CENTRAL RESERVE BANK OF PERU

Summary
Inflation Report

March 2016

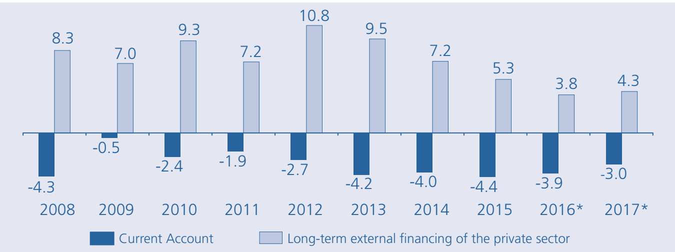
This ***Inflation Report*** was prepared using data on the Balance of Payments and Gross Domestic Product at Q4-2015 and data on Monetary Accounts, Inflation, Financial Markets, Exchange Rate and Non - Financial Public Sector at February 2016.

GDP GROWTH
(Annual % change)

	PPP % 2015	Trading Peru % 2015	2014	2015	2016* RI Dec.15	2016* RI Mar.16	2017* RI Dec.15	2017* RI Mar.16
Advanced economies	**42.4**	**47.4**	**1.8**	**1.9**	**2.2**	**1.9**	**2.1**	**2.0**
Of which:								
1. United States of America	15.9	17.5	2.4	2.4	2.6	2.2	2.6	2.3
2. Eurozone	12.0	11.0	0.9	1.5	1.6	1.5	1.7	1.7
Germany	3.4	2.8	1.6	1.5	1.5	1.5	1.5	1.5
France	2.3	0.9	0.2	1.1	1.4	1.2	1.5	1.6
Italy	1.9	1.7	-0.3	0.8	1.2	1.1	1.2	1.2
Spain	1.4	2.5	1.4	3.2	2.5	2.7	2.1	2.1
3. Japan	4.3	3.0	0.0	0.4	1.3	0.9	0.4	0.6
4. United Kingdom	2.4	1.1	2.9	2.2	2.4	2.1	2.2	2.2
5. Canada	1.4	4.4	2.5	1.2	2.1	1.6	2.2	2.2
Emerging market and developing	**57.6**	**52.6**	**4.6**	**4.0**	**4.3**	**4.3**	**4.7**	**4.7**
Of which:								
1. Developing Asia	30.9	26.9	6.8	6.6	6.4	6.4	6.2	6.3
China	17.2	22.2	7.3	6.9	6.4	6.5	5.9	6.2
India	7.1	2.2	7.2	7.3	7.4	7.4	7.6	7.6
2. Commonwealth of Independent States	4.4	0.7	1.0	-2.6	0.7	0.0	1.9	2.0
Russia	3.1	0.5	0.6	-3.7	-0.2	-1.1	1.0	1.2
3. Latin American and Caribbean	8.3	23.2	1.3	-0.1	0.5	-0.4	2.3	1.8
Brazil	2.8	4.1	0.1	-3.8	-1.8	-3.5	1.5	0.0
Chile	0.4	3.2	1.9	2.1	2.6	2.2	3.2	2.7
Colombia	0.6	3.0	4.6	3.1	2.5	2.4	3.5	3.2
Mexico	2.0	3.4	2.1	2.5	2.8	2.6	3.3	2.9
Peru	0.3	-	2.4	3.3	4.0	4.0	4.8	4.6
World Economy	**100.0**	**100.0**	**3.4**	**3.1**	**3.4**	**3.3**	**3.6**	**3.6**
Peru's trading partners 1/	66.2		3.6	3.1	3.2	2.9	3.4	3.2
BRICs 2/	30.2		5.8	4.9	5.0	5.0	5.3	5.4

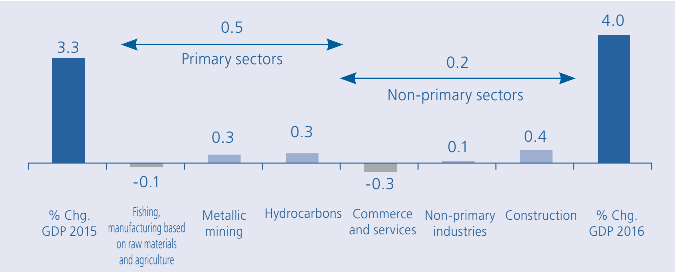
* Forecast.
Source: Bloomberg, IMF and Consensus Forecast.
1/ Basket of Peru's 20 main trading partners.
2/ Brazil, Russia, India and China.
IR: Inflation Report

CURRENT ACCOUNT AND LONG-TERM EXTERNAL FINANCING OF THE PRIVATE SECTOR: 2008-2017 1/
(% GDP)



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

GDP GROWTH: 2016 VS. 2015
(% Chg. and % contributions)



Reflecting lower economic dynamism in economies like China, Russia, and Brazil, the rate of global growth in 2015 was the lowest rate recorded since 2009. A gradual recovery of growth is forecast for 2016 with a rate of 3.3 percent (versus 3.1 percent in 2015). In contrast with what was observed in previous reports, today the developed countries account mostly for the downward revision of global growth due to uncertainty in financial markets, fears of deflation in Europe, and the strengthening of the dollar observed until recently. The forecast of global growth in 2017 remains at 3.6 percent, although growth in the region has been revised on the downside (1.8 percent in 2017 versus 2.3 percent in our previous Report).

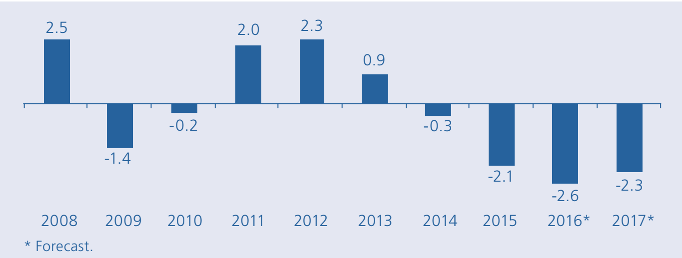
In 2015 the deficit in the current account of the balance of payments was higher than in 2014 (4.4 percent of GDP versus 4.0 percent). Nonetheless, a lower current account deficit is forecast for 2016 (3.9 percent) as a result of increased volumes of traditional exports. In line with the strong growth of mining exports and with the slight improvement of the terms of trade, the deficit in the current account is foreseen to decline from 3.9 percent in 2016 to 3.0 percent in 2017.

Peru's GDP grew 3.3 percent in 2015, higher than estimated in our previous Inflation Report (2.9 percent), due to the better output in metal mining as a result of the expansion of Cerro Verde and the start of operations at Las Bambas.

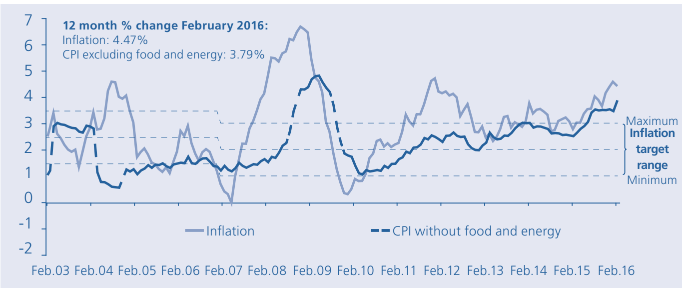
The growth forecast for 2016 remains at 4.0 percent –as estimated in our Inflation Report of December–, but with a higher contribution to growth from the primary sectors resulting from the higher production levels being observed in some mining units like Cerro Verde, for example. In addition to this, the earlier-than-initially foreseen start of operations at Las Bambas has also been considered here. On the other hand, the growth forecast of the non-primary sectors has been revised down due to the impact that lower growth in the Latin American region would have on non-primary manufacturing as well

GPD: 2008 - 2017
(Real % change)

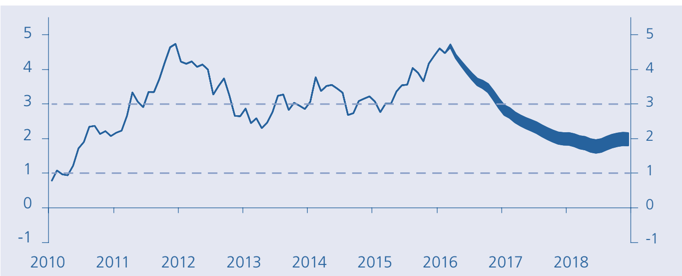
ECONOMIC BALANCE OF THE NON-FINANCIAL PUBLIC SECTOR: 2008-2017
(% GDP)



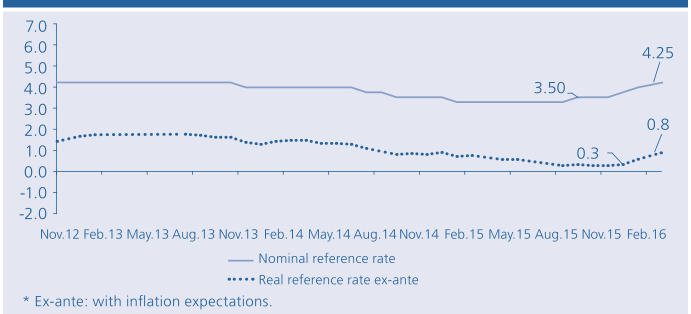
INFLATION AND INFLATION TARGETING
(Last 12 month % change)



INFLATION FORECAST: 2010-2018
(Last 12 month % change)



NOMINAL AND REAL REFERENCE INTEREST RATE*
(%)



as due to the impact of a lower pace of implementation of public works on the growth rate of the construction sector.

In 2017, GDP would continue to show an upward trend, a growth rate of 4.6 percent being forecast.

Showing a negative economic balance for a second consecutive year, the operations of the non-financial public sector registered a deficit of 2.1 percent of GDP in 2015. This negative balance is explained by the decline of the current revenue of the general government, associated with the drop of commodity prices, the slowdown of economic activity, and tax reduction measures. In 2016 the deficit is estimated to be equivalent to 2.6 percent of GDP, after which it would start showing a downward trend and register 2.3 percent of GDP in 2017

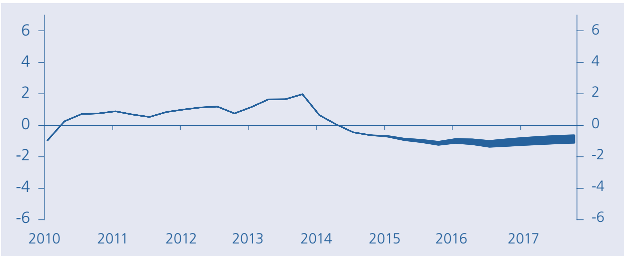
Inflation accumulated in the last twelve months rose from 4.4 percent in December 2015 to 4.5 percent in February 2016. Food supply shocks reversed in part in February and a decline was also observed in fuel prices. Moreover, the annual rate of inflation without food and energy rose to 3.8 percent in February after showing rates of around 3.5 percent for several months due to the effect of higher-than-seasonal rises in education costs.

Since our last Inflation Report was published, the risks of the inflation forecast on the upside have continued to materialize. The effect of an increased depreciation on prices has generated a rise in inflation and in inflation expectations, while supply shocks associated with El Niño have temporarily affected inflation.

In this context, with the aim of favoring the convergence of inflation expectations to the target range and offsetting the second-round effects of inflation in price formation in the economy, the Board of BCRP raised the benchmark interest rate by 25 basis points in both January and February, to 4.25 percent. The Board also reiterated that the BCRP oversees inflation forecasts and inflations determinants and stands ready to make further adjustments in the policy rate, if necessary, to lead inflation and inflation expectations to converge to the target range.

Since March, with the aim of complementing the actions taken to sterilize banks' liquidity surpluses, the BCRP also raised the minimum current account reserve requirement used to calculate reserve requirements in the general regime of reserves in domestic currency by 25 basis point.

OUTPUT GAP: 2010 - 2017
(% potential GDP)



The projected evolution of the output gap is determined by the evolution of external conditions, the monetary policy stance and other financial conditions, the fiscal impulse, and economic agents' confidence in the course of the economy. With the information available to date, a negative output gap indicating no inflationary pressures on the side of the demand is estimated. Moreover, a gradual reduction of the output gap is estimated in the 2016-2017 forecast horizon.

Risk Balance

The balance of risks remains neutral in the inflation forecast, which means that there are no signals indicating an upward or a downward bias of the inflation forecast. The events that could divert the rate of inflation from the baseline scenario would include greater volatility in international financial markets, a slowdown of domestic demand, slower global growth, and the occurrence of supply shocks.

Volatility in international financial markets

This risk could materialize if the withdrawal of monetary stimulus by the U.S. Federal Reserve brought about volatility in international financial markets. In such case, this could generate capital outflows from the emerging markets and depreciation pressures on the currencies of these countries, which could lead to higher inflation.

Slowdown in domestic demand

In this year of elections, economic recovery could take longer than expected if the implementation of both public and private investment projects were postponed, which would generate a more negative output gap and lower inflation in the forecast horizon.

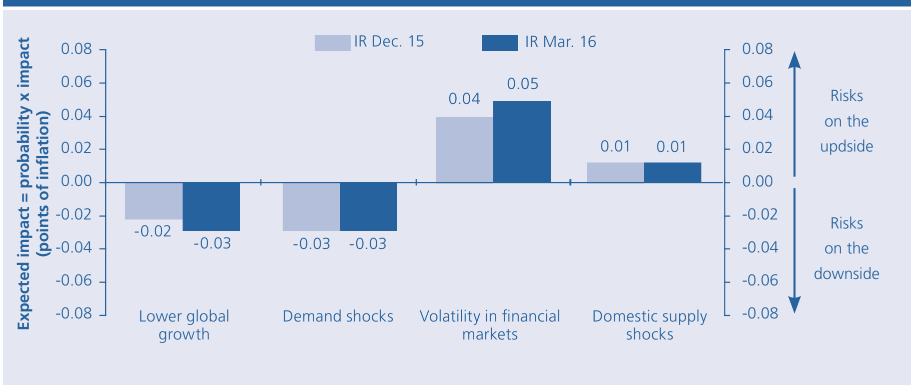
Lower global growth

The baseline scenario considers a slower recovery in the world economy in 2016-2017 than the one estimated in our Inflation Report of December, due mainly to lower growth in the United States and in the emerging economies as well as due to uncertainty about growth in China. However, if such recovery were to take even longer and if the terms of trade deteriorated further, the resulting lower external impulse would translate into a lower output gap and into lower domestic inflation.

Supply shocks

A rise in international oil prices and other imported goods significantly above the levels considered in the baseline scenario could generate inflationary pressures. Similarly, more severe effects of El Niño than those foreseen could push upwards the prices of some food products.

BALANCE OF RISKS AGAINST THE BASE SCENARIO



SUMMARY OF INFLATION REPORT FORECAST

	2014	2015	2016 1/		2017 1/	
			IR Dec. 15	IR Mar. 16	IR Dec. 15	IR Mar.16
Real % change						
1. Gross Domestic Product	2.4	3.3	4.0	4.0	4.8	4.6
2. Domestic demand	2.1	3.0	3.0	2.5	3.8	3.8
a. Private consumption	4.1	3.4	3.5	3.5	3.8	3.8
b. Public consumption	10.1	9.5	5.3	4.0	4.0	3.0
c. Fixed private investment	-2.1	-4.3	0.0	0.0	4.0	4.0
d. Public investment	-2.0	-7.5	10.9	7.4	5.0	5.0
3. Exports (good and services)	-0.8	3.3	5.4	6.4	7.9	6.7
4. Imports (good and services)	-1.5	2.4	1.3	0.7	4.0	3.5
5. Economic growth in main trading partners	2.4	1.8	2.1	1.6	2.5	2.3
Memo:						
Output gap 2/ (%)	-1.0 ; 0.0	-1.5 ; -1.0	-1.5 ; 0.0	-1.5 ; -0.0	-1.0 ; -0.0	-1.0 ; 0.0
% change						
6. Inflation	3.2	4.4	2.5 - 3.0	3.0 - 3.5	2.0 - 2.5	2.0 - 2.2
7. Average price of crude oil	-4.9	-47.7	-6.8	-27.3	7.8	17.8
8. Terms of trade 3/	-5.4	-6.3	-4.0	-2.6	1.7	0.1
a. Export price index	-6.9	-14.9	-6.4	-5.2	3.5	2.3
b. Import price index	-1.5	-9.2	-2.5	-2.7	1.8	2.2
Nominal % change						
9. Currency in circulation	11.2	3.8	8.0	4.6	8.0	5.0
10. Credit to the private sector 4/	10.4	9.6	9.0	8.0	9.0	7.0
% GDP						
11. Gross fixed investment.	25.7	24.3	23.8	23.9	23.9	24.0
12. Current account of the balance of payments	-4.0	-4.4	-3.6	-3.9	-2.6	-3.0
13. Trade balance	-0.7	-1.7	-1.3	-0.9	-0.3	-0.4
14. Gross external financing of the private sector 5/	7.2	5.3	3.9	3.8	4.0	4.3
15. Current revenue of the general government	22.2	20.0	19.8	19.5	19.6	19.5
16. Non-financial expenditure of the general government	21.5	21.3	21.3	20.8	21.0	20.6
17. Overall balance of the non-financial public sector	-0.3	-2.1	-2.9	-2.6	-2.7	-2.3
18. Total public debt balance	20.0	23.3	24.8	24.7	24.2	24.0

1/ Forecast.
2/ Differential between GDP and potential GDP (%).
3/ Average.
4/ Includes loans made by banks' branches abroad.
5/ Includes net direct investment, portfolio investment and private sector's long term disbursement.
IR: Inflation Report.