ACCOUNT FLOWS
(Millions of US$)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
I. ASSETS	**-1,298**	**-2,477**	**-4,123**	**-4,209**	**-4,141**	**-4,396**
Direct investment abroad	-113	57	0	0	0	0
Portfolio investment abroad	-1,185	-2,534	-4,123	-4,209	-4,141	-4,396
II. LIABILITIES	**10,918**	**18,826**	**14,668**	**21,209**	**14,256**	**15,468**
Foreign direct investment in the country	8,233	12,240	8,171	10,841	9,336	9,404
Long-term loans	2,787	5,011	4,182	6,072	2,554	3,694
Financial sector	1,696	2,988	3,365	3,365	1,666	1,666
Non-financial sector	1,091	2,023	817	2,706	888	2,028
Foreign portfolio investment in the country	-102	1,575	2,316	4,295	2,366	2,369
III. TOTAL (I+II)	**9,620**	**16,349**	**10,545**	**16,999**	**10,115**	**11,072**
% of GDP	*5.4*	*8.2*	*4.8*	*7.7*	*4.3*	*4.6*

IR: Inflation report.
* Forecast.

In 2013 the long-term private sector financial account would amount to US$ 17.0 billion, a similar amount to the one registered in 2012 but higher than the one estimated for this year in our December report (US$ 10.5 billion). The private financial account has been revised upwards due to the increased flow of external funding expected for the implementation of some major investment projects, such as Toromocho, whose total investment would increase from US$ 2.2 billion to US$ 3.5 billion. A greater foreign portfolio investment is also expected both as a result of bonds issued abroad and as a result of an increased participation of foreign investment funds in the local market. This greater capital inflow would be partially offset by increased capital outflows of the private administrators of pension funds (AFPs) given that the limit for their investment abroad was raised from 30 percent to 34 percent in February this year.

A positive flow of US$ 11.1 billion, equivalent to 4.6 percent of GDP, is estimated in 2014. This slightly higher flow than the one forecast in our previous report would be explained by the increase in the requirement of external funding for the implementation of private investment projects and by the non-financial sector's replacement of domestic funding by external funding in a context of favorable conditions and high liquidity in international financial markets. A more moderate growth would be observed in the financial account in 2014 compared to 2013 due in part to the completion of the construction stage of some major investment projects scheduled to start operating that year.

Graph 59
PRIVATE SECTOR EXTERNAL FINANCING 1/
(% of GDP)

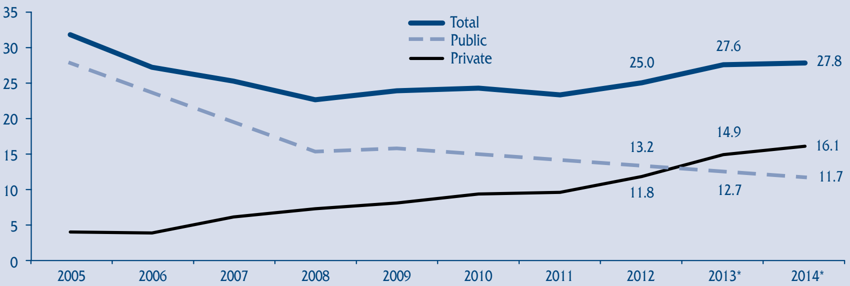
1/ Includes foreign direct investments , foreign portfolio investment, and long-term disbursements.
* Forecast.

42. On the other hand, in 2012 the **public sector financial account** had a positive flow of US$ 1.7 billion. This flow is mostly explained by non-residents' acquisition of sovereign bonds. It is worth pointing out that the participation of non-residents increased from 45 percent in 2011 to 55 percent in 2012.

    In 2013 the public sector financial account would show a positive flow of US$ 209 million, a figure that contrasts with the flow of US$ 940 million estimated for this year in our December report. This is explained by higher outlays associated with the prepayment of the debt programmed to be made in the first semester (US$ 1.68 billion), offset by non-residents purchases of sovereign bonds and by the placement of bonds by Fondo MiVivienda for a total of US$ 500 million.

43. With these flows, the balance of the medium-term and the long-term external debt would increase from 25.0 percent of GDP in 2012 to 27.8 per cent in 2013. The growing trend observed in the external indebtedness of the private sector –up from 11.8 percent of GDP in 2012 to 16.1 percent of GDP in 2014– would imply for the first time that the external debt of the private sector is higher than the public sector debt. Including the domestic bonds held by non-residents, it is projected that the latter would decline from 13.2 percent of GDP in 2012 to 11.7 percent of GDP in 2014.

Graph 60
MEDIUM AND LONG TERM EXTERNAL DEBT STOCK
(% of GDP)



* Forecast.

44. In 2012 the **flow of short-term foreign capital** showed a reversal from an outflow of US$ 1.3 billion in 2011 to a positive flow of US$ 2.2 billion. A downward path is foreseen in this aggregate in the forecast horizon since an inflow of US$ 1.3 billion and US$ 700 million of banks' liabilities is projected for 2013 and 2014, respectively. These amounts would be lower than the inflow observed in 2012 (US$ 2.02 billion) due to the moderation anticipated in external funding as a result of the international context and the reserve requirement measures taken by the Central Bank to offset the impact of capital inflows on the growth of credit.

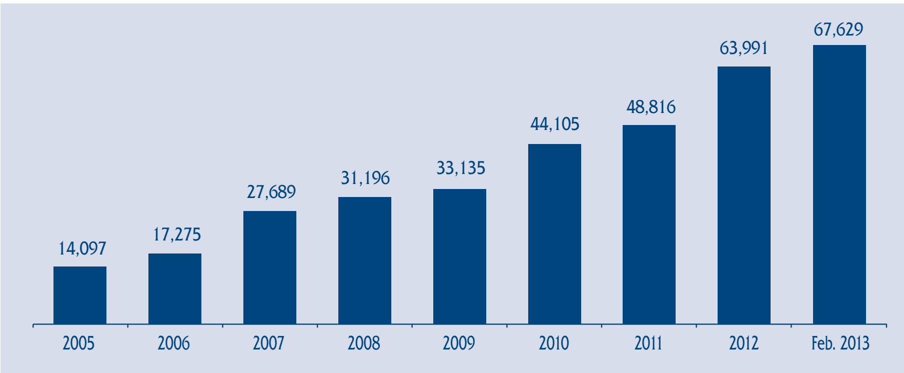
45. The accumulation of international reserves has allowed the Central Bank to continue reducing the economy's vulnerability vis-à-vis events of an abrupt reduction of external financing. The country's reserves represent 34 percent of GDP, they are equivalent to more than 5 times the amount of the short-term external debt, and to 95 percent of banks' total obligations with the private sector (total liquidity).

Table 24
NIR INDICATORS

	Feb.03	Feb.08	Feb.13
Net International Reserves (NIR, millions of US$)	10,277	32,306	67,629
BCRP International Position (Millions of US$)	3,468	25,140	47,877
NIR / GDP (%) 1/	18.1	30.1	33.9
NIR / Short term debt (# of times) 2/	2.3	3.4	5.5
NIR / Total Liquidity (%)	82.8	109.1	94.9

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

Graph 61
NET INTERNATIONAL RESERVES: 2005 - FEB.2013
(Millions of US$)



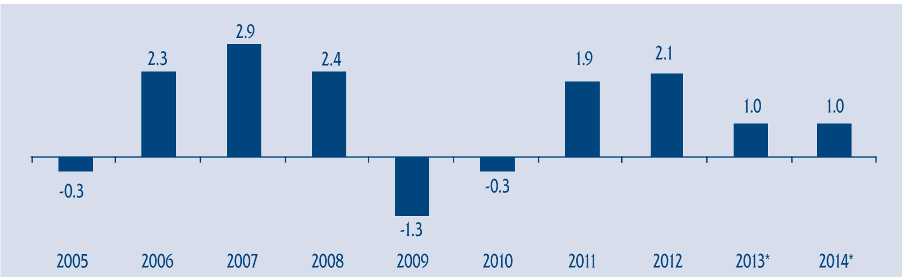
IV. Public Finances

46. In 2012 the operations of the **non-financial public sector** recorded an economic surplus of S/. 11.1 billion, equivalent to 2.1 percent of GDP, which was a slightly higher balance than the surplus of 1.9 percent registered in 2011. This increased balance is associated, on the one hand, with higher current revenues of the general government, which grew by a real 7.3 percent, and on the other hand with the higher primary balance obtained by non-financial public enterprises, offset by the real growth of the non-financial expenditure of the general government (up 8.0 percent). It should be pointed out that this increase in expenditure was mainly associated with an increased spending in gross capital formation (16.0 percent), while current expenditure increased by a real 5.2 percent due mainly to higher spending in goods and services by the sub-national governments.

47. The economic balance projected for **2013** and **2014** has been revised downwards from 1.1 percent of GDP (Inflation Report of December) to 1.0 percent of GDP. This lower result is due to the lower revenue expected as a result of lower international prices for our main export products, as well as due to increased current expenditure of the general government. This projection takes into account further salary rises as well as greater staff engagement, in accordance with what was approved in the 2013 Budget.

    Among other things, the Public Sector Financial Equilibrium Law passed this year establishes that the economic balance should not be negative (deficit), which replaces the macro fiscal rules of the Responsibility and Fiscal Transparency Act (which established that the fiscal deficit of the government should be of less than 1 per cent of GDP and that the real spending increase in consumption should not exceed 4 percent).

Graph 62
ECONOMIC BALANCE OF THE NON FINANCIAL PUBLIC SECTOR: 2005-2014
(% of GDP)



* Forecast.

Table 25
NON FINANCIAL PUBLIC SECTOR
(% of GDP)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
1. General government current revenues 1/	**21.0**	**21.6**	**21.7**	**21.6**	**21.7**	**21.6**
Real % change	*13.6*	*7.3*	*6.5*	*5.8*	*6.6*	*6.8*
2. General government non financial expenditure 2/	**18.1**	**18.7**	**19.5**	**19.6**	**19.6**	**19.7**
Real % change	*1.7*	*8.0*	*10.6*	*11.2*	*7.0*	*7.1*
Of which:						
Current	13.0	13.1	13.5	13.6	13.3	13.5
Real % change	*7.1*	*5.2*	*9.4*	*9.8*	*5.6*	*5.9*
Gross capital formation	4.7	5.2	5.7	5.7	5.9	5.8
Real % change	*-8.1*	*16.0*	*11.7*	*14.8*	*10.7*	*10.0*
3. Others	**0.1**	**0.3**	**0.0**	**0.0**	**0.0**	**0.0**
4. Primary balance (1-2+3)	**3.0**	**3.2**	**2.2**	**2.0**	**2.1**	**1.9**
5. Interests	**1.2**	**1.1**	**1.0**	**1.0**	**1.0**	**0.9**
6. Overall Balance	**1.9**	**2.1**	**1.1**	**1.0**	**1.1**	**1.0**
Memo: (billions of S/.):						
1. General government current revenues	102	114	123	123	133	134
2. General government non-financial expenditure	88	98	111	112	120	122
3. Nominal GDP	487	526	568	569	616	620

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.

Evolution of fiscal revenues

48. In 2012 the current revenues of the general government amounted to 21.6 percent of GDP. This revenue is 0.6 percentage points higher than in 2011, which is explained mainly by higher revenues from the income tax of both individuals and companies, and by higher revenues from the value added tax (VAT). Other revenues which also contributed to this increase were the higher amounts of transfers of tax withholdings from Banco de la Nación to the Treasury and other revenues associated with mining activity. In 2012 revenues from mining royalties, the special tax on mining (Impuesto Especial a la Minería - IEM), and the special levy on mining (Gravamen Especial a la Minería - GEM) amounted to S/. 1.97 billion, a figure 90 percent higher than the one registered in 2011 (S/. 1.04 billion), when these taxes were established.

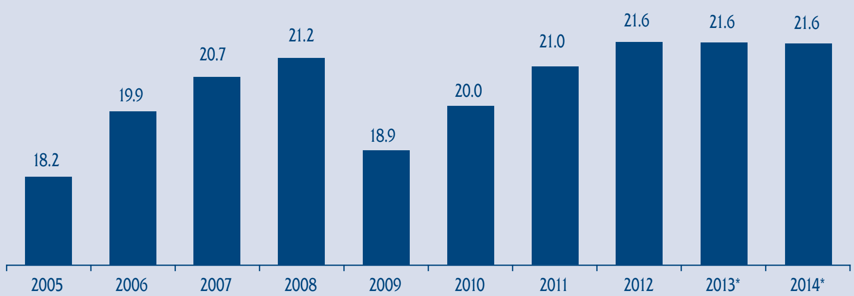
    It is worth pointing out that SUNAT developed various formalization campaigns in sectors where high levels of tax evasion were detected and also carried out control operations on the transport of goods, verifying as well that shops and stores provided payment receipts to buyers. Moreover, other sectors such as the sectors of non-gold metal mining and non-metal mining were also included in the tax withholdings system.

Table 26
GENERAL GOVERNMENT CURRENT REVENUES
(% of GDP)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
TAX REVENUES	**15.9**	**16.4**	**16.5**	**16.2**	**16.5**	**16.3**
Income tax	6.9	7.1	7.3	6.9	7.3	7.0
Value added tax	8.3	8.4	8.5	8.5	8.5	8.5
Excise tax	1.0	0.9	0.9	0.9	0.9	0.9
Import duties	0.3	0.3	0.3	0.3	0.3	0.3
Other tax revenues	1.4	1.7	1.7	1.7	1.7	1.7
Tax returns	-2.0	-2.0	-2.1	-2.1	-2.1	-2.1
NON TAX REVENUES	**5.1**	**5.2**	**5.1**	**5.3**	**5.1**	**5.3**
TOTAL	**21.0**	**21.6**	**21.7**	**21.6**	**21.7**	**21.6**

IR: Inflation report.
* Forecast.

Graph 63
GENERAL GOVERNMENT CURRENT REVENUES: 2005 - 2014
(% of GDP)

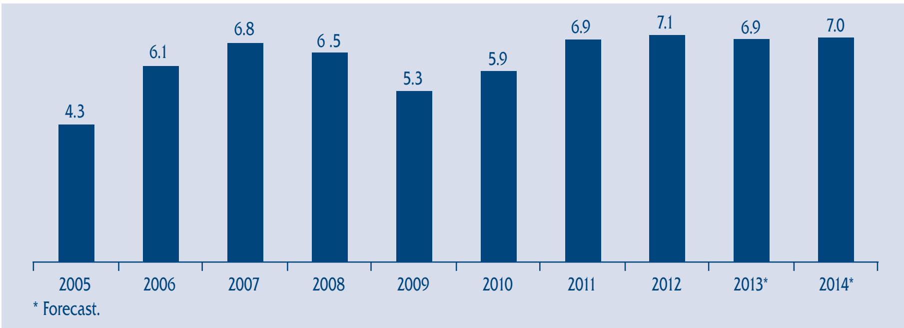


* Forecast.

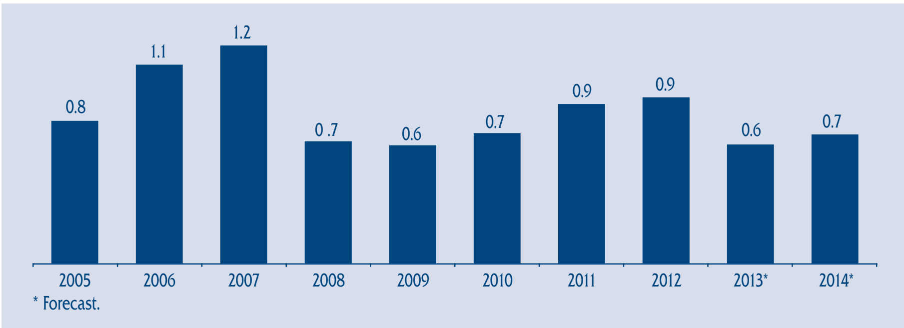
49. The real growth of the current revenues of the general government in **2013** has been revised downwards from 6.5 percent (Inflation Report of December) to 5.8 percent due mainly to the lower revenues expected from the regularization of the income tax, in line with the lower revenues and profits that would be observed in the mining sector. Thus, the ratio of current revenues to GDP is also revised down from 21.7 percent (previous report) to 21.6 percent of GDP, while this ratio in 2014 has also been revised downwards by 0.1 percentage points.

In 2013 the revenue from the **income tax** would amount to 6.9 percent of GDP, lower by 0.4 percentage points than estimated in December, due to a lower regularization of this tax (0.6 percent of GDP), partially offset by higher revenues from the payroll income tax in a context of growth in formal employment. A slight increase to 7 percent of GDP would be observed in 2014, although this figure would still be lower than the 7.3 percent forecast in December.

Graph 64
INCOME TAX: 2005 - 2014
(% of GDP)



Graph 65
INCOME TAX REGULARIZATION: 2005 - 2014
(% of GDP)

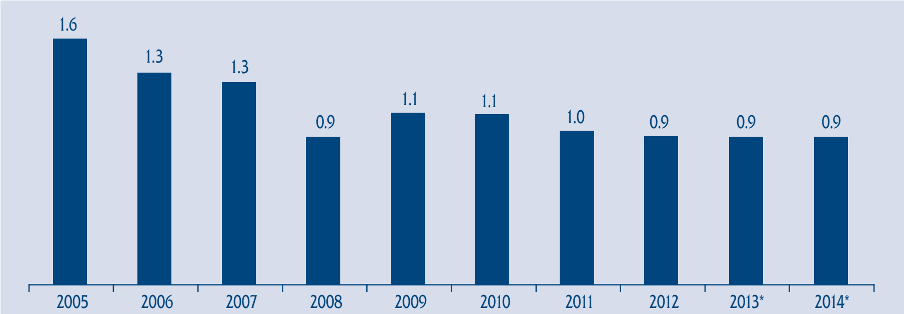


Revenue from the **value added tax** (VAT) would remain at 8.5 percent of GDP in 2013 and 2014, recording a real growth of 7.8 percent and 6.1 percent in these years, respectively. It is worth mentioning that the domestic VAT would show growth rates of 11.7 percent and 7.8 percent, respectively, in line with the greater dynamism of domestic demand and the improvements resulting from the administrative measures aimed at broadening the tax base.

Graph 66
VALUE ADDED TAX: 2005 - 2014
(% of GDP)

The reduction approved in the rate of the **excise tax** on fuels in mid-2011 caused a reduction of 0.1 percentage point in the revenue from this tax in 2012, which reached 0.9 percent of GDP. In 2013 and 2014 revenue from this tax is projected to remain at 0.9 percent of GDP since no rate changes are foreseen in this tax.

Graph 67
EXCISE TAX: 2005 - 2014
(% of GDP)



* Forecast.

Evolution of government expenditure

50. Showing a recovery compared to the real growth rate registered in 2011 (1.7 percent), the non-financial expenditure of the general government in 2012 grew 8.0 percent. This growth was driven by the increased capital spending of sub-national governments, which showed real growth rates close to 40 percent, a figure that contrasts with the spending contractions recorded in 2011 as a result of management problems associated with the change of municipal authorities. With this, the non-financial spending-to-GDP ratio reached 18.7 percent, a level 0.6 percentage points higher than in 2011.

Table 27
GENERAL GOVERNMENT NON FINANCIAL EXPENDITURE
(Real % change)

	2011	2012				
		Q1	Q2	Q3	Q4	Year
CURRENT EXPENDITURE	**7.1**	**-3.2**	**1.2**	**2.7**	**17.0**	**5.2**
National government	7.6	-11.9	-4.4	-2.2	20.9	1.6
Regional governments	6.7	10.8	11.7	9.9	10.8	10.8
Local governments	5.0	34.6	15.7	19.0	7.6	17.1
CAPITAL EXPENDITURE	**-10.1**	**34.0**	**1.0**	**26.3**	**11.9**	**15.2**
National government	-3.9	-32.0	-39.6	2.2	7.5	-13.3
Regional governments	-9.4	44.1	42.0	43.5	30.5	37.1
Local governments	-17.0	213.1	74.3	44.0	6.7	39.1
TOTAL EXPENDITURE	**1.7**	**3.0**	**1.1**	**8.6**	**15.1**	**8.0**
National government	5.0	-14.7	-12.8	-1.5	17.7	-1.4
Regional governments	1.6	17.0	19.1	18.7	18.3	18.3
Local governments	-7.8	87.1	39.2	31.6	7.0	28.6

Table 28
GENERAL GOVERNMENT NON FINANCIAL EXPENDITURE
(Contribution to the real % change)

	2011	2012				
		Q1	Q2	Q3	Q4	Year
CURRENT EXPENDITURE	**4.9**	**-2.7**	**0.8**	**2.0**	**10.7**	**3.8**
National government	3.5	-7.1	-2.2	-1.2	8.7	0.8
Regional governments	0.9	1.6	1.5	1.4	1.4	1.5
Local governments	0.4	2.8	1.5	1.8	0.7	1.6
CAPITAL EXPENDITURE	**-3.2**	**5.7**	**0.3**	**6.6**	**4.4**	**4.2**
National government	-0.5	-3.1	-6.3	0.2	1.0	-1.7
Regional governments	-0.6	1.5	1.8	2.1	2.3	2.0
Local governments	-2.1	7.3	4.8	4.2	1.1	3.9
TOTAL EXPENDITURE	**1.7**	**3.0**	**1.1**	**8.6**	**15.1**	**8.0**
National government	3.0	-10.3	-8.5	-0.9	9.6	-0.9
Regional governments	0.3	3.2	3.3	3.5	3.7	3.5
Local governments	-1.6	10.1	6.3	6.0	1.8	5.4

51. In **2013** the non-financial expenditure of the general government would grow by a real 11.5 percent as a result of the salary rises approved in the 2013 budget mainly for the sectors of education, interior, and defense. Thus, in 2013 this variable would be equivalent to 19.6 percent of GDP, a higher rate than that recorded in 2012 (18.7 per cent). Moreover, in 2014 the non-financial expenditure of the general government would reach a level equivalent to 19.7 percent of GDP showing a more moderate growth path than the one foreseen for 2013.

Table 29
GENERAL GOVERNMENT NON FINANCIAL EXPENDITURE
(% of GDP)

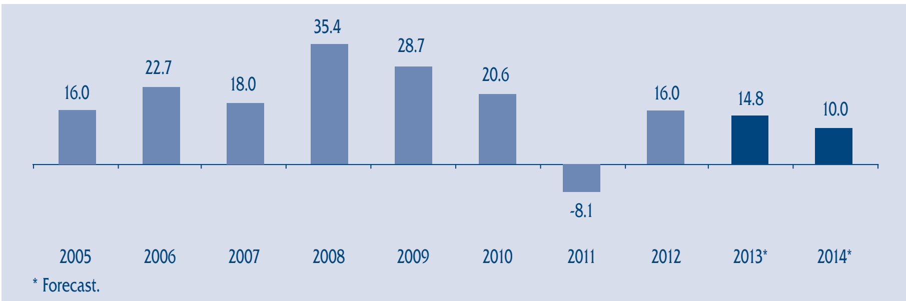
	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
CURRENT EXPENDITURE	**13.0**	**13.1**	**13.5**	**13.6**	**13.3**	**13.5**
National government	8.9	8.7	9.0	8.9	8.9	8.8
Regional governments	2.5	2.6	2.6	2.7	2.6	2.7
Local governments	1.6	1.8	1.8	2.0	1.8	2.0
CAPITAL EXPENDITURE	**5.0**	**5.5**	**6.1**	**6.0**	**6.2**	**6.2**
National government	2.3	1.9	2.3	2.1	2.3	2.1
Regional governments	1.0	1.3	1.1	1.4	1.4	1.4
Local governments	1.8	2.4	2.6	2.5	2.5	2.7
TOTAL EXPENDITURE	**18.1**	**18.7**	**19.5**	**19.6**	**19.6**	**19.7**
National government	11.2	10.6	11.3	11.0	11.3	10.8
Regional governments	3.4	3.9	3.8	4.1	4.0	4.2
Local governments	3.4	4.2	4.5	4.5	4.3	4.7

* Forecast.

Graph 68
GENERAL GOVERNMENT NON FINANCIAL EXPENDITURE: 2005 - 2014
(Real % change)

Graph 69
GENERAL GOVERNMENT NON FINANCIAL CURRENT EXPENDITURE: 2005 - 2014
(Real % change)

Graph 70
GENERAL GOVERNMENT GROSS CAPITAL FORMATION: 2005-2014
(Real % change)

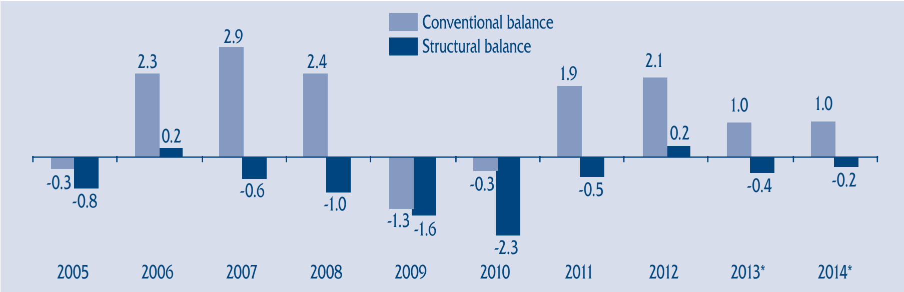


Structural economic balance and fiscal impulse

52. The **structural economic balance**, indicator of the long term fiscal policy position since it isolates the effects of the economic cycle and the price effects of the major mining exports from the conventional economic balance, was 0.2 percent of GDP in

2012. In 2013 the structural balance would show a negative rate of 0.4 percent of GDP, associated with higher spending in the general government, while in 2014 the structural deficit would decline to 0.2 percent of GDP.

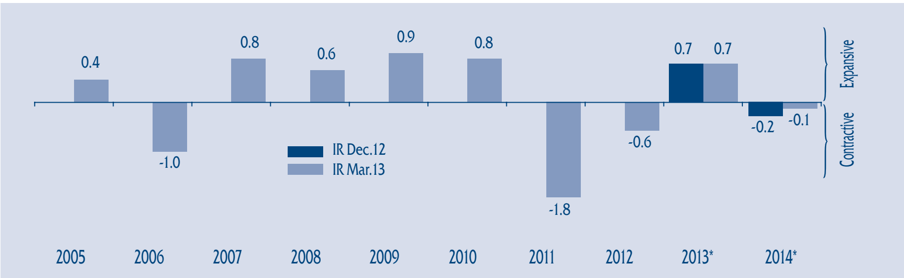
Graph 71
CONVENTIONAL AND STRUCTURAL BALANCE OF THE NON FINANCIAL PUBLIC SECTOR: 2005-2014
(% of GDP)



* Forecast.

53. The variation in the structural balance determines the **fiscal impulse**. This indicator allows us to identify changes in the fiscal policy position isolating the effects of the economic cycle. In 2012 the fiscal impulse registered a negative rate of 0.6 points of GDP (contractionary position) as a result of the slow recovery observed in the growth of public spending. In 2013 the fiscal impulse would be 0.7 percent (expansionary fiscal position), in line with the salary rises approved for this year, while in 2014 the fiscal impulse would be -0.1 percent of GDP, slightly lower than estimated in our report of December.

Graph 72
FISCAL IMPULSE 1/: 2005-2014
(% of GDP)



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

Financial requirements and public debt

54. In 2012, the fiscal surplus was higher than the amortization payments and therefore the financing **requirement of the public sector** was negative, which represented a

saving of S/. 6.8 billion. Given that lower fiscal surpluses are expected for 2013 and 2014, this would translate into lower savings in these years.

It should be pointed out that this requirement excludes the debt management operations to be carried out in 2013, which includes making a debt prepayment of US$ 1.68 billion and the issuance of sovereign bonds for a total of S/. 4.43 billion. In line with this, in February the government issued bonds for a total of S/. 1.91 billion (at face value), 85 percent of which were acquired by local investors.

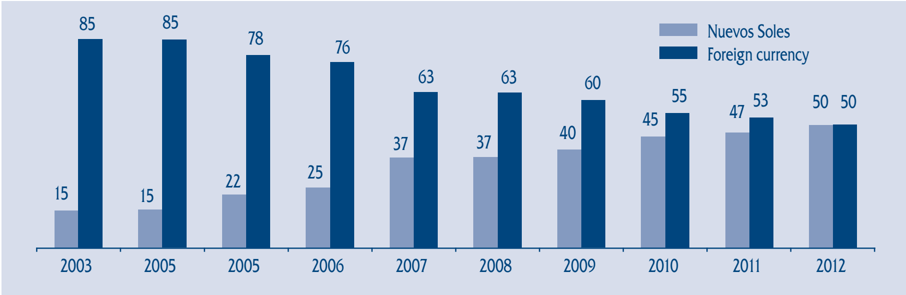
Table 30
FINANCIAL REQUIREMENTS OF THE NON-FINANCIAL PUBLIC SECTOR AND ITS FINANCING 1/
(Millions of S/.)

	2011	2012	2013*		2014*	
			IR Dec.12	IR Mar.13	IR Dec.12	IR Mar.13
I. USES	**-5,444**	**-6,761**	**-2,276**	**-1,866**	**-2,565**	**-2,483**
1. Amortization	3,634	4,342	4,206	3,719	4,513	3,659
a. External debt	2,291	3,105	2,451	2,478	3,188	2,734
Millions of US$	*831*	*1,175*	*943*	*960*	*1,226*	*1,060*
b. Domestic debt	1,343	1,237	1,755	1,241	1,325	924
Of which: Recognition bonds	*530*	*509*	*451*	*223*	*448*	*240*
2. Overall balance (negative sign indicates surplus)	-9,077	-11,104	-6,481	-5,585	-7,078	-6,142
II. SOURCES	**-5,444**	**-6,761**	**-2,276**	**-1,866**	**-2,565**	**-2,483**
1. External	2,807	1,224	2,552	2,491	2,104	2,633
Millions of US$	*1,023*	*467*	*981*	*966*	*809*	*1,021*
2. Bonds 2/	0	1,345	1,422	1,448	1,484	1,745
3. Internal 3/	-8,251	-9,330	-6,250	-5,804	-6,153	-6,861
Memo:						
Balance of gross public debt						
Billions of S/.	103.3	104.4	105.8	103.4	106.2	106.4
% of GDP	21.2	19.8	18.6	18.2	17.2	17.2
Balance of net public debt 4/						
Billions of S/.	39.3	26.0	24.5	19.6	17.7	14.9
% of GDP	8.1	4.9	4.3	3.4	2.9	2.4

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 deposits.
4/ Defined as the difference between gross public debt and NFPS deposits.
IR: Inflation report.
* Forecast.

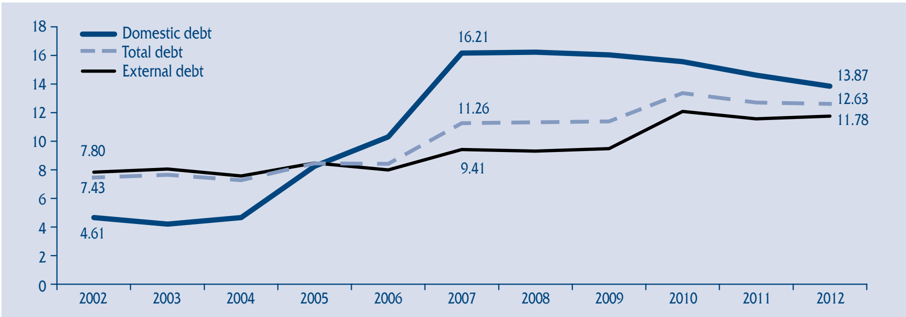
55. As a result of the debt management operations carried out in recent years, at the end of 2012 the balance of public debt denominated in national currency was similar to the balance of debt denominated in foreign currency, which has allowed the Central Bank to reduce the economy's vulnerability to exchange rate shocks. It is worth highlighting that in the last decade the percentage of debt in nuevos soles has increased from 15 percent in 2003 to 50 percent in 2012.

Graph 73
PUBLIC DEBT BALANCE BY CURRENCY
(% structure)



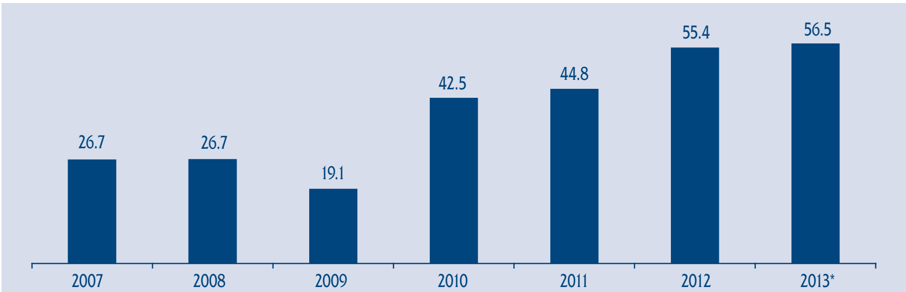
Other debt indicators worth pointing out include the following: at December 2012, the average life of the public debt reached 12.6 years, while the percentage of debt at a fixed rate reached 87 percent. These indicators are expected to improve even further with the debt prepayment to international agencies that will be carried out this year.

Graph 74
AVERAGE LIFE OF THE PUBLIC DEBT
(Years)



On the other hand, at March 20, 2013, the share of sovereign bonds held by non-residents was 56.5 percent of the total amount of bonds, 11.7 percentage points higher than at end 2011.

Graph 75
SOVEREIGN BONDS HELD BY NON-RESIDENTS
(%)



* Preliminary as of March 20.

56. Moreover, the yield on sovereign bonds PERU 2037 rose 9 basis points between December 2012 and February 2013, while the yield on global bonds PERU 2037 fell 4 basis points in the same period. This would also be an indicator of a reversal of appreciatory expectations observed in the international market.

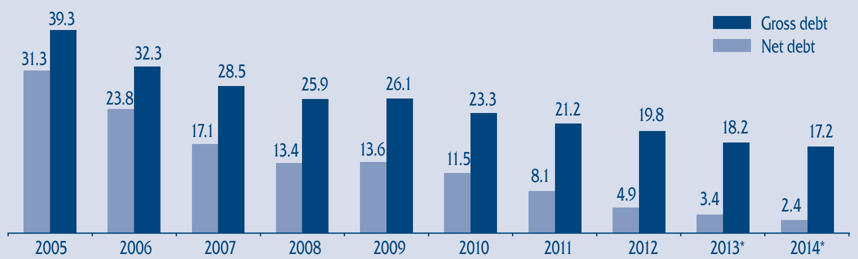
Table 31
YIELDS ON SOVEREIGN AND GLOBAL BONDS FROM PERU AND US TREASURY BONDS ACCORDING MATURITY DATE
(End of period data, in percentage points)

	Dec.11	Dec.12	Jan.13	Feb.13	Variation (in basis points)	
	(4)	(3)	(2)	(1)	Feb.13 / Dec.12 (1)-(2)	Feb.13 / Dec.11 (1)-(2)
Sovereign Bonds (S/.)						
PERU 2013	4.03	2.70	1.57	1.40	-17	-263
PERU 2015	4.47	2.71	1.75	1.40	-35	-307
PERU 2017	4.81	3.05	2.60	2.39	-21	-242
PERU 2020	5.72	3.80	3.76	3.73	-3	-199
PERU 2023	n.d	4.09	4.09	4.16	8	n.d
PERU 2026	6.16	4.24	4.21	4.20	-1	-196
PERU 2031	6.45	4.79	4.79	4.85	6	-160
PERU 2037	6.55	4.90	4.87	4.96	9	-159
PERU 2042	6.65	5.10	5.05	5.14	9	-151
Global Bonds (US$)						
PERU 2015	1.84	0.82	1.09	0.68	-41	-116
PERU 2016	2.38	1.10	1.20	1.33	12	-106
PERU 2019	3.05	1.84	2.04	2.04	0	-101
PERU 2025	4.12	3.00	3.21	3.24	3	-88
PERU 2033	4.81	3.64	3.91	4.04	13	-77
PERU 2037	4.68	3.70	4.17	4.13	-4	-55
US Treasury Bonds						
2-years Bonds	0.24	0.25	0.26	0.24	-3	-1
3-years Bonds	0.36	0.35	0.40	0.34	-6	-1
5-years Bonds	0.83	0.71	0.88	0.76	-12	-7
10-years Bonds	1.88	1.70	1.99	1.88	-11	0
30-years Bonds	2.90	2.87	3.17	3.09	-9	19

*Differences in basis points.
Source: Bloomberg.

At December 2012 the gross debt and the net debt reached 19.8 percent and 4.9 percent of GDP, respectively. Given the positive results registered in public finances, the expected increase in economic activity and the increase in public sector deposits would allow the Peruvian economy to continue reducing its gross debt, which is estimated to decline to 17.2 percent of GDP in 2014, while the net debt would represent 2.4 percent of GDP on the same year.

Graph 76
PUBLIC DEBT: 2005-2014
(% of GDP)



* Forecast.

V. Monetary Policy

57. In 2012, the Board of the Central Bank decided to maintain the policy interest rate at 4.25 percent, the same rate level observed since May 2011. In this period, the monetary policy communiqués highlighted the decline of inflation and its return to the target range of between 1 and 3 percent as a result of the reversal of supply factors amid a context of economic growth close to the economy's potential growth and inflation expectations anchored to the target.

Graph 77
BCRP REFERENCE INTEREST RATE
(%)

SUMMARY OF MONETARY POLICY COMMUNIQUÉS

December: 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 fact that inflation continues to decline and that it has returned to the target range after the shocks on the side of supply partially reversed in a domestic context characterized by an economic pace of growth close to the economy's potential growth and in an external context still characterized by high uncertainty. The Board oversees the inflation forecasts and inflation determinants to consider future adjustments in monetary policy instruments.

January: 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 fact that inflation continues to decline due to the reversal of the shocks on the side of supply, in a domestic context characterized by an economic pace of growth close to the economy's potential growth and a still complicated external context. The Board oversees the inflation forecasts and inflation determinants to consider future adjustments in monetary policy instruments.

February: 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 fact that inflation continues reflecting both the reversal of the shocks on the side of supply and a pace of economic growth close to the economy's potential level of growth. The Board oversees the inflation forecasts and inflation determinants to consider future adjustments in monetary policy instruments.

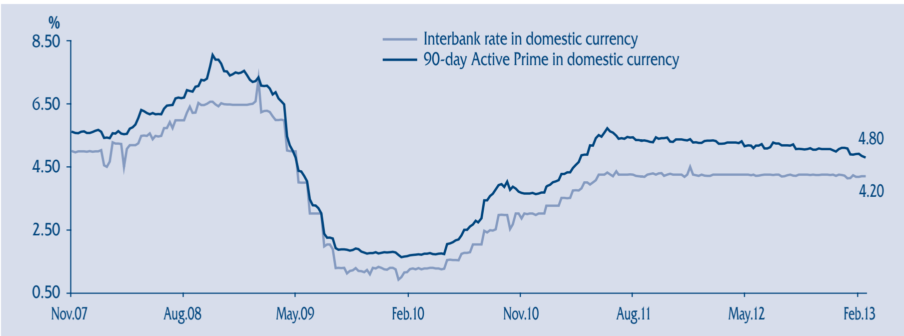
March: The Board of the Central Reserve Bank of Peru approved to maintain the monetary policy reference rate at 4.25 percent.

This decision is based on the fact that inflation continues evidencing both the reversal of the shocks on the side of supply and a pace of economic growth close to the economy's potential level of growth. The Board oversees the inflation forecasts and inflation determinants to consider future adjustments in monetary policy instruments.

Interest rates in domestic currency

58. Since the end of December the 90-day lending corporate prime interest rate in local currency declined 26 basis points to a level of 4.80 percent, where it has remained stable. Because it is a short-term rate and because it has a lower premium for credit risk, this is the interest rate with the greater relationship with the monetary policy interest rate. The evolution of this rate is consistent with a situation of ample availability of liquidity in local currency in the economy and with a reference interest rate which has remained at 4.25 percent since May 2011, as well as with an inverted yield curve in the Central Bank's certificates.

Graph 78
90-DAY CORPORATE PRIME RATE VERSUS INTERBANK OVERNIGHT RATE IN DOMESTIC CURRENCY: NOV.07 - FEB.13



59. Interest rates on corporate credits in national currency continue showing a rise of between 18 and 36 basis points in the cost of credit for this segment, reflecting the

effect of the recent measures implemented in the rate of reserve requirements. The largest increase is observed in the interest rates for mortgage loans (36 basis points). On the other hand, the interest rates on consumer loans and loans to micro-enterprises and small businesses have fallen by 158, 67, and 3 basis points, respectively, due to greater competition in this segment.

Table 32
INTEREST RATE BY TYPE OF LOANS 1/
(%)

	Domestic currency						
	Corporate	Large companies	Medium-size firms	Small businesses	Micro-businesses	Consumer	Mortgages
Dec.10	4.6	5.9	10.3	23.3	27.2	40.7	9.3
Dec.11	6.0	7.4	11.2	23.2	33.0	38.5	9.4
Mar.12	6.1	7.0	11.2	23.4	32.9	35.6	9.4
Jun.12	6.0	7.3	11.2	23.1	33.0	34.9	9.3
Sep.12	5.7	7.5	11.1	22.9	33.2	38.0	8.9
Oct.12	6.0	7.5	11.0	23.0	33.0	38.8	8.9
Nov.12	6.2	7.6	10.9	23.0	32.7	38.6	8.8
Dec.12	5.8	7.4	11.0	22.5	33.2	41.2	8.8
Jan.13	6.0	7.4	11.0	22.2	33.4	40.9	8.9
Feb.13	6.0	7.5	11.0	22.4	32.5	39.6	9.1
Accumulated change (bps)							
Feb.13-Dec.12	25	18	0	-3	-67	-158	36
Feb.13-Dec.11	1	18	-19	-73	-54	113	-27

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

60. As regards deposit rates in national currency, a decline of between 11 and 44 basis points is observed in all the different deposit terms.

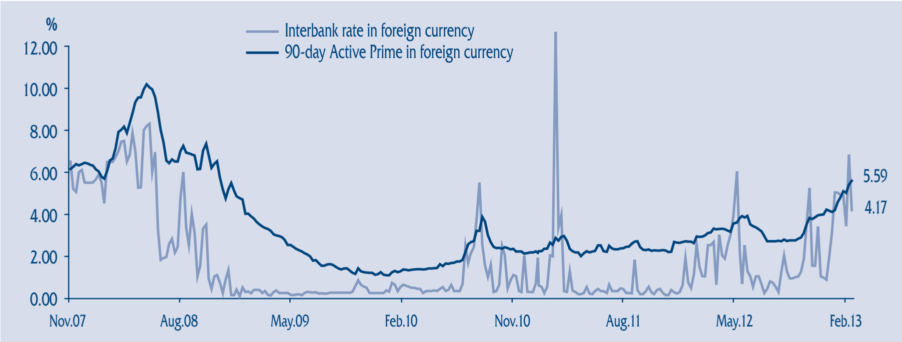
Table 33
INTEREST RATES IN NUEVOS SOLES
(%)

	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
Jan.12	3.8	4.0	4.7
Feb.12	3.7	4.0	4.7
Mar.12	3.7	3.9	4.5
Apr.12	3.7	3.9	4.4
May.12	3.7	3.9	4.3
Jun.12	3.7	3.9	4.3
Jul.12	3.8	3.9	4.3
Aug.12	3.8	3.9	4.2
Sep.12	3.7	3.8	4.3
Oct.12	3.7	3.9	4.2
Nov.12	3.6	3.8	4.1
Dec.12	3.6	3.6	4.1
Jan.13	3.4	3.6	4.0
Feb.13	3.1	3.4	3.9
Accumulated change (bps)			
Feb.13-Dec.12	-44	-24	-11
Feb.13-Dec.11	-74	-9	-53

Interest rates in foreign currency

61. A lower availability of liquidity in dollars is observed in foreign currency as a result of the higher reserve requirements established by the Central Bank and banks' sales of foreign currency to the BCRP, all of which reflected since December in a rise of 139 basis points in the corporate prime rate in dollars to 5.59 percent. Moreover, the interbank interest rate reached an average of 3.50 percent in the quarter, higher by 333 basis points than the average level recorded in December.

Graph 79
90-DAY CORPORATE PRIME RATE VERSUS INTERBANK OVERNIGHT RATE IN FOREIGN CURRENCY: NOV.07 - FEB.13



62. The lending interest rates in foreign currency showed rises, although these rises were lower than the ones registered by the short-term interest rates in dollars. Thus, the rates on consumer loans, loans to large companies and medium-sized enterprises, mortgages and corporate loans increased between 27 and 160 basis points, whereas the rate on loans to small enterprises showed a drop of 174 basis points.

Table 34
INTEREST RATE BY TYPE OF CREDIT 1/
(%)

	Foreign currency						
	Corporate	Large companies	Medium-size firms	Small businesses	Micro-businesses	Consumer	Mortgages
Dec.10	3.3	5.5	8.6	14.2	14.8	19.4	8.1
Dec.11	3.0	5.4	8.9	15.0	19.2	22.0	8.2
Mar.12	3.8	5.7	8.9	16.4	19.3	23.0	8.2
Jun.12	4.0	6.1	8.7	15.2	20.0	22.9	8.0
Sep.12	3.8	5.8	9.2	15.6	19.6	23.6	8.0
Oct.12	3.7	5.9	9.2	15.5	20.1	24.0	8.1
Nov.12	4.0	5.9	9.2	15.9	20.3	24.2	8.0
Dec.12	4.1	6.4	9.0	15.5	19.3	22.4	8.0
Jan.13	4.1	6.7	8.7	14.4	20.8	23.1	8.0
Feb.13 2/	4.3	6.8	9.4	13.8	15.1	24.0	8.3
	Accumulated change (bps)						
Feb.13-Dec.12	27	45	42	-174	-421	160	33
Feb.13-Dec.11	131	140	54	-126	-405	201	7

1/ Annual active interest rates on the operations carried out in the last 30 working days.
2/ The decline observed in the interest rates on loans to micro businesses is associated with statistics classification problems and should be corrected in the next months.

63. A higher increase is observed in the case of deposit interest rates in foreign currency than in the lending rates, particularly in the interest rates on 30-day deposits (129 basis points) and the interest rates on 31-day to 180-day deposits (42 basis points). On the other hand, the interest rate on 181-day to 360-day deposits declined by 29 basis points, which indicates the tightness of liquidity in the short term.

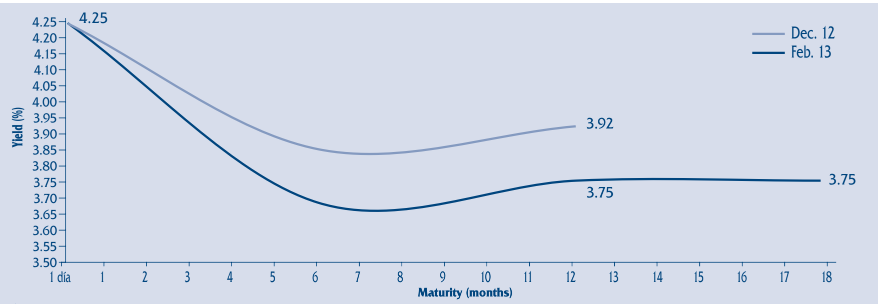
Table 35
INTEREST RATES IN US DOLLARS
(%)

	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
Jan.12	0.9	1.1	1.6
Feb.12	1.0	1.1	1.6
Mar.12	1.3	1.2	1.6
Apr.12	1.4	1.2	1.6
May.12	2.1	1.1	1.6
Jun.12	1.7	1.2	1.6
Jul.12	1.1	1.2	1.6
Aug.12	0.8	1.2	1.6
Sep.12	0.9	1.1	1.6
Oct.12	0.9	1.0	1.8
Nov.12	1.7	1.7	1.6
Dec.12	1.7	1.6	1.6
Jan.13	2.3	1.5	1.5
Feb.13	3.0	2.0	1.3
Accumulated change (bps)			
Feb.13-Dec.12	129	42	-29
Feb.13-Dec.11	232	98	-26

Monetary operations

64. In 2012 the operations of the Central Bank were mainly oriented to maintaining adequate levels of liquidity and ensuring the flow of operations in the monetary market in a scenario with no liquidity tightness in the financial system, which reflected in lower interest rates for the CDBCRP. The yield curve shifted down 17 basis points on average.

Graph 80
YIELD CURVE OF CENTRAL BANK SECURITIES 1/



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

Between November 2012 and February 2013, the Central Bank made net placements of BCRP instruments for a total of S/. 7.87 billion, including mainly term deposits for a total of S/. 5.7 billion. In the same period, the public sector deposits at the Central Bank declined by S/. 4.56 billion as a result of the increased public spending registered in December and the purchase of foreign currency for a total of US$ 1.35 billion in the first months of 2013.

65. As a result of these operations, the participation of the instruments issued by the BCRP increased in terms of the total liabilities of BCRP. Thus, in terms of the international reserves the BCRP monetary instruments increased from representing 17.7 percent in December to 19.8 percent in February 2013. Moreover, the participation of total deposits of reserve requirements also increased from 27.8 to 30.2 percent, mainly due to higher deposits of reserve requirements in national currency, which increased from 12.1 to 14.0 percent. Public sector deposits continued to be the main source of sterilization of foreign exchange interventions with a share of 34 percent of the total liabilities of the BCRP.

Table 36
SIMPLIFIED BALANCE SHEET OF THE BCRP
(As % of Net International Reserves)

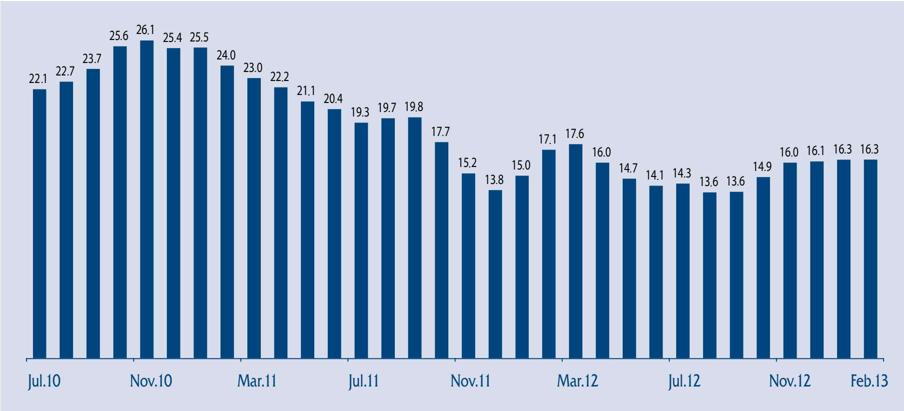
Net assets	Dec.12	Feb.13
I. Net International Reserves	100% (US$ 63,991 mills.)	100% (US$ 67,629 mills.)
Net liabilities		
II. Total public sector deposits	**36.4%**	**34.2%**
In domestic currency	23.6%	20.0%
In foreign currency	12.8%	14.2%
III. Total reserve requirements	**27.8%**	**30.2%**
In domestic currency	12.1%	14.0%
In foreign currency 1/	15.7%	16.2%
IV. BCRP Instruments	**17.7%**	**19.8%**
CD BCRP	12.3%	13.1%
Term deposits	5.5%	6.8%
V. Currency	**19.0%**	**17.0%**
VI. Other	**-0.9%**	**-1.2%**

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

Currency in circulation and credit

66. Between January and February 2013, average currency in circulation grew 16.3 percent in annual terms, in line with the evolution of economic activity which has been showing levels close to the economy's potential output in recent months. In Q1-2013, currency in circulation would grow at a slightly faster pace in a context in which economic agents increase their demand for currency due to the Easter holidays, which this year will be at the end of March.

Graph 81
AVERAGE CURRENCY IN CIRCULATION
(% change respect to the similar period of previous year)



Reserve requirements

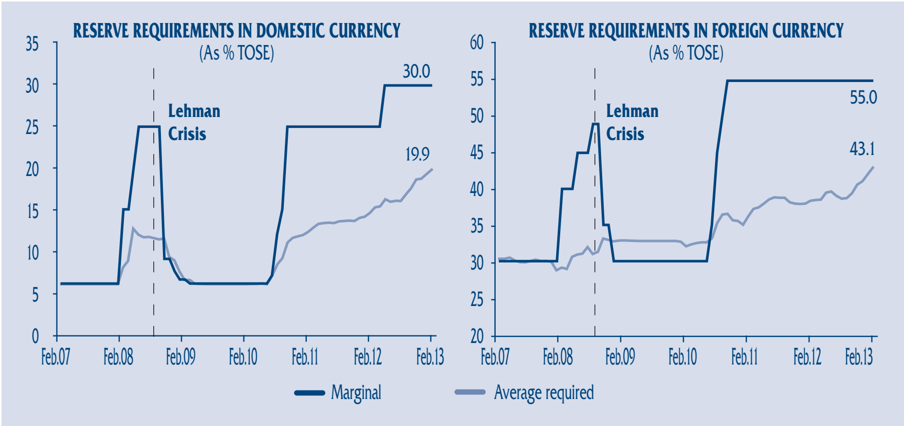
67. In order to maintain the growth of credit at a sustainable level, the Central Bank has increased the rates of reserve requirements in national currency and in foreign currency. The mean rate of reserve requirements in national currency was raised by 0.25 percentage points in January, while the mean rate of reserve requirements in foreign currency was raised by 0.75, 1.00 and 0.50 percentage points in January, February and March, respectively.

To control the dispersion of the reserve requirement measures among the financial entities and to achieve a more uniform impact, in January the mean rate of reserve requirements in local currency was raised by 0.25 percentage points up to a maximum of 20 percent while the rate of reserves in foreign exchange rate was raised by 0.75 percentage points up to a maximum of 45 percent. In February and March the rate base in foreign currency was increased by 1.00 and 0.50 percentage points up to a maximum of 50 percent.

In addition to this, in February the Central Bank established a reserve requirement deduction equivalent to 25 percent for local banks' increase in investments and placements abroad relative to their balance of December 31, 2012, in order to encourage the substitution of foreign currency-denominated assets abroad and moderate in this way the growth of domestic credit in dollars and offset the appreciatory pressures on the exchange rate.

With these measures, the mean rate of reserve requirements in national currency rose from 18.8 percent in December, to 19.9 percent in February, while this rate in dollars rose from 41.2 percent in December to 43.1 percent in February.

Graph 82



Furthermore, measures were taken in March to raise the rate of reserve requirements in foreign currency in the financial entities that showed a higher expansion in mortgage and vehicle loans in dollars given that a high ratio of dollarization –45 percent and 77 percent, respectively– is observed in these segments. At January 2013, car loans in foreign currency showed a growth rate of 39.1 percent in the last twelve months, while mortgage loans showed a growth rate of 16.5 percent.

Thus, the mean rate of reserves will rise by 0.75 percentage points in the case of financial entities whose average daily balance of mortgage and vehicle loan in foreign currency exceeds the balance recorded in February 2013 by 10 percent. If the expansion of these loans is higher than 20 percent, the mean rate of reserves will increase by 1.5 percentage points.

In addition to this, the Central Bank raised the rate of additional reserves from 20 to 25 percent for external loans and for bonds with maturities longer than 3 years when the amount of this funding exceeds 2.2 times banks' equity registered in September 2012.

68. The rate of reserve requirements is an instrument that contributes to the maintenance of adequate levels of liquidity in the financial system, which reduces financial entities' vulnerability to possible scenarios of foreign capital outflows. Moreover, since this instrument increases the cost of financial intermediation, it also contributes to raise the interest rates of loans. The reserve requirement measures implemented in March are also intended to induce financial entities to internalize the risks associated with an excessive use of external funding to provide families with loans in dollars in a context of low international interest rates.

Table 37
RESERVE REQUIREMENTS MEASURES

	Legal minimum reserve requirement	Domestic Currency		Foreign currency		
				General regime		Foreign liabilities
		Marginal reserve requirement on deposits	Increase in the average reserve requirement	Marginal reserve requirements on deposits	Increase in the average reserve requirement	Short term
Feb.10	6%			30%		35%
Jul.10	7%			35%		40%
Aug.10	8%	12%		45%	0.10%	50%
Sep.10	8.5%	15%		50%	0.20%	65%
Oct.10	9%	25%		55%	0.20%	75%
Nov.10	9%	25%		55%		75%
Dec.10	9%	25%		55%		75%
Jan.11 1/	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 2/	9%	30%	0.50%	55%	0.50%	60%
Jul.12 3/	9%	30%		55%		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%
Jan.13	9%	30%	0.25%	55%	0.75%	60%
Feb.13	9%	30%	-.-	55%	1.00%	60%
Mar.13 4/	9%	30%	-.-	55%	0.50%	60%

1/ The operations in the domestic financial market of local bank's branches abroad are subject to reserve requirements since January 2011. base period was updated to December 2012.
2/ Since May 2012, the 60 percent rate of reserve requirements extended also to new short term debts with maturities of 3 years or less. A 20 percent rate of required reserves will be applied to debts with maturities of over 3 years exceeding 2.5 times the bank's equity or exceeding S/. 400 million, whichever is higher.
3/ Since July 2012, the rate of reserve requirements in foreign currency on credit for foreign trade operations was lowered from 60% to 25%.
4/ Since March 2013, BCRP raised the rates of reserve requirements in foreign currency for financial institutions that show a greater expansion of mortgage and vehicle loans in foreign currency.

Box 3
RECENT RESERVE REQUIREMENT MEASURES

The use given by the Central Bank of Peru to the rate of reserve requirements in the last 5 years has changed significantly. In February, the BCRP changed the regime of reserves in foreign currency with the purpose of offsetting the impact of foreign capital inflows on the expansion of credit and the appreciation of the national currency.

At that time, the BCRP raised the rate of reserve requirements from 20 to 25 percent for liabilities and long-term bonds exceeding a prudential limit of 2.2 times the effective equity of a financial entity (from May 2012 the limit was established at 2.5 times a bank's equity).

The aim of this measure is to moderate the rapid expansion of the long-term external funding and thus slow down the pace of growth of credit in foreign currency, ensuring in this way an orderly evolution of liquidity in the current context of a rapid de-dollarization of deposits and of significant short-term and medium-term capital inflows as a result of low international interest rates. Measures were taken in March to raise the rates of reserve requirements in foreign currency for those financial institutions that show a greater expansion of mortgage and vehicle loans in foreign currency given that a high level of dollarization is observed in these segments (44.3 percent and 77.3 percent, respectively, at February 2013).

RATIO OF DOLLARIZATION OF CREDIT TO THE PRIVATE SECTOR 1/						
	%					
	Dec.09	Dec.10	Feb.12	Dec.12	Jan.13	Feb.13
Corporate credit	**55.8**	**56.0**	**54.6**	**53.6**	**54.0**	**54.0**
Foreign trade	94.0	95.5	95.5	96.3	96.8	97.3
Individual credit	**29.1**	**26.4**	**25.0**	**23.9**	**24.1**	**24.0**
Consumer loans	12.2	10.7	9.8	9.7	9.9	10.0
Car loans	68.9	64.0	70.6	76.5	77.1	77.3
Credit cards	8.0	7.2	6.4	6.4	6.6	6.7
Mortgage loans	58.0	52.2	48.8	44.8	44.6	44.3
Total	**46.8**	**46.1**	**44.2**	**42.9**	**43.1**	**43.1**
Dollarization to constant exchange	43.7	43.7	43.0	42.9	42.8	42.7

Thus, the mean average rate of reserves was raised depending on the growth of mortgage and car loans in two different cases: the mean rate of reserve requirements was raised by 0.75 percentage points for financial entities whose average daily balance of mortgage and vehicle loans in foreign currency exceeds their balance of February 2013 by 10 percent and the mean rate would be raised by 1.5 percentage points if the increase of both types of loans exceeds 20 percent.

This measure is aimed at contributing to induce an orderly replacement of banks and families' funding through credit while reducing their exposure to exchange rate and credit risk. Even though the reserve requirement measures mentioned above have influenced a gradual increase in interest rates, the pace of growth of credit is still high, especially in the case of car loans, credit cards, and mortgage loans in dollars. At February 2013 car loans in foreign currency registered a growth rate of 38.4 percent in the last twelve months, while mortgage loans showed a rate of 15.4 percent.

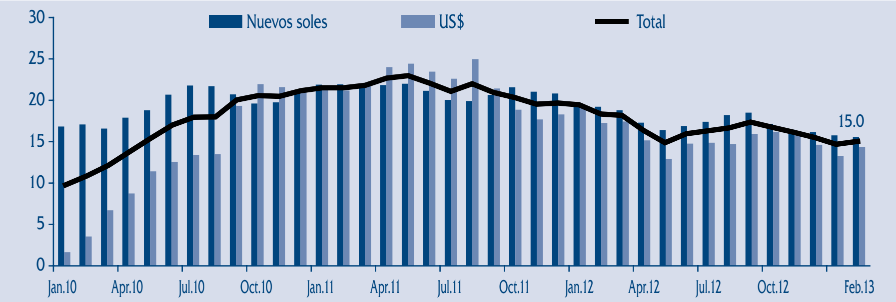
RATIO OF DOLLARIZATION OF CREDIT TO THE PRIVATE SECTOR						
	Balance in millions of US$			Growth rate (%)		
	Feb.12	Jan.13	Feb.13	Jan.13/Jan.12	Feb.13/Feb.12	Feb.13/Jan.13
Corporate credit	**19,979**	**22,664**	**22,723**	**12.2**	**13.7**	**0.3**
Foreign trade	2,893	3,550	3,624	18.6	25.3	2.1
Rest	17,086	19,114	19,099	11.1	11.8	-0.1
Individual credit	**4,956**	**5,755**	**5,778**	**17.5**	**16.6**	**0.4**
Consumer loans	1,179	1,398	1,418	20.3	20.3	1.5
Car loans	405	551	560	39.0	38.4	1.8
Credit cards	260	308	315	21.7	21.2	2.3
Rest	514	539	543	5.1	5.6	0.7
Mortgage loans	3,777	4,357	4,360	16.7	15.4	0.1
Total	**24,935**	**28,419**	**28,501**	**13.2**	**14.3**	**0.3**

These complementary monetary policy measures should contribute to an orderly growth of bank credit, particularly to the orderly growth of credit in foreign currency, thereby reducing the risk of the emergence of vulnerabilities that undermine our financial system's capability to face future scenarios of outflows of external capital.

Credit to the private sector

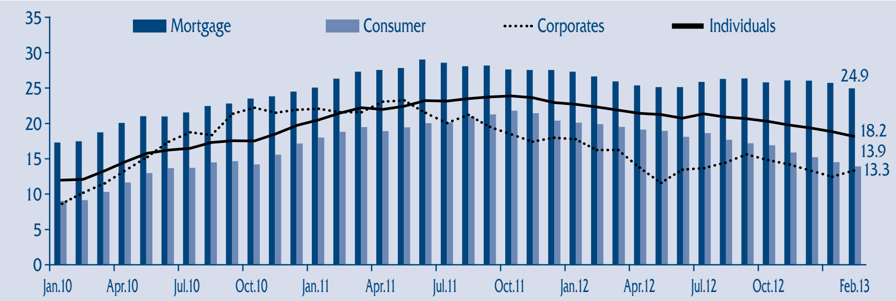
69. Credit to the private sector has moderated its pace of growth showing an annual variation of 15.0 percent in February (vs. 19.7 percent at end 2011 and 16.1 percent in November 2012). Having declined from 18.0 percent in December to 14.2 percent in November 2012 and to 13.3 percent in February 2013, the growth of credit to enterprises also shows more sustainable rates. In the case of personal credit, personal loans registered a rate of 18.2 percent in February, while consumer loans showed a rate of 13.9 percent, and mortgage loans showed a rate of 24.9 percent.

Graph 83
CREDIT TO THE PRIVATE SECTOR
(12 month % change)



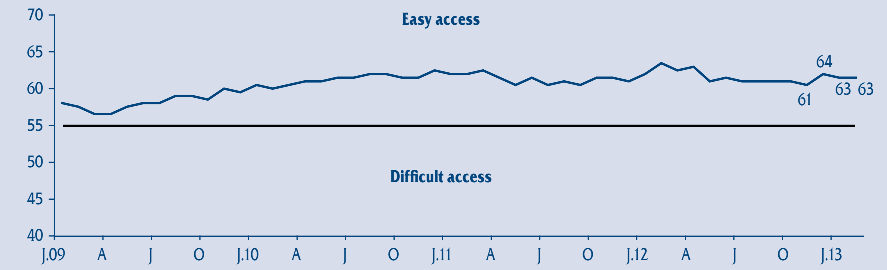
Credit		Dec.09	Dec.10	Dec.11	Aug.12	Sep.12	Oct.12	Nov.12	Dec.12	Jan.13	Feb.13
Nuevos soles	Monthly flows (Millions of S/.)	569	1,514	1,677	1,351	1,367	773	1,348	1,695	-54	756
	Monthly % change	1.0	2.2	2.1	1.5	1.5	0.8	1.4	1.8	-0.1	0.8
	Annual % change	17.9	21.2	20.8	18.2	18.5	17.1	16.4	16.1	15.7	15.5
US$	Monthly flows (Millions of US$)	343	368	561	220	425	182	207	368	-52	82
	Monthly % change	2.0	1.8	2.3	0.8	1.6	0.7	0.7	1.3	-0.2	0.3
	Annual % change	-0.1	21.3	18.3	14.7	15.9	16.2	15.7	14.6	13.2	14.3
Total	Monthly flows (Millions of US$)	1,444	2,451	3,108	1,913	2,450	1,237	1,876	2,633	-186	965
	Monthly % change	1.4	2.0	2.2	1.2	1.5	0.8	1.1	1.6	-0.1	0.6
	Annual % change	9.3	21.2	19.7	16.6	17.4	16.7	16.1	15.5	14.6	15.0

Graph 84
CREDIT BY TYPE OF LOANS: JANUARY 2010 - FEBRUARY 2013
(12 month % change)



Credit		Dec.09	Dec.10	Dec.11	Aug.12	Sep.12	Oct.12	Nov.12	Dec.12	Jan.13	Feb.13
Corporates	Monthly flows (Millions of S/.)	965	1,451	2,157	934	1,549	510	892	1,704	-558	475
	Monthly % change	1.5	1.8	2.3	0.9	1.5	0.5	0.8	1.6	-0.5	0.4
	Annual % change	8.0	22.0	18.0	14.4	15.6	14.8	14.2	13.4	12.4	13.3
Individuals	Monthly flows (Millions of S/.)	479	1,000	951	979	901	727	984	929	371	490
	Monthly % change	1.4	2.5	1.9	1.7	1.6	1.2	1.7	1.5	0.6	0.8
	Annual % change	11.8	19.7	23.0	20.9	20.7	20.3	19.8	19.4	18.8	18.2
Consumer	Monthly flows (Millions of S/.)	314	714	585	500	402	394	412	471	42	271
	Monthly % change	1.4	2.8	1.9	1.5	1.2	1.1	1.2	1.3	0.1	0.7
	Annual % change	9.3	17.1	20.4	17.7	17.2	16.9	15.9	15.2	14.5	13.9
Mortgages	Monthly flows (Millions of S/.)	165	287	366	479	500	333	572	458	330	219
	Monthly % change	1.4	1.9	1.9	2.1	2.2	1.4	2.4	1.9	1.3	0.9
	Annual % change	16.8	24.5	27.5	26.3	26.3	25.8	26.0	26.0	25.7	24.9

Graph 85
STATUS OF ACCESS TO CREDIT OF THE COMPANIES



Source: Survey of Macroeconomic Expectations, BCRP.

70. The dollarization of credit continued to decline in January although to a lesser extent than the dollarization of liquidity. The ratio of dollarization of credit declined from 43.3 percent in November to 43.1 percent in February, while the dollarization ratio of liquidity dropped from 31.4 percent in November to 29.5 percent in February.

Graph 86
DOLLARIZATION RATIO: 1998 - 2013
(%)

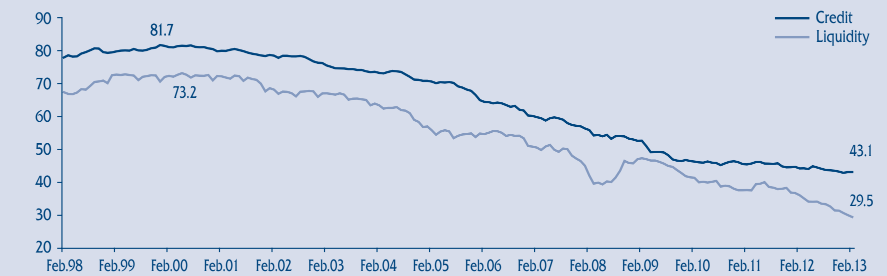


Table 38
RATIO OF DOLLARIZATION OF CREDIT TO THE PRIVATE SECTOR 1/

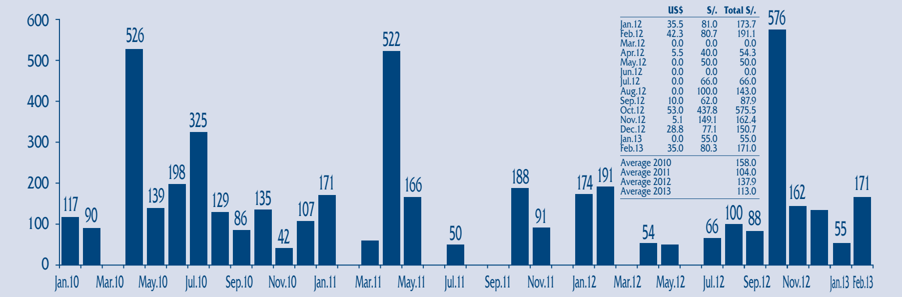
	Dec.08	Dec.09	Dec.10	Dec.11	Dec.12	Feb.13
Corporate credit	**62.0**	**55.8**	**55.9**	**54.9**	**53.6**	**54.0**
Individual credit	**34.3**	**29.1**	**26.5**	**25.1**	**23.9**	**24.0**
Consumer loans	15.1	12.2	10.8	9.8	9.7	10.0
Car loans	80.5	68.9	64.0	69.7	76.5	77.3
Credit cards	8.8	7.7	7.2	6.3	6.4	6.7
Mortgage loans	67.9	58.0	52.2	49.2	44.8	44.3
By type of institutions						
Banks 1/	57.8	53.1	52.7	51.2	49.5	49.7
The state bank	1.7	4.7	1.8	1.1	0.1	0.1
Non financial institutions	20.4	14.0	14.4	13.4	12.3	12.1
TOTAL	**53.0**	**46.8**	**46.1**	**44.6**	**42.9**	**43.1**
Memo:						
Credit dollarization to constant exchange rate	47.8	43.7	43.7	43.2	42.9	42.7

1/ Includes banks' branches from abroad.

Capital market

71. The bond issuances of non-financial firms showed a slower pace of growth rate in Q4-2012. Bond placements of non-financial companies in February amounted to S/. 171 million, while private banks' placement of bonds amounted to S/. 110 million.

Graph 87
BOND ISSUANCES OF NON FINANCIAL FIRMS*
(Millions of nuevos soles)



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

On the other hand, the amount of bonds issued by non-financial firms in the international market has increased significantly, rising from US$ 320 million in 2011 to US$ 1.81 billion in 2012. Bonds for a total of US$ 1.69 billion have been issued so far this year. Local enterprises continue to be encouraged to obtain financing in the international market given the international context of low interest rates.

Table 39
BONDS ISSUED BY NON FINANCIAL FIRMS IN THE INTERNATIONAL MARKET

	US$ Millions	Maturity (years)	Rate
2011 Total	**320**		
Corporación Lindley	320	10	6.75%
2012 Total	**1,810**		
Volcan	600	10	5.38%
Camposol	125	5	9.88%
Terminales Portuarios Euroandinos	110	25	8.13%
Ajecorp	450	10	6.50%
Coazúcar (Grupo Gloria)	325	10	6.38%
Maestro	200	7	6.75%
2013 Total	**1,694**		
Copeinca	75	5	9.00%
Pesquera Exalmar	199	7	7.38%
Cementos Pacasmayo	300	10	4.63%
Alicorp	450	10	3.88%
Gas Natural de Lima y Callao	320	10	4.38%
Compañía Minera Milpo	350	10	4.63%

Non-financial firms have announced bond issuances for a total of US$ 3.4 billion in 2013. Among the issuances announced for the year, the bonds to be issued by Transportadora de Gas del Perú and Nexus Capital Partner II stand out.

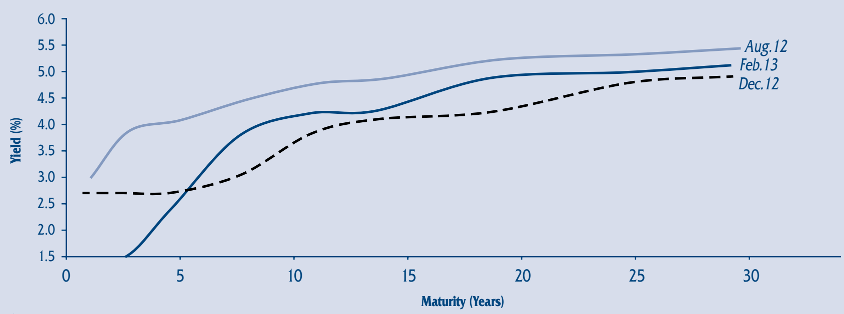
Table 40
BONDS ISSUED IN THE EXTERNAL MARKET: 2013
(Millions of US$)

Total	**4,174**
Financial system	**800**
BBVA	300
BCP*	500
Non financial firms	**3,374**
Copeinca	75
Pesquera Exalmar	199
Cementos Pacasmayo	300
Alicorp	450
Gas Natural Lima y Callao	320
Milpo	350
H2Olmos S.A. *	50
Chinalco *	130
Andino Investment Holding *	150
Nexus Capital Partner II *	500
Transportadora de Gas del Perú*	850

* Announced.

72. The interest rates in the sovereign bond market continued showing a downward trend between December and February due to non-resident investors' increased demand for these bonds. The yields in the short section of the curve (less than 5 years) continue to be below the Central Bank's reference rate of 4.25 percent. Between December and February, non-resident investors have increased their holdings of sovereign bonds by around S/. 340 million, from S/. 16.4 billion to S/. 16.92 billion, which represents 56 percent of the balance of sovereign bonds issued.

Graph 88
SECONDARY MARKET OF SOVEREIGN BONDS 1/



1/ End of month yield.

73. In the last quarter, the spreads of Peru's 5-year and 10-year sovereign bonds, measured by the credit default swap (CDS), continued declining (9 basis points). The downward trend observed is associated with a perception of a lower country risk and with a better economic outlook.

The decline in spreads accounts in part for the decline in the yield of the sovereign bonds.

Graph 89
CREDIT DEFAULT SWAPS OF SOVEREIGN PUBLIC DEBT
(Basis points)

74. Another important factor is associated with the demand of pension funds (AFPs) for local assets since the closer they are to their limit of investment abroad, the more they can increase their demand for bonds and shares in the domestic market, pushing the prices of these securities upwards. Today, pension funds have 31.1 percent of their portfolio invested overseas.

In February, the AFPs' investment abroad increased by S/. 2.38 billion relative to December, whereas their investment in government bonds fell by S/. 995 million in the same period.

This was the result of the increase in the limit of AFPs' investment abroad, which was raised by the BCRP from 30 to 34 percent. This limit was first raised from 30 to 32 percent in January and then more recently it was raised to 34 percent of the total portfolio in February.

Table 41
CONSOLIDATED PORTFOLIOS MANAGED BY FINANCIAL INSTRUMENTS AND AFP
(Millions of nuevos soles)

	Dec.11		Dec.12		Feb.13	
	Amount	%	Amount	%	Amount	%
I. DOMESTIC INVESTMENT	**58,185**	**71.1**	**68,055**	**70.3**	**68,178**	**68.6**
1. Government	**13,915**	**17.0**	**16,939**	**17.5**	**15,950**	**16.0**
Certificates and term depostis of BCRP /1	886	1.1	2,830	2.9	2,836	2.9
Bonds of Central Government	13,029	15.9	14,109	14.6	13,113	13.2
2. Financial system	**14,333**	**17.5**	**16,268**	**16.8**	**17,624**	**17.7**
Shares and Securitised Shares	5,294	6.5	5,572	5.8	5,742	**5.8**
3. Non-financial firms	**23,175**	**28.3**	**26,058**	**26.9**	**25,879**	**26.0**
Shares and Securitised Shares	16,881	20.6	19,272	19.9	18,909	19.0
4. Fund managers	**3,000**	**3.7**	**3,680**	**3.8**	**3,711**	**3.7**
5. Securitization companies	**3,763**	**4.6**	**5,111**	**5.3**	**5,014**	**5.0**
II. FOREIGN INVESTMENTS	**23,437**	**28.6**	**28,512**	**29.4**	**30,894**	**31.1**
1. Government	**949**	**1.2**	**1,705**	**1.8**	**2,871**	**2.9**
2. Financial system	**2,738**	**3.3**	**2,640**	**2.7**	**2,877**	**2.9**
3. Non-financial firms	**8,220**	**10.0**	**6,249**	**6.5**	**6,512**	**6.6**
4. Fund managers	**11,529**	**14.1**	**17,918**	**18.5**	**18,635**	**18.7**
5. Securitization companies	**-**	**-**	**-**	**-**	**-**	**-**
III. OPERATIONS IN TRANSIT	**260**	**0.3**	**286**	**0.3**	**327**	**0.3**
TOTAL	**81,881**	**100.0**	**96,853**	**100.0**	**99,399**	**100.0**
Foreign investment / Portfolio managed	**28.6%**		**29.4%**			**31.1%**

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

75. Reflecting a reversal in their expectations of an appreciation of the exchange rate, in February the administrators of pension funds increased their net offer in the forward market by US$ 917 million, that is, a lower amount than that of their investments in dollars in the same period (US$ 3.3 billion).

Table 42
AFP: INVESTMENT
(Millions of US$)

	Total	
Date	**In the foreign market**	**In US$**
Dec.12	11,184	16,656
Jan.13	11,794	16,696
Feb.13	11,947	19,999

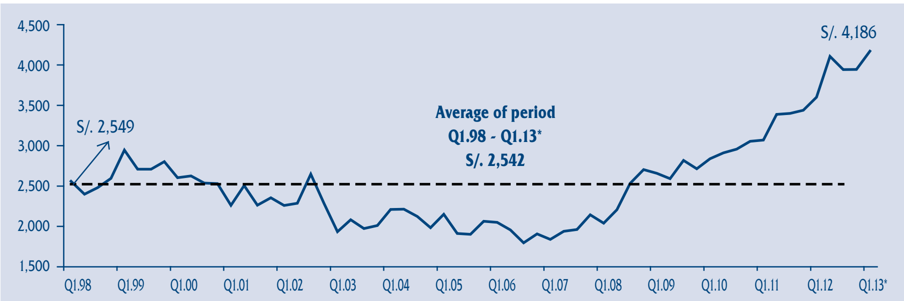
76. In the variable income market, the General Index of the Lima Stock Exchange (IGBVL) showed a slight contraction of 0.09 percent in February relative to December. This contraction was associated with uncertainty in international financial markets and with the evolution of the prices of minerals.

Graph 90
LSE: GENERAL INDEX
(January 2, 2012=100)

Real estate market

77. In line with the growth observed in the demand of mortgage-financed houses, the prices of property per square meter in five districts of the sample increased 15 percent at constant soles between Q4-2011 and Q4-2012. The graph below shows the evolution of quarterly median sale prices in constant soles per square meter of apartments.

Graph 91
MEDIANS OF QUARTERLY SALES PRICES
PER SQUARE METER OF APARTMENTS
La Molina, Miraflores, San Borja, San Isidro and Surco (Base 2009=100)



*Preliminary in February.

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

The PER ratio shows the number of years a property has to be rented in order that the purchasing value of the property be recovered. In Q4-2012, the purchasing value of an apartment is equivalent on average to the income obtained from 16 years of renting the apartment.

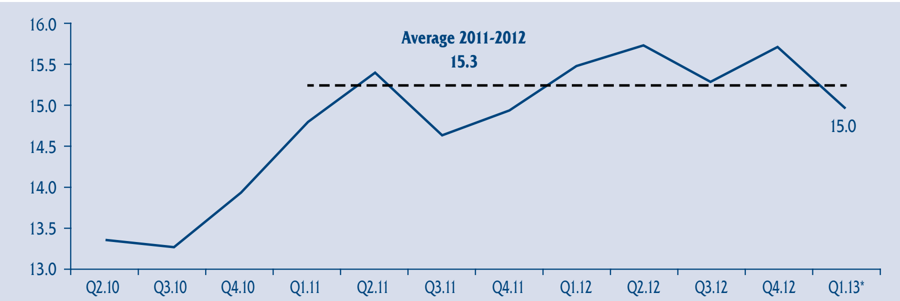
Table 43
PER: PRICE TO EARNING RATIO

MEDIANS 1/	Q2.10	Q3.10	Q4.10	Q1.11	Q2.11	Q3.11	Q4.11	Q1.12	Q2.12	Q3.12	Q4.12
Jesús María	11.8	10.5	11.9	12.6	13.1	12.9	13.0	13.0	15.7	15.5	14.9
La Molina	13.0	15.7	16.1	16.5	17.2	15.2	15.8	12.7	10.7	12.4	11.6
Lince	15.9	14.2	14.8	14.3	15.6	16.5	14.1	13.9	14.2	14.2	16.4
Magdalena	10.6	11.7	10.9	11.6	13.7	12.7	12.5	14.5	14.1	13.1	16.0
Miraflores	10.9	12.1	13.3	12.9	14.0	15.6	15.7	19.0	17.0	15.3	15.0
Pueblo Libre	14.5	13.6	14.1	15.6	15.6	15.0	15.3	15.4	16.5	15.2	16.0
San Borja	15.8	15.5	14.7	15.3	17.2	16.6	17.2	15.3	19.5	16.8	18.2
San Isidro	14.4	13.6	13.8	15.6	15.9	14.9	16.7	19.7	17.7	17.2	18.4
San Miguel	13.6	12.0	14.8	17.7	15.9	13.7	12.8	14.8	15.3	16.1	15.6
Surco	12.8	13.8	14.7	15.9	15.8	13.3	16.3	16.6	16.7	17.1	15.0
Aggregated											
Average	13.3	13.3	13.9	14.8	15.4	14.6	14.9	15.5	15.7	15.3	15.7

1/ 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.

Even though this ratio has shown a rising trend in recent years, it remains within the ranges considered normal, which, according to Global Property Guide, is between 12.5 and 25.

Graph 92
PER: PRICE TO EARNING RATIO

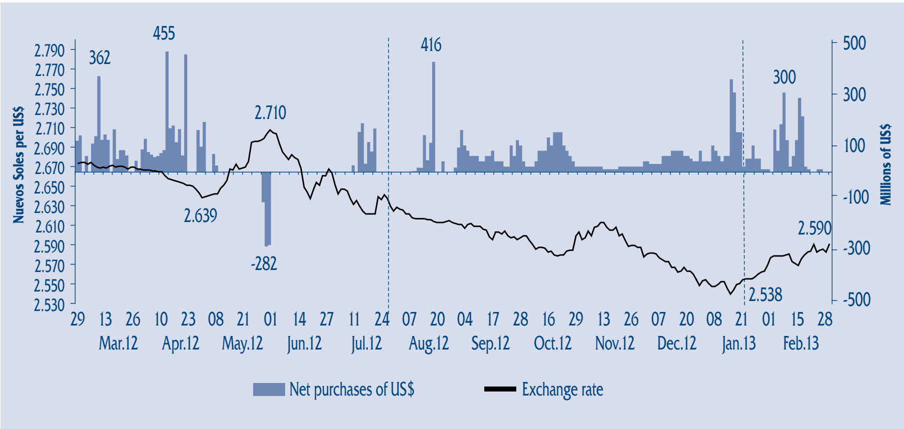


* Preliminary in February.

Foreign exchange rate

78. Noise in international markets generated expectations of appreciation at the beginning of the year leading some agents to advance their sales of foreign currency. However, in contrast with the trend observed in Q4-2012 when the exchange rate appreciated 1.73 percent, between the end of December 2012 and February 2013, the US dollar registered a nominal depreciation of 1.49 percent against the nuevo sol (from S/. 2.552 to S/. 2.59 per dollar). In this period, the Central Bank maintained its foreign exchange intervention strategy and intervened in the foreign exchange market even in periods of depreciation of the nuevo sol. Between December and February, the BCRP bought foreign currency for a total of US$ 3.36 billion in the foreign exchange market.

Graph 93
INTERVENTION IN THE FOREIGN EXCHANGE MARKET AND EXCHANGE RATE



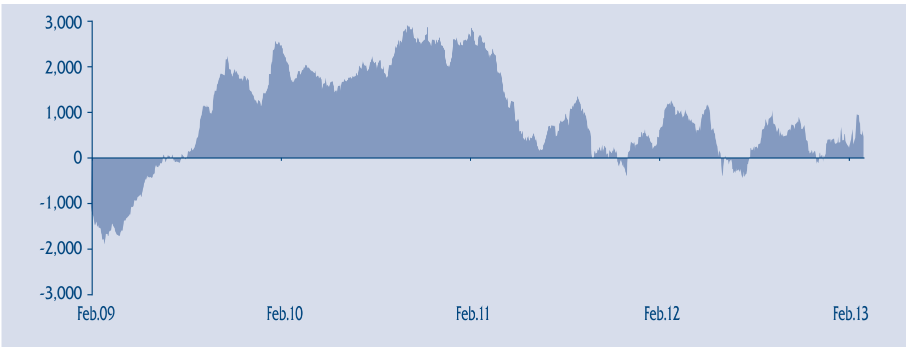
The intervention of the BCRP in the foreign exchange market was coupled by a series of measures aimed at reversing the appreciation trend of the exchange rate and changing economic agents' expectations. First, the BCRP intervention was carried out together with consecutive increases in the rate of reserve requirements in foreign currency, which restricted liquidity in dollars. Second, the investment limit for the AFPs' investment abroad was raised from 30 to 34 percent, which allowed offsetting capital inflows. Third, the Treasury announced purchases of foreign currency for a total of US$ 4 billion to prepay the external debt by US$ 1.68 billion, to deposit funds in the Fiscal Stabilization Fund, and to pay the current debt service. For this purpose, the Treasury issued sovereign bonds for a total of S/. 1.9 billion in the local market, which were mainly purchased by local investors.

The supply of dollars which in the period came mainly from private agents, such as mining companies and retail customers, was offset by non-residents demand for dollars in the forward market and by the interventions of the BCRP.

Graph 94
FOREX MARKET FLOWS
(Millions of US$)

Since the end of December, banks' net purchases of dollars in the forward market increased from US$ 393 million in December 2012 to US$ 464 billion in February 2013.

Graph 95
BALANCE OF NET FORWARD PURCHASES
(Millions of US$)



79. The net increase in non-residents' demand for forward contracts in February was US$ 658 million, which reflected that the exchange rate was expected to depreciate. It is worth pointing out that these flows exceed the amounts required by non-residents to cover their positions in Treasury bonds in domestic currency, which increased by US$ 124 million in February.

Table 44
AFP AND NON RESIDENTS: NET FORWARD BALANCE 1/
(Millions of US$)

	Non residents		AFP	
Date	Stock	Flow	Stock	Flow
Dec.12	3,792	1,842	-4,390	-1,872
Jan.13	3,619	-173	-4,114	276
Feb.13	4,277	658	-5,031	-917

1/ A positive balance indicates a foreign exchange position of purchases of forwards in foreign currency while a negative balance indicates a foreign exchange position of sales of forwards in foreign currency.

80. The survey on the exchange rate expected shows that financial agents and economic analysts reversed their expectations on an appreciation of the exchange rate due to the coordinated response of fiscal and monetary authorities and due to the effective depreciation of the dollar observed until February.

Table 45
SURVEY ON MACROECONOMIC EXPECTATIONS: EXCHANGE RATE
(Nuevos Soles per US$)

	Expectations about:		
	IR Sep.12	**IR Dec.12**	**IR Mar.13**
Financial entities			
2013	2.59	2.55	2.50
2014	2.58	2.50	2.45
Economic analysts			
2013	2.60	2.53	2.50
2014	2.60	2.50	2.45
Non-financial firms			
2013	2.65	2.60	2.55
2014	2.67	2.60	2.55
Average			
2013	2.61	2.56	2.52
2014	2.62	2.53	2.48

IR: Inflation report.
Source: Survey made during the second half of February 2013.

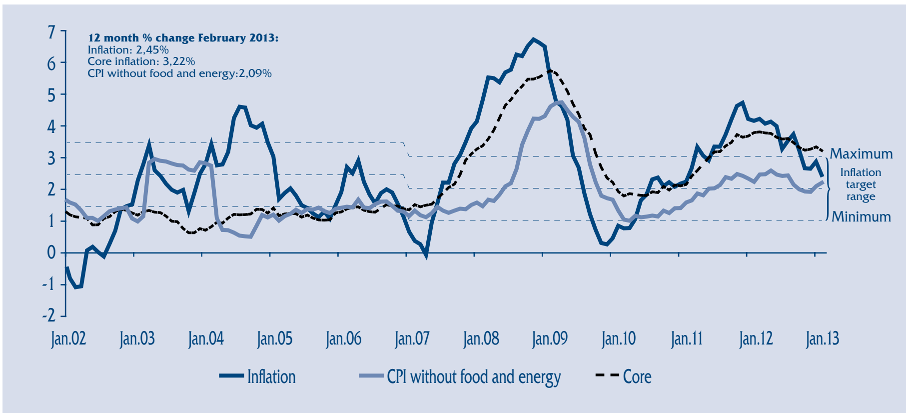
81. Between December 2012 and February 2013 the real multilateral exchange rate index rose from 88.8 to 89.0, which represented a real depreciation of 0.21 percent in the period and reached thereafter 0.80 percent in February. This real depreciation between December and February corresponds to a decline of -0.5 percent in the nominal rate against a basket of currencies and to a greater difference in the rates of inflation.

Graph 96
MULTILATERAL RER
(Index 2009=100)

VI. Inflation

82. The rate of inflation in the last twelve months continued declining, falling from 2.65 percent in December 2012 to 2.45 percent in February 2013, within the target range. One of the factors that contributed to this result was the fall in the prices of non-core food products due both to an increased supply and to the lower international prices of imported food inputs.

Graph 97
INFLATION AND INFLATION TARGET
(12 month % change)



83. At February the annual rate of core inflation, which excludes the items with higher volatility from the CPI, was 3.2 percent, similar to the rate observed in December (3.3 percent). The non-core component of inflation, which was affected by the rise in commodity prices in 2011, fell from an annual rate of 6.8 percent in December 2011 to 1.5 percent in December 2012 and to 1.0 percent in February 2013, reflecting mainly the dynamics of food prices, which dropped from a rate of 11.5 percent in December 2011 to 2.4 percent in December 2012 and to 0.2 percent in February 2013.

Inflation without food and energy rose from 1.9 percent in December to 2.2 percent in February, reflecting the price rises observed in services, especially in meals outside the home, education, and health.

Table 46
INFLATION
(Variación porcentual)

	Weight 2009=100	2006	2007	2008	2009	2010	2011	2012	February 2013 Acum.	February 2013 12 months
I. Inflation	**100.0**	**1.14**	**3.93**	**6.65**	**0.25**	**2.08**	**4.74**	**2.65**	**0.03**	**2.45**
II. CPI without food and energy	**56.4**	**1.28**	**1.49**	**4.25**	**1.71**	**1.38**	**2.42**	**1.91**	**0.22**	**2.20**
III. Core Inflation	**65.2**	**1.37**	**3.11**	**5.56**	**2.35**	**2.12**	**3.65**	**3.27**	**0.50**	**3.22**
Goods	32.9	0.97	3.30	5.32	2.17	1.53	3.17	2.56	0.31	2.41
Services	32.2	1.85	2.88	5.86	2.56	2.72	4.13	3.97	0.68	4.04
IV. Non core Inflation	**34.8**	**0.83**	**5.07**	**8.11**	**-2.54**	**2.00**	**6.79**	**1.52**	**-0.84**	**1.02**
Food	14.8	2.06	7.25	10.97	-1.41	1.18	11.50	2.36	-2.72	0.23
Fuels	2.8	-1.50	6.45	-0.04	-12.66	12.21	7.54	-1.48	1.53	0.72
Transportation	8.9	1.12	0.82	5.86	0.19	1.94	3.61	1.99	0.11	3.08
Utilities	8.4	-3.22	0.24	7.48	-4.56	0.01	1.50	0.54	0.92	0.41
Foodstuffs	**37.8**	**1.8**	**6.0**	**9.7**	**0.6**	**2.4**	**8.0**	**4.1**	**-0.5**	**3.1**

Table 47
INFLATION
(Weighted contribution)

	Weight 2009=100	2006	2007	2008	2009	2010	2011	2012	February 2013 Acum.	February 2013 12 months
I. CPI	**100.0**	**1.14**	**3.93**	**6.65**	**0.25**	**2.08**	**4.74**	**2.65**	**0.03**	**2.45**
II. CPI without food and energy	**56.4**	**0.58**	**0.67**	**1.88**	**0.74**	**0.78**	**1.36**	**1.05**	**0.12**	**1.20**
III. Core Inflation	**65.2**	**0.79**	**1.80**	**3.20**	**1.34**	**1.38**	**2.38**	**2.11**	**0.32**	**2.09**
Goods	32.9	0.31	1.05	1.69	0.68	0.50	1.04	0.82	0.10	0.78
Services	32.2	0.48	0.75	1.52	0.66	0.88	1.34	1.29	0.22	1.31
IV. Non core Inflation	**34.8**	**0.35**	**2.13**	**3.44**	**-1.09**	**0.69**	**2.36**	**0.54**	**-0.29**	**0.36**
Foods	14.8	0.48	1.69	2.63	-0.35	0.17	1.68	0.37	-0.42	0.04
Fuels	2.8	-0.09	0.36	0.00	-0.68	0.34	0.23	-0.05	0.05	0.02
Transportation	8.9	0.10	0.07	0.51	0.03	0.17	0.32	0.18	0.01	0.27
Utilities	8.4	-0.14	0.01	0.30	-0.09	0.00	0.12	0.04	0.07	0.03
Foodstuff	**37.8**	**0.63**	**2.17**	**3.56**	**0.21**	**0.91**	**3.03**	**1.59**	**-0.21**	**1.22**

84. At February imported inflation showed a last twelve month variation of 1.0 percent, a higher rate than in December 2012 (0.4 percent). The rise in the prices of fuels stands out with an annual variation that went from -1.5 percent in December 2012 to 0.7 percent in February 2013.

Graph 98
DOMESTIC AND IMPORTED INFLATION
(Last 12 month % change)

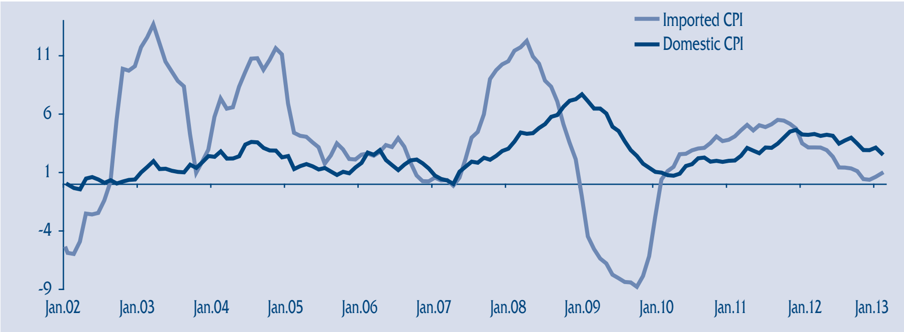


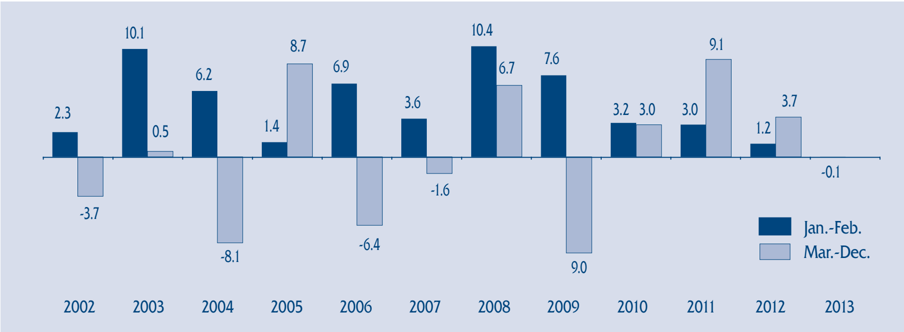
Table 48
DOMESTIC AND IMPORTED INFLATION: 2006 - 2013
(% change)

	Weight 2009=100	2006	2007	2008	2009	2010	2011	2012	2013 Jan-Feb	2013 12 months
I. IMPORTED CPI	**10.8**	**0.27**	**10.46**	**2.20**	**-6.25**	**3.78**	**4.87**	**0.41**	**0.44**	**0.97**
Food	3.0	2.08	18.83	4.75	-3.07	0.76	9.59	1.99	0.11	1.73
Fuels	2.8	-1.50	6.45	-0.04	-12.66	12.21	7.54	-1.48	1.53	0.72
Electric appliances	1.3	-1.29	-1.50	-0.06	-2.39	-0.58	-1.13	-2.44	-0.17	-2.41
Other	3.7	0.64	0.47	0.46	-0.34	1.20	0.83	1.73	-0.04	1.67
II. DOMESTIC CPI	**89.2**	**1.28**	**2.84**	**7.44**	**1.35**	**1.87**	**4.72**	**2.92**	**-0.02**	**2.63**
III. CPI	**100.0**	**1.14**	**3.93**	**6.65**	**0.25**	**2.08**	**4.74**	**2.65**	**0.03**	**2.45**
Exchange rate		**-6.40**	**-7.00**	**4.47**	**-7.59**	**-2.15**	**-4.24**	**-4.80**	**0.43**	**-3.94**
Imported without foods	6.7	5.57	11.66	4.96	-1.02	4.31	3.15	-0.20	0.57	0.68
Domestic food and beberages	42.1	2.18	3.04	1.52	1.72	4.14	7.83	4.23	-0.58	3.24
Domestic without foods	45.8	2.60	1.60	1.25	0.89	1.64	2.70	2.03	0.37	2.21

85. Accumulated inflation in January-February showed a rate of 0.03 percent and a variation in the last twelve months of 2.45 percent. This lower variation in the general price index reflected the lower rates recorded in the non-core component of inflation, especially in food.

The climate changes that usually affect the food supply in the first quarter of the year were offset by an increased supply of some food products which were favored by several factors, such as better weather conditions in the previous months and lower production costs due to the decline of the international prices of inputs, among others.

Graph 99
PRICE OF PERISHABLE AGRICULTURAL FOOD
(% change)



Between January and February the items that contributed most to reduce inflation were chicken meat, sugar, eggs, corn and potato, whereas the items that contributed most to the rise in inflation included meals outside the home and electricity rates. The rises in the prices of citrus fruits and other vegetables stand out too.

Table 49
ITEM WITH THE HIGHEST WEIGHTED CONTRIBUTION TO INFLATION:
JANUARY - FEBRUARY 2013

Positive	Weight	% Chg.	Contribution	Negative	Weight	% Chg.	Contribution
Meals outside the home	11.7	1.3	0.16	Chicken meat	3.0	-9.2	-0.29
Electricity	2.9	2.5	0.07	Sugar	0.5	-7.5	-0.05
Citrics	0.5	8.0	0.05	Eggs	0.6	-9.3	-0.05
Other vegetables	0.4	8.4	0.04	Corn	0.1	-20.9	-0.04
Gasoline and lubricants	1.3	2.2	0.03	Potato	0.9	-2.9	-0.03
Carrots	0.1	25.7	0.03	Fresh and canned fish	0.7	-3.8	-0.03
Papaya	0.2	13.5	0.03	Grapes	0.1	-17.3	-0.02
Urban fares	8.5	0.3	0.03	Onion	0.4	-6.4	-0.02
Fresh legumes	0.2	7.7	0.02	Banana	0.3	-5.6	-0.02
Beef	1.2	1.5	0.02	National transportation	0.3	-4.7	-0.02
Total			**0.48**	**Total**			**-0.57**

Table 50
ITEM WITH THE HIGHEST WEIGHTED CONTRIBUTION TO INFLATION:
MARCH 2012 - FEBRUARY 2013

Positive	Weight	% Chg.	Contribution	Negative	Weight	% Chg.	Contribution
Meals outside the home	11.7	5.9	0.73	Sugar	0.5	-17.9	-0.14
Education (fees and tuition)	8.8	4.8	0.43	Papaya	0.2	-23.5	-0.07
Urban fares	8.5	3.2	0.26	Eggs	0.6	-12.8	-0.07
Potato	0.9	15.1	0.13	Telephone rates	2.9	-2.2	-0.05
Water rates	1.6	5.2	0.09	Fresh and canned fish	0.7	-5.4	-0.04
Evaporated milk	1.6	5.4	0.09	Carrots	0.1	-18.4	-0.04
Toiletries	4.9	1.5	0.07	Gasoline and lubricants	1.3	-2.1	-0.03
Sodas	1.3	4.2	0.06	Rice	1.9	-1.6	-0.03
Beef	1.2	4.6	0.06	Plane tickets	0.4	-6.3	-0.02
Gas	1.4	3.7	0.05	Apparatus of recreation and culture	0.9	-3.0	-0.02
Total			**1.97**	**Total**			**-0.51**

Inflation components at February 2013

86 After closing 2012 with an increase of 9.3 percent, the price of **chicken meat** showed negative growth rates in the first two months of the year. Factors accounting for this result included the lower price of substitute products like fish, mainly mackerel and bonito; the increase in placements of baby chicken (up about 3 percent compared with the same period of the previous year), and the decline in the international price of maize –the main input of chicken food– from US$ 319 in August 2012 to US$ 282 in December and to US$ 280 in February.

The price of **eggs** dropped 9.3 percent, mainly as a result of an increase in production (8.8 percent at January) associated with a decrease of production costs due to the lower international prices of maize, as well as with technical improvements implemented in the industry.

The price of **sugar** fell 7.5 percent due mainly to an increase in the domestic production of sugarcane (7.9 percent in January) as well as to the decline in the international price of sugar, which dropped from US$ 515.7 in December 2012 to US$ 500.8 in January 2013 and to US$ 498.16 in February (contract 5).

The prices of farming products, such as **potatoes** and **corn**, fell too. A good level of supply was observed in both products. However, it is worth pointing out that even though there was less cultivation of potatoes in the second half of 2012, the supply of potatoes increased since lower rainfall facilitated the harvest of this crop.

Meals outside the home continued showing the rising trend observed over the past five years. In January-February this item showed an accumulated variation of 1.3 percent, higher than the general index (0.03 percent) and higher than the variation of total food and beverages consumed at home (-1.4 percent).

The rise in the prices of **gasoline** and **lubricants** resulted from higher oil prices. The international price of WTI oil rose from US$ 89.2 in December 2012 to US$ 94.5 in January and to US$ 95.6 in February.

Other price increases that contributed to inflation were the rise in **electricity rates** decreed by Osinergmin as a result of new supply contracts effective as from January and the quarterly generation rate established in February taking into account the higher price of natural gas as well. In addition to this, the toll of the main transmission system and the onset of operations of a new transmission line (Zapallal-Trujillo) were also updated.

Inflation forecast

87. In line with the forecasts of our December report, in February inflation in the past 12 months fell within the target range with a rate of 2.44 percent. The forecast

of inflation in the next two years considers the evolution of the economic cycle, the supply factors that affect the prices of energy and food, and inflation expectations.

The **output gap** measures the cyclical fluctuations of economic activity that become inflationary pressures on the side of demand. The forecast considers that the negative external impulse, characterized by an international environment of still-weak global growth, would be offset by a positive fiscal impulse and by a positive private impulse in a context of consumers and entrepreneurs' optimistic expectations. Thus, a neutral economic cycle with an output gap close to zero is forecast for the next years. This implies that no domestic demand pressures that would affect the inflation rate are foreseen in the forecast horizon.

The supply factors that affect the rate of inflation can have an external or a domestic origin. As regards the external factors, the forecast considers lower international price levels in **food commodities** such as maize and wheat than those considered in the inflation report of December. This effect would be partially offset by a price of oil forecast to be around its current level, which equates to an upward revision of the forecast compared to our previous report. In the case of domestic factors, assuming normal weather conditions, no significant increases are foreseen in the prices of **perishable agricultural products**.

According to the BCRP survey on expectations, the **inflation rate expected** for next year has also declined in recent months and is within the target range.

In sum, the central forecast scenario considers that no major inflationary pressures associated with increases in the prices of commodities would be observed and that inflation expectations would remain within the target range. Inflation would remain within the target range, converging thereafter in the following months to the 2.0 percent target. In 2013 and 2014 inflation would show rates within a range of 1.5 and 2.5 percent.

Table 51
INFLATION: 2009 - 2013
(Last 12 month % change)

	Weight	2009	2010	2011	2012	2013		
						Feb.	Year* IR Dec. 12	Year* IR Mar.13
CPI	**100.0**	**0.2**	**2.1**	**4.7**	**2.6**	**2.4**	**2.0**	**2.0**
Food and energy	43.6	-0.9	3.0	7.7	3.6	2.8	2.5	2.4
a. Food	37.8	0.6	2.4	8.0	4.1	3.1	2.4	2.2
b. Energy	5.7	-10.4	6.8	6.0	0.2	0.4	3.2	3.7
CPI without food and energy	56.4	1.7	1.4	2.4	1.9	2.2	1.5	1.7

* Forecast.

88. Core inflation would be lower than 2 percent due to better climate conditions and to the favorable evolution of the international prices of food. The main factors that affect the path of **core inflation** are the output gap, imported inflation, and inflation expectations.

In the forecast horizon, the central scenario considers that GDP will grow at rates close to the economy's potential growth, which equates a neutral economic cycle. Therefore, no major demand inflationary pressures are expected in this period.

Moreover, the component of imported inflation is expected to show a relatively rapid normalization which would contribute to reduce inflation in the forecast horizon.

Finally, inflation expectations are foreseen to remain anchored within the target range and to gradually converge towards 2 percent. In mid-2012, inflation expectations fell close to the upper band (3 percent) of the target range due to the supply shocks on the prices of food and energy that affected the rate of inflation.

Output gap

89. The **output gap** measures the cyclical fluctuations of economic activity that become inflationary pressures on the side of demand. 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 impulse is expected to be similar, in line with the pace of growth foreseen in our trade partners and with relatively stable terms of trade. In addition, this forecast scenario also considers a positive fiscal impulse of 0.7 percent in 2013, in line with a higher growth of public expenditure. Thus, in 2013 the negative contribution of the external impulse on the output gap would be offset by the conduct of the fiscal impulse. A slightly contractionary fiscal impulse is projected for 2014.

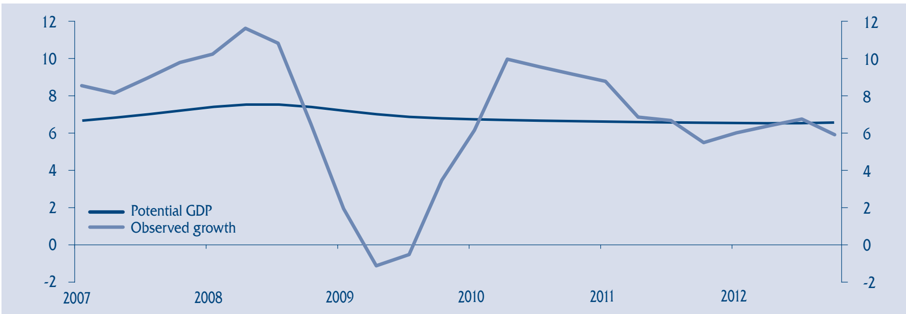
Moreover, both private consumption and private investment would maintain the dynamism observed recently, which would translate into a positive private impulse over the forecast horizon.

Finally, the baseline forecast scenario considers a monetary policy position which would not be substantially different in the short term from the one observed today. 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.

Graph 100
OUTPUT GAP: 2007 - 2014
(% of potential GDP)

The economy's potential growth was around 6.3 percent in 2012. In the next two years the growth of the potential output is projected to remain at similar levels. This projection is consistent with a greater accumulation of physical capital, derived from the high growth rates of fixed gross investment in 2012 and the growth rates foreseen for the period 2013-2014.

Graph 101
POTENTIAL GDP GROWTH AND ACTUAL GROWTH: 2007 - 2014
(% change in the last 4 quarters)



It should be pointed out that the GDP forecasts included in this report are based on the assumption that there will be no power rationing between 2013 and 2015, in line with the projected balance of electricity supply and demand in the horizon analyzed considering no significant or persistent power generation and transmission failures.

However, recent evidence shows that the degrees of vulnerability of the Peruvian electricity system should warn us about the investments required to be made to increase the reserve system[9]. The vulnerability of the electrical system in the

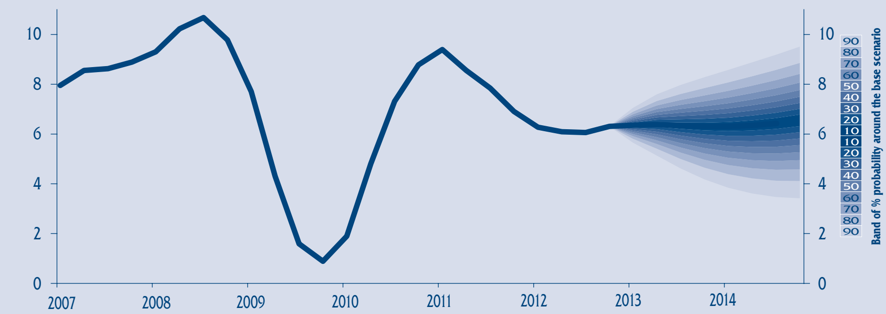
9 A total of 25 partial and transitory power cuts were observed in the country between January and February 2013 due mostly to electricity generation and transmission failures (versus 15 in the same period in 2012). Three of these power interruptions exceeded 250 MW, that is, approximately 5 percent of the maximum demand (versus 1 in the same period in 2012).

event of generation and transmission failures is mainly explained by its limited reserve of electrical supply (reserve margin), which is less than 10 percent of the peak demand that would be observed in the season of scarce rainfall in the period 2013-2015.

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

Adverse demand shocks associated with the impact of social conflicts on private investment could occur in a scenario of risks of internal origin. In addition, constraints in the supply of electricity could be observed on the supply side due to the low electricity reserve margin available. On the other hand, although some improvement has been observed in the global economy recently, there is still uncertainty about whether the evolution of the global economy may contribute to deteriorate macroeconomic conditions. Despite this, massive capital inflows motivated by investors' search for profitable investment alternatives in the emerging economies would be observed in a context of abundant liquidity in international markets. The risk scenarios referred to in this report are discussed in the chapter of Balance of Risks.

Graph 102
FORECAST OF GDP GROWTH 1/, 2013 - 2014
(Interanual % change)



1/ GDP growth is defined 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.

Energy and food prices

a. Energy

91. In 2012, the price of WTI oil dropped 0.9 percent to an annual average of US$ 94 per barrel. The downward trend observed in the price of oil during most of the year was associated with a production increase in the USA which reached levels unseen in at least 15 years (due to the rise in the production of non-conventional crude) and with the OPEC's higher production than those announced.

However, in the first two months of 2013 the price of WTI oil increased 8.0 percent –from US$ 88 per barrel in December to a monthly average of US$ 95 per barrel in February–. This increase, which was mainly recorded in January, was influenced by the reduction of the OPEC's actual high levels of production in the months of November and December 2012 (Saudi Arabia reduced its production) and by the decrease of crude oil inventories in Oklahoma associated with the onset of operations of the Cushing pipeline (oil is transported through this pipeline from Oklahoma to the refineries located in the Gulf of Mexico). This upward trend has been reversing since mid-February after the crude oil production in the U.S. continued to be revised upwards and after the projected global demand for oil was revised downwards according to the International Energy Agency.

The current scenario shows an adequate supply of oil in the world market, but there are still upside risk factors in the Middle East and it is estimated that inventories in Oklahoma will continue to be near their current levels (i.e. lower than those considered previously). In the forecast horizon, WTI oil prices would stabilize around their current level (slightly higher than the one considered in our previous report).

Graph 103
WTI OIL: JANUARY 2007 - DECEMBER 2014
(US$/bl)

b. Imported food products

92. In 2012, FAO's real food price index showed an annual average decline of 8.1 percent. Prices fell during most of the year, except during the beginning of the third quarter when the prices of cereals increased due to the effects of a severe drought in key agricultural areas of USA.

Food prices declined during the first two months of 2013 and the FAO index registered a fall of 0.9 percent. The price increases in vegetable oils were offset by the fall in the prices of cereals, which reflected mainly the reduction in the price of wheat and, to a lesser extent, the decline in the price of maize.

Graph 104
FAO REAL FOOD PRICE INDEX*
(Base 2002 - 2004 = 100)

* The real price index is the index of nominal prices deflated by the unit value of manufactures of the World Bank.

According to Global Food Supply and Demand Balance of the Department of Agriculture of the United States (USDA) of March 2013, tighter market conditions with drops in the global final inventories of the major products are being observed in the current 2012/13 farming season. However, the first production forecasts for the following season (2013/14) not only reveal an improvement in the future supply of maize and soybean, but also project record production levels. The estimates indicate that grain prices would fall with the new season if no weather problems are observed.

Table 52
USDA: GLOBAL FOOD SUPPLY AND DEMAND BALANCE
(Millions tons)

	2010/11	2011/12	2012/13	% change	
	(3)	(2)	(1)	(2) / (3)	(1) / (2)
MAIZE					
Initial stock	145.9	128.1	131.2	-12.2	2.4
Production	832.5	882.7	854.1	6.0	-3.2
Global supply	**978.4**	**1,010.8**	**985.2**	**3.3**	**-2.5**
Total consumption	850.3	879.6	867.8	3.4	-1.3
Final stock	128.1	131.2	117.5	2.4	-10.4
WHEAT					
Initial stock	201.0	197.9	196.5	-1.5	-0.7
Production	652.2	697.0	655.5	6.9	-6.0
Global supply	**853.2**	**894.9**	**852.0**	**4.9**	**-4.8**
Total consumption	655.3	698.5	673.7	6.6	-3.5
Final stock	197.9	196.5	178.2	-0.7	-9.3
SOYBEAN OIL					
Initial stock	3.3	3.5	3.8	7.6	8.2
Production	41.3	42.4	43.2	2.7	1.8
Global supply	**44.6**	**45.9**	**47.0**	**3.1**	**2.3**
Total consumption	40.8	41.8	43.4	2.5	3.8
Final stock	3.5	3.8	3.3	8.2	-12.3

Source: USDA - WASDE March 2013.

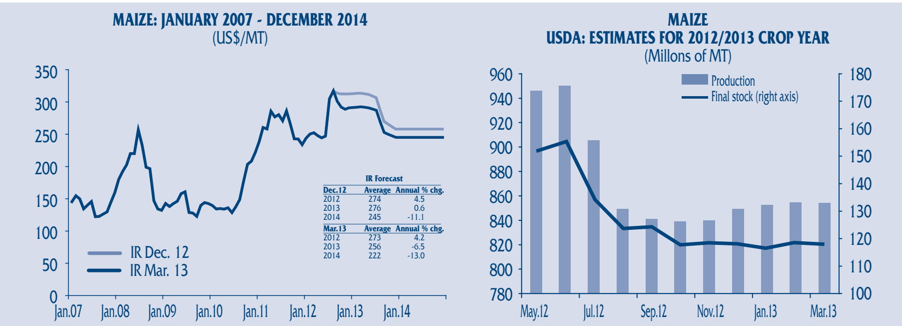
Maize

93. Slowing its pace of growth relative to 2011 when it rose 66.9 percent, the price of **maize** in 2012 showed an increase of 4.2 percent. In December, maize registered an average price of US$/ton 282 and in February 2013, an average price of US$/ton 280, thus showing a decline of 0.7 percent so far this year. With this, the price of maize accumulates six straight months of decline and reverses the strong rise seen in mid-2012, associated with the severe drought that affected USA.

The decline in the first two months of this year was associated with expectations of a recovery in global supply. The USDA announced that the USA will have a record production in 2013/14 due to the recovery of yields in this crop.

In line with this, it is estimated that food prices in the forecast horizon will show lower levels than the ones considered in our report of December 2012. However, considering that the USDA forecast for the 2013/14 season is preliminary and that some producing areas of USA continue to be affected by the drought, there are risks on the upside.

Graph 105



Source: USDA.

Wheat

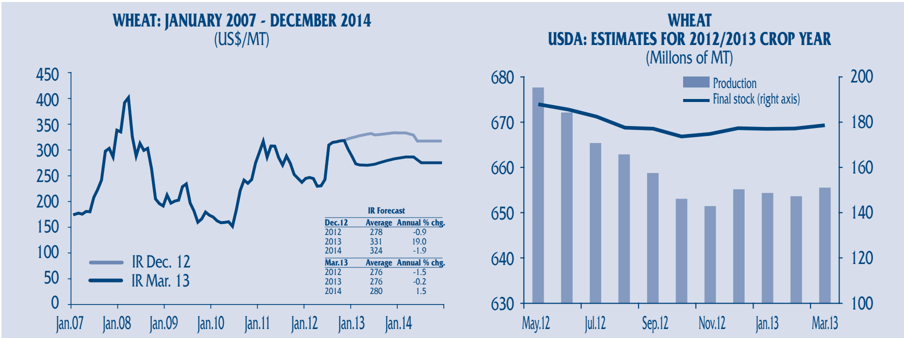
94. The international price of **wheat** declined 1.5 percent in 2012, after having increased 43.7 percent in 2011. In the first two months of this year, the price continued to decline registering an accumulated drop of 9.7 percent (down from a monthly average of US$/ton 302 in December 2012 to US$/ton 273 in February).

The decrease accumulated at the second month of the year is associated with the USDA's upward revision of global final inventories, with a lower demand for U.S. wheat in international markets, and with better weather conditions registered in the USA. The winter wheat harvest in the USA has been more favorable than expected, which has led to seasonally low prices.

As a result of an expected higher global production due to increased production in India and in European countries as well as of better weather conditions in U.S.

producing areas, the price of wheat is expected to register lower levels than those estimated in our previous Inflation Report.

Graph 106



Source: USDA.

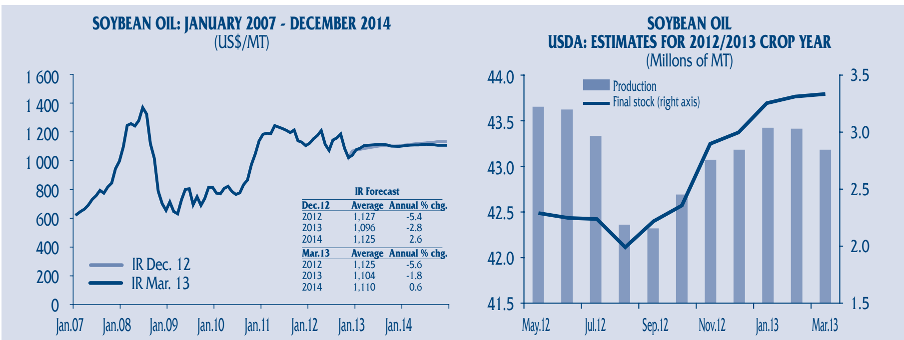
Soybean oil

95. In 2012 the price of **soybean oil** fell by an average of 5.6 percent and closed with an annual average price of US$/ton 1,125 in December, reversing in part the 38.6 percent increase registered in 2011. During the first two months of 2013, the price of soybean oil rose 4.8 percent, closing February at an average price of US$/ton 1,088.

This increase is associated with both the behavior of the international price of oil and with the determinants of the supply of soybean, i.e. the increased demand for soybean oil, especially of China. In addition to this, the USDA revised down the production projected in Argentina for the period 2012/13, and the distribution of Brazil's supply of soybean was affected by shipping logistics problems in Brazilian ports.

Based on these factors as well as on the higher oil prices foreseen, it is estimated that soybean oil will register higher price levels than those considered in our previous report.

Graph 107

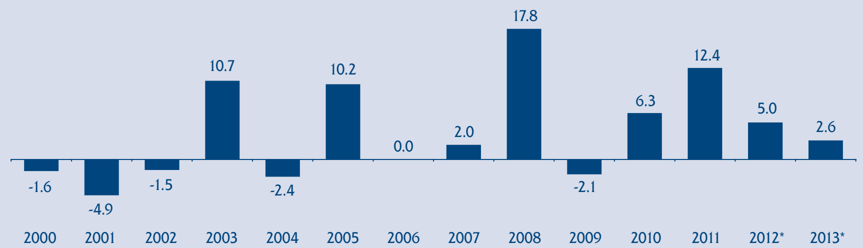


Source: USDA.

c. Perishable agricultural food products

In 2012, the supply of perishable food products was affected by climate anomalies until Q3. In contrast, normal weather conditions are expected in 2013, with the consequent lower price increase in this group of products.

Graph 108
PRICE OF PERISHABLE AGRICULTURAL FOOD
(% change)



* Forecast.

A price increase is usually observed in perishable foodstuffs in the first quarter of the year due to a lower seasonal supply derived from lower crop yields and increased rainfall. However, perishable foodstuffs have not been affected in the same degree by these factors in January and February of this year given that some crops have been favored by the better weather conditions registered in the last months of 2012.

However, heavier rains are expected in Cuzco, Huancavelica, and in parts of Arequipa, Ayacucho, and Huánuco in March. Junín would not be very affected, although heavy rains could cause landslides and interrupt the transportation of products to Lima as in other years.

In contrast to what happened in previous years, on the coast there has been a good crop management with pest and disease controls and the water reservoirs of the north coast are also expected to have the required level of water to ensure a good farming season. Rains are expected to decline from April and temperatures are foreseen to be within the normal ranges.

Lemon

The production of **lemons** in the past two years has faced climate disturbances. In 2011, the blooming of plants and the formation of fruits were affected during most of the year by low temperatures caused by La Niña event. In 2012, production was affected in Q3 due to climatic variability in the previous months, normalizing thereafter since October as reflected in a good level of supply and in a price reversal in the first months of 2013. This trend would reverse from now on since rainfall in the early days of March have caused flowers to fall and this would affect the supply in the second semester.

Potato

A rise in the supply of potatoes that come from the central highlands is expected in March-June due to increased yields in the large crop season. These higher yields could offset the decline observed in terms of areas cultivated with potatoes, which would recover in the coast due to the higher prices observed in that period.

Papaya

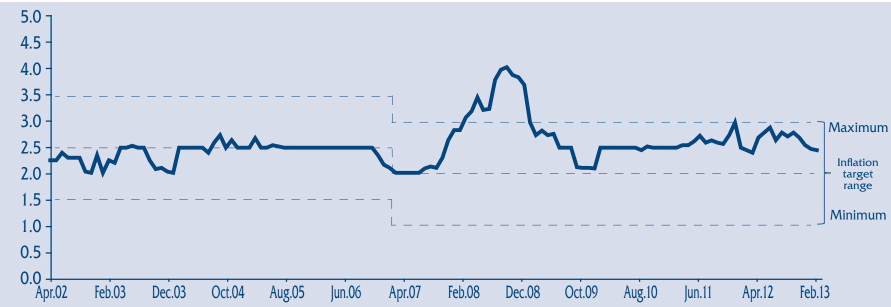
After registering a sharp decline in production in 2011 due to the overflowing of several rivers and the presence of pests in Ucayali, the production of papaya recovered in 2012 as a result of the onset of production in new plantations and better weather conditions in Ucayali which have led the price of this fruit to drop in 2012. So far this year, the supply of this crop to Lima has not been affected by rains as there is a higher production in San Martin. A good level of supply is estimated in the rest of the year.

Expectations of inflation

96. As in our Inflation Report of December, economic agents continue to expect inflation levels that are within the Central Bank's inflation target range for 2013 and 2014. Inflation levels of between 2.5 and 3.0 percent are expected in 2013, declining thereafter in the forecast horizon to values of between 2.4 and 3.0 percent in 2014.

According to the BCRP survey of expectations, the rate of inflation expected for next year also show a downward conduct in recent months and fall within the target range.

Graph 109
INFLATION EXPECTATIONS FOR THE NEXT YEAR*
(%)



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

Expected inflation levels are foreseen to continue declining and to converge to a rate close to 2 percent in the next two years. The transitory increase observed in the rates of expected inflation reflected that inflation had been affected by supply shocks in food and energy prices. Since these shocks have reversed at end 2012, the expected levels of inflation have corrected downwards.

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

	Expectations about:		
	IR Sep.12	IR Dec.12	IR Mar.13
Financial entities			
2013	2.8	2.6	2.7
2014	2.5	2.5	2.5
Economic analysts			
2013	2.8	2.8	2.5
2014	2.5	2.5	2.4
Non-financial firms			
2013	3.0	3.0	3.0
2014	3.0	3.0	3.0

IR: Inflation report.
Source: Survey conducted during the second half of February 2013.

Finally, the baseline forecast scenario considers a monetary policy position which will not be substantially different in the short term from the one held today. A suitable position of monetary policy contributes to keeping inflation expectations anchored, in particular in a context of persistent significant shocks that affect sensitive products in the CPI basket. The Central Bank will continue to oversee developments in the world economy and in the domestic economy to adjust its monetary policy position if required in order to maintain inflation within the target range.

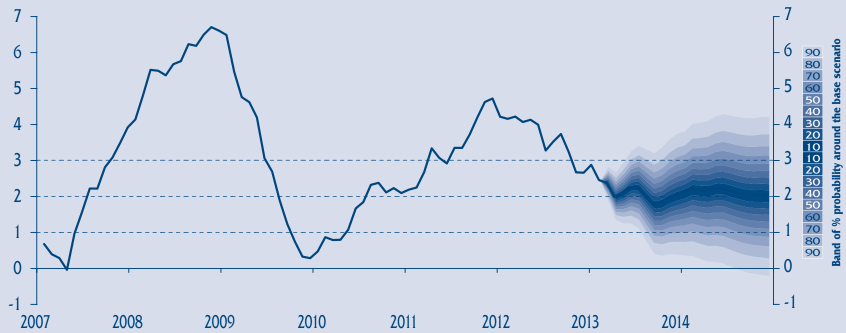
Forecast

97. The evolution of the variables described in this report 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 based on alternative forecast assumptions that divert inflation from the baseline scenario are also assessed here.

This is illustrated in the following graph. 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 the information available at February 2013, the probability that inflation will fall within the target range in 2013 and 2014 is approximately 65 percent and the probability that it will be below 3 percent is 70 percent.

Graph 110
INFLATION FORECAST: 2013 - 2014
(Last 12 month % 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

98. The baseline scenario for the inflation forecast takes into account relevant data on macroeconomic and financial variables as well as information on the domestic and international environment that is complemented with qualitative information not necessarily considered in statistical data.

    Given that the forecast process is not free from uncertainty about future developments in the domestic and in the global economies, other scenarios based on alternative forecast assumptions that, in the end, divert inflation from the baseline scenario are also evaluated in the balance of risks in addition to the baseline scenario.

    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 the risk scenario. Together, these two factors determine the bias of the inflation forecast in the balance of risks.

99. 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 and the international flow of capitals, the evolution of domestic demand and the impact of commodity prices in international markets, and adverse climate conditions. The balance of these risks remains neutral, although the perception of the expected impact of each of these risks has changed. The graph in this section shows the expected impact of each of these risk factors on the inflation forecast in a 2-year horizon.

    The **downward risk** scenarios in the inflation forecast are external factors associated with the potential unfolding of an international financial crisis.

    a. Uncertainty about the world economy.

    Even though a growth rate of global economic activity similar to the one forecast in our December Inflation Report is considered in the baseline scenario, this estimate could be conservative given growing uncertainty in international markets due to the lack of agreement on fiscal policy in the United States, to the worsening of the debt problem in the Eurozone, and to the economic deceleration observed in some emerging economies. A deepening of these risk conditions would bring about a lower global growth and a weakening in external demand, which would affect the Peruvian economy through financial and trade channels .

A drop in global economic activity coupled by a reduction in the terms of trade would take place in this adverse international scenario. In addition, the increase of global uncertainty could generate panic among investors and trigger a sudden stop –a sudden capital reversal– with a real depreciation and an increase in the country risk. In this context, international interest rates are expected to remain low for a longer period of time than the one considered in the baseline scenario.

Should these risks occur and materialize, the Central Bank would use the significant amount of the international reserves it has available as well as various liquidity injection mechanisms, both in national currency and in foreign currency, to offset the impact of this shock on domestic financial conditions. Should it be required, the Central Bank would respond by easing monetary conditions.

It should be pointed out that the expected impact of this hypothetical scenario of international economic downturn is the same as that considered in our December Inflation Report. This revision considers recent information indicating a more moderate growth in the United States and signs of a recovery of growth in China. Notwithstanding, the negative impact of this scenario is still latent as long as the persistence of the problems in the Eurozone continue affecting uncertainty and market volatility.

On the other hand, there are scenarios of **upward risk** for inflation associated mainly with an increase in capital inflows and a rise in commodity prices.

b. Increased capital inflows.

The high availability of liquidity in international markets due to the aggressive expansion of the balance sheets of central banks in developed countries, on the one hand, together with few attractive investment options in a context of high global uncertainty, on the other hand, could attract foreign capital inflows to emerging economies such as the Peruvian economy. A greater capital inflow would accelerate the expansion of credit, stimulating aggregate demand and inflation, on the one hand, but on the other hand, this would generate appreciatory pressures on the exchange rate, which would translate into lower domestic inflation.

In this scenario, the Central Bank would adjust its monetary position and its macro prudential policy instruments, such as the rates of reserve requirements. This scenario of higher capital inflows has a similar expected impact to that considered in our December Inflation Report.

c. Imported inflation and adverse climate conditions.

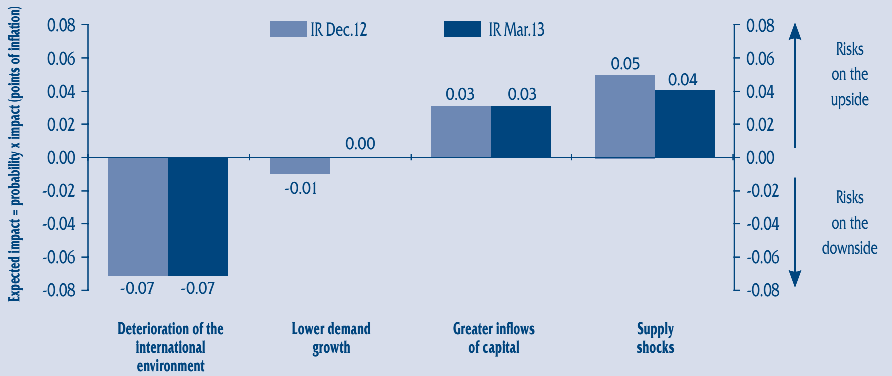
Like in the December Inflation Report, the risk of higher international prices of oil crude and oil derivatives is also considered in this report due to market fears regarding a deepening of international geopolitical tensions. Should this risk occur, global inflationary pressures would be more persistent than what they are currently expected to be.

The risk of weather conditions that could affect the normal development of the production and supply of food products remains in the domestic arena.

In this scenario, the Central Bank would adjust its monetary position only if these supply shocks were to "contaminate" or affect economic agents' expectations of inflation. It should be pointed out, however, that the impact of this scenario of internal and external shocks is lower than the impact considered in our December Inflation Report, which reflects the reversal of supply shocks observed recently.

The effects of risk factors pushing inflation downwards are offset by the effects of risk factors pushing it upwards. Thus, the balance of these risks is neutral for the inflation forecast in late 2014. Based on the information available to date, the probability that inflation will be below the projected level of the baseline scenario is the same as the probability that it will be above this level.

Graph 103
BALANCE OF RISKS AGAINST THE BASE SCENARIO



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 risks for the inflation forecast is neutral in the forecast horizon. In other words, the probability that inflation will fall below the projection in the baseline scenario is the same as the probability that it will fall above this projection. The sum of the bars in the graph is the same as zero.

Conclusion

100. The annual rate of inflation has been declining within a context of reversal of supply shocks, declining levels of expected inflation within the target range, lower imported inflation, and a neutral economic cycle. With this, the path of inflation would remain within the target range in 2013 and 2014. The balance of risks is neutral.

 It is estimated that the GDP would continue to grow at rates close to the economy's potential growth, with domestic demand showing a dynamic evolution.

 The Central Bank will continue to oversee the evolution of inflation forecasts and inflation determinants to adjust its monetary policy position if required to do so in order to maintain inflation within the target range. In addition to this, in order to prevent an excessive growth of credit and to reduce the vulnerabilities associated with dollarization, the Central Bank will continue taking actions such as changing the rates of reserve requirements.