CENTRAL RESERVE BANK OF PERU

Summary Inflation Report

June 2021

This ***Inflation Report*** has been prepared using data on the balance of payments and the gross domestic product as of the first quarter of 2021, data on the monthly GDP, the trade balance, and monetary accounts as of April 2021, data on the operations of the non-financial public sector and inflation as of May, and data on financial markets and the exchange rate as of June.

Global economic activity has evolved better than expected in recent months, boosting an optimistic growth outlook for the second half of 2021. These positive expectations have been reinforced by the rapid progress of the vaccination process in developed economies, increased fiscal stimulus in the United States, and excess private savings generated during the pandemic. The projection of global growth is therefore revised up from 5.8 to 5.9 percent for 2021 and from 4.0 to 4.2 percent for 2022.

The **terms of trade** increased by 17.3 percent in the first quarter of 2021, driven by the strong increase in copper prices following the progress of the global vaccination process and the recovery of the world economy. Because of this, the growth of terms of trade projected for 2021 in this report (13 percent) is expected to be higher than the rate estimated in the previous Report (6.4 percent). Moreover, the terms of trade would continue to grow in 2022, showing an expansion rate of 2.8 percent (2.2 percent in the previous Report).

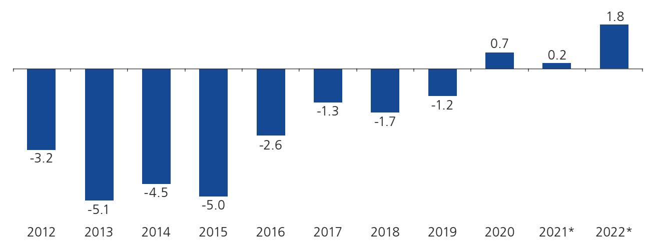
The **current account** of the balance of payments recorded a deficit of US$ 1,674 million in the first quarter of 2021, this deficit being associated with higher imports and a larger deficit in services. The current account projection for 2021 is revised up from zero to a surplus of 0.2 percent of GDP, reflecting the higher increase in the terms of trade and the favorable evolution of non-traditional exports so far this year. In 2022, the current

GLOBAL GDP GROWTH
(Annual % change)

	PPP*	2020	2021		2022	
			IR Mar.21	IR Jun.21	IR Mar.21	IR Jun.21
Developed economies	**42.5**	**-4.7**	**5.2**	**5.4**	**3.3**	**3.9**
Of which						
1. USA	16.0	-3.5	6.5	6.7	3.3	4.2
2. Eurozone	12.0	-6.6	4.7	4.7	3.8	4.3
3. Japan	4.0	-4.8	2.7	3.0	2.2	2.5
4. United Kingdom	2.3	-9.9	4.5	6.0	3.3	4.9
5. Canada	1.4	-5.4	4.9	6.1	3.8	4.1
6. Others	6.8	-4.1	4.6	4.9	3.1	3.2
Developing economies	**57.5**	**-2.2**	**6.2**	**6.2**	**4.5**	**4.5**
Of which						
1. China	18.6	2.3	8.4	8.7	5.7	5.7
2. India	6.7	-8.0	11.0	10.5	6.5	6.5
3. Russia	3.1	-3.1	3.4	3.4	2.7	2.7
4. Latin America and the Caribbean	7.3	-6.9	4.1	4.3	2.7	2.8
Argentina	0.6	-9.9	4.8	5.1	2.2	2.2
Brasil	2.4	-4.1	3.5	3.5	2.1	2.1
Chile	0.4	-5.8	5.0	5.4	3.5	3.5
Colombia	0.6	-6.8	4.9	4.9	3.9	3.7
Mexico	1.9	-8.2	3.9	4.5	3.0	3.3
Peru	0.3	-11.1	10.7	10.7	4.5	4.5
5. Others	17.9	-4.0	4.8	4.9	4.5	4.5
Global GDP Growth	**100.0**	**-3.3**	**5.8**	**5.9**	**4.0**	**4.2**

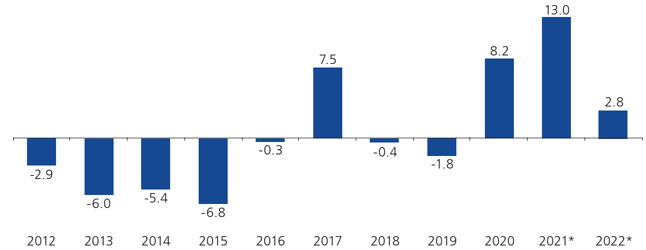
* Base 2020.
Source: IMF and Consensus Forecast.

CURRENT ACCOUNT: 2012-2022
(% GDP)



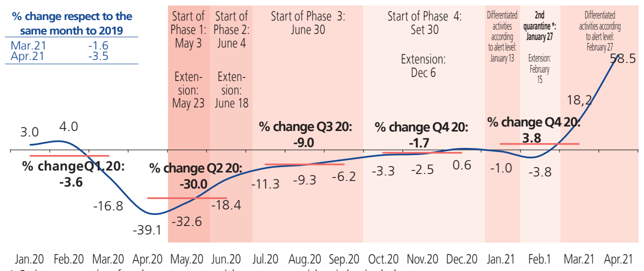
* Forecast.

TERMS OF TRADE: 2012-2022
(Annual average % change)



* Forecast.

REAL GDP
(Annual % change)



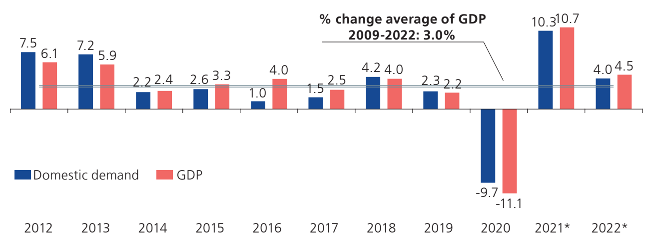
* Strict quarantine for departments with extreme epidemiological alert.
Memo: The beginning of the phases is based on the publication of the corresponding Supreme Decree. Extension refers to the date on which other activities came into operation or the current regime was postponed.

GDP BY PRODUCTION SECTOR
(Real % change)

	2020	2021* S1.21 respect to: 1Q.20	2021* S1.21 respect to: 1Q.19	2021* IR Mar.21	2021* IR Jun.21	2022* IR Mar.21	2022* IR Jun.21
Primary GDP	**-7,9**	**2,7**	**-0,5**	**7,4**	**7,4**	**5,7**	**5,7**
Agriculture and livestock	1,3	0,2	3,9	1,8	2,0	3,0	3,0
Fishing	2,1	38,6	13,6	7,2	7,2	4,7	4,7
Metallic mining	-13,9	3,0	-4,0	11,0	11,4	6,9	6,9
Hydrocarbons	-11,0	-15,8	-15,6	6,5	4,0	9,0	9,0
Based on raw materials	-2,6	14,7	13,8	6,7	6,7	5,1	5,1
Non-Primary GDP	**-12,0**	**4,1**	**0,3**	**11,7**	**11,7**	**4,2**	**4,2**
Non-primary industries	-16,7	15,9	1,9	18,1	18,1	2,0	2,0
Electricity and water	-6,1	2,7	0,8	7,5	7,5	2,3	2,3
Construction	-13,9	41,5	24,5	17,4	17,4	3,8	3,0
Commerce	-16,0	-0,5	-7,6	18,0	18,0	3,3	3,3
Services	-10,3	-0,2	-0,9	8,9	8,9	4,8	4,9
GDP	**-11,1**	**3,8**	**0,1**	**10,7**	**10,7**	**4,5**	**4,5**

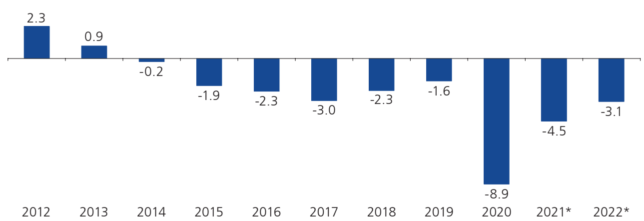
IR: Inflation Report
* Forecast.

DOMESTIC DEMAND AND GDP: 2012-2022
(Real % change)



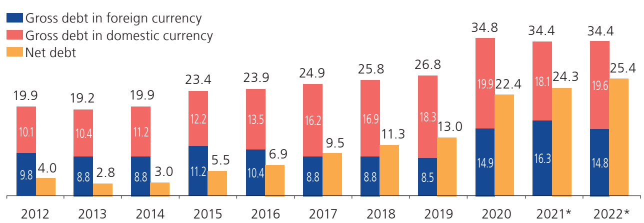
*Forecast.

ECONOMIC BALANCE OF THE NON-FINANCIAL PUBLIC SECTOR: 2012-2022
(% GDP)



* Forecast.

DEBT OF THE NON-FNANCIAL PUBLIC SECTOR: 2012-2022
(% gdp)



account would register a surplus of 1.8 percent of GDP considering a continued positive impact of the terms of trade on the value of exports.

Economic activity registered a year-on-year growth rate of 3.8 percent in the first quarter of 2021, a higher than expected result. However, the pace of recovery moderated with respect to the previous quarter due to the implementation of a targeted quarantine in February. The projection for the 2021-2022 horizon assumes a massive vaccination process in the second half of this year, a context of political and social stability, a favorable environment for business development and the creation of productive employment, the maintenance of monetary and fiscal impulses, the recovery of external demand, and the maintenance of highly favorable terms of trade. The projection also assumes that there will be no new waves of high-impact COVID-19 infections.

Under these conditions, the economy would continue to recover over the projection horizon, with growth of 4.5 percent in 2022, associated with the normalization of spending habits and the recovery of the services sector following the immunization of the population, which would boost employment and domestic demand. As a result, economic activity would return to pre-pandemic levels in the first half of 2022.

The **fiscal deficit**, which decreased from 8.9 to 6.7 percent between February and May 2021, is likely to continue declining in the rest of the year and reach 4.5 percent of GDP in 2021, as a result of the recovery of current revenues associated mainly with higher export prices and the recovery of activity. On the other hand, non-financial expenditure would slow its growth rate due to lower spending because of the COVID-19 health crisis, although it would still be higher than projected in the March report. In 2022, the fiscal deficit would continue to decline and would reach 3.1 percent of GDP.

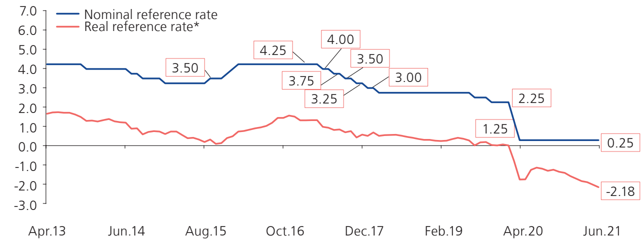
The **gross debt of the non-financial public sector** would represent 34.4 percent of GDP in 2021, maintaining the same level in 2022, while the net debt would increase to 24.3 percent of output in 2021 and reach 25.4 percent in 2022. The projected trajectory of gross debt is opposite to that of the net debt, which would be explained by the use of non-financial public sector deposits.

BCRP has maintained a **benchmark interest rate** of 0.25 percent since April 2020, which in June 2021 is equivalent to a negative real rate of 2.18 percent. Both the nominal and the real rates are at their historical lows. Given the magnitude of the shock associated with the pandemic, the monetary impulse has been amplified through other monetary policy instruments.

The balance of liquidity injection operations in local currency decreased from S/ 64.1 billion at the end of February to S/ 60.4 billion on June 16. Of this balance of liquidity injection operations equivalent to 8.2 percent of GDP as of June 16, 2021, S/ 48.4 billion corresponds to the amount liquidated from repos of the government-guaranteed credit portfolio (Reactiva Peru program). In comparative terms, this total balance resulting from liquidity injection operations is 7.6 times higher than the maximum balance reached during the 2008-2009 international financial crisis (S/ 7.9 billion) and 1.9 times the balance recorded during the 2013-2016 commodity price slump period and the de-dollarization program (S/ 31.8 billion).

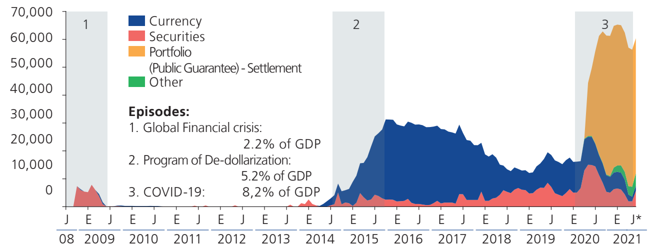
In line with the expansionary monetary stance, **credit to the private sector** had a clearly countercyclical behavior, counterbalancing the negative effects of the pandemic on economic activity and thereby facilitating its recovery. Thus, the year-on-year growth rate of credit accelerated from 6.9 percent in 2019 to 9.3 percent in April 2021, driven mainly by the loans associated with the Reactiva Peru program granted between May and December of last year. Taking into account the significant expansion of credit in 2020 and the beginning of the amortization of the loans granted under the Reactiva program, a more subdued credit growth of 3.0 percent is projected in 2021 and 2022. With this, the ratio of credit to the private sector relative to GDP would register 43 percent at the end of the forecast horizon.

REFERENCE INTEREST RATE
(%)



* With expectation on inflation.

BALANCE OF MONETARY INJECTION OPERATIONS OF BCRP
(Balance in mill. S/)



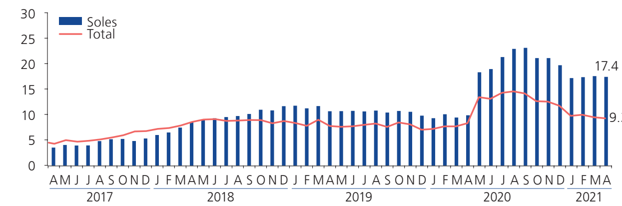
* As of June 16.

CREDIT TO THE PRIVATE SECTOR 1/
(Annual growth rate)

	Dec.19	Mar.20	Jun.20	Sep.20	Dec.20	Mar.21	Apr.21
Businesses	**4.2**	**6.6**	**20.0**	**24.6**	**21.7**	**18.6**	**16.7**
Corporate and large companies	4.4	9.6	21.8	14.2	8.3	3.3	-0.7
Medium-sized enterprises. small and micro business	4.1	3.0	17.8	37.0	37.4	37.6	39.5
Individuals	**11.3**	**9.3**	**2.8**	**-1.3**	**-3.1**	**-4.5**	**-2.6**
Consumers	12.8	10.2	1.6	-4.2	-7.1	-10.6	-8.2
Car loans	11.9	6.9	0.9	-3.1	-2.5	-8.3	-4.4
Rest	12.9	10.3	1.7	-4.2	-7.3	-10.6	-8.3
Mortgage	9.0	8.0	4.6	3.1	3.2	4.8	6.0
TOTAL	**6.9**	**7.6**	**13.2**	**14.3**	**11.8**	**9.5**	**9.3**

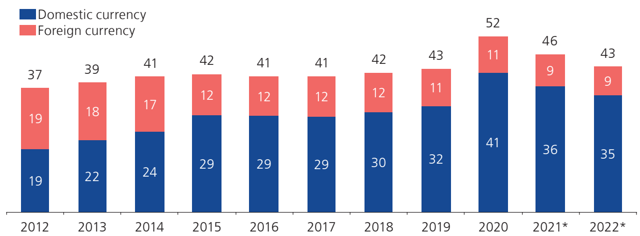
1/ Balances are valuated at constant exchange rate on December 2019.

TOTAL CREDIT TO THE PRIVATE SECTOR AND IN SOLES
(Annual growth rate)



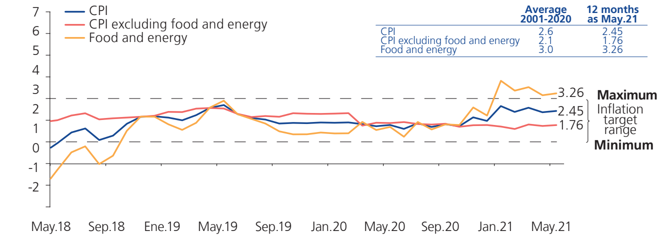
Source: BCRP.

RATIO CREDIT/GDP
(%)

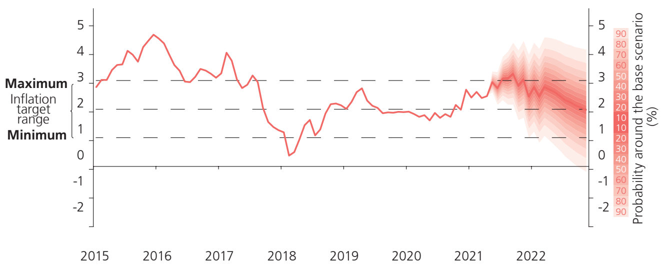


1/ Balances are valuated at constant exchange rate on December 2019.
* Forecast.

INFLATION
(Last 12-month % change)



INFLATION FORECAST: 2021 - 2022
(Last 12-month % change)

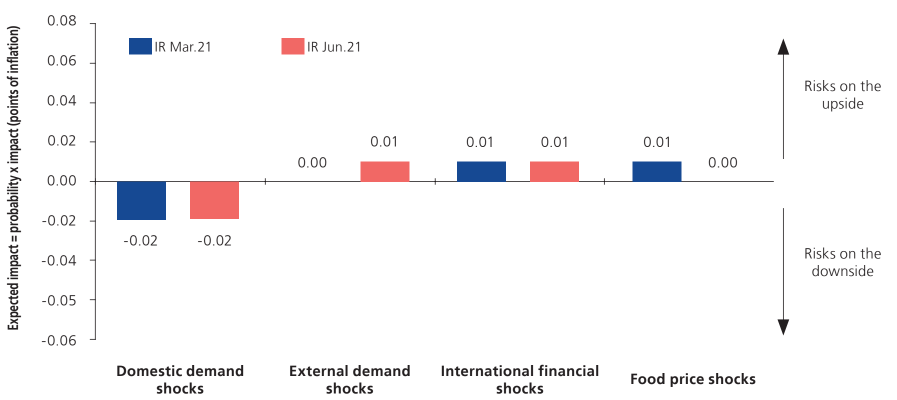


Year-on-year **inflation** increased from 2.40 percent in February to 2.45 percent in May, driven by the depreciation of the PEN, higher fuel prices, and the higher prices of food products with high imported contents. In this context, 12-month inflation expectations rose from 2.11 percent to 2.43 percent in the same period. Trend inflation indicators remain in the lower part of the target range. Inflation in 2021 would register 3.0 percent due to temporary supply effects (increase in fuel prices and some food goods, as well as in the foreign exchange rate) and would then remain within the target range during 2022. This projection considers that inflation expectations will gradually decline towards the middle of the target range (2.0 percent), in a context in which the output gap will gradually close as the aggregate economy continues to recover.

Balance of risks

The balance of **inflation risk factors** in this report is neutral, but the variance of the inflation projection is high. The risks in the projection consider mainly the following contingencies: (i) a slower level of local activity if private spending decelerates due to lower consumer and business confidence or due to a significant new wave of COVID-19 infections, and (ii) upward pressures on the exchange rate due to higher international interest rates associated with higher external inflation or a delay in the normalization of the recent volatility observed in local financial markets. A positive scenario likely to materialize is the progress in the vaccination process in the world and its favorable impact on the economies of Peru's trading partners.

BALANCE OF RISKS AGAINST THE BASE SCENARIO



SUMMARY OF INFLATION REPORT FORECAST

	2019	2020	2021[1/]		2022[1/]	
			IR Mar.21	IR Jun.21	IR Mar.21	IR Jun.21
Real % change						
1. Gross Domestic Product	2.2	-11.1	10.7	10.7	4.5	4.5
2. Domestic demand	2.3	-9.7	9.6	10.3	4.6	4.0
a. Private consumption	3.0	-8.7	8.5	8.5	4.8	4.8
b. Public consumption	2.2	7.4	3.5	7.0	3.0	1.0
c. Fixed private investment	4.5	-16.6	15.5	15.5	4.5	2.5
d. Public investment	-1.5	-15.5	15.0	19.0	4.5	4.5
3. Exports (good and services)	0.7	-20.1	13.9	13.5	6.5	6.4
4. Imports (good and services)	1.2	-15.7	9.2	11.8	7.3	4.4
5. Global economic growth	2.8	-3.3	5.8	5.9	4.0	4.2
Memo:						
Output gap 2/ (%)	-0.6	-13.6	-11.0;-2.0	-11.0;-2.0	-9.0;0.0	-9.0;0.0
% change						
6. Inflation	1.9	2.0	2.0	3.0	1.6	2.0
7. Expected inflation [3/]	2.3	1.5	2.1	2.5	2.2	2.3
8. Expected depreciation [3/]	-0.3	7.4	-2.1	-0.2	-1.4	0.3
9. Terms of trade	-1.8	8.2	6.4	13.0	2.2	2.8
a. Export prices	-3.4	2.7	17.8	26.3	0.5	1.0
b. Import prices	-1.7	-5.1	10.7	11.8	-1.7	-1.7
Nominal % change						
10. Currency in circulation	4.7	37.3	10.0	10.0	3.0	3.0
11. Credit to the private sector	6.9	11.8	3.0	3.0	3.0	3.0
% GDP						
12. Gross fixed investment	22.7	21.1	21.8	21.8	21.7	21.2
13. Current account of the balance of payments	-1.2	0.7	0.0	0.2	0.1	1.8
14. Trade balance	2.9	3.8	6.4	7.4	6.3	8.0
15. Long-term external financing of the private sector [4/]	1.9	-0.7	-1.3	0.7	-0.4	-1.4
16. Current revenue of the general government	19.7	17.9	19.0	19.3	19.9	20.1
17. Non-financial expenditure of the general government	20.0	24.8	21.8	22.3	21.1	21.7
18. Overall balance of the non-financial public sector	-1.6	-8.9	-4.4	-4.5	-2.8	-3.1
19. Balance of total public debt	26.8	34.8	34.4	34.4	34.3	34.4
20. Balance of net public debt	13.0	22.4	24.1	24.3	25.3	25.4

IR: Inflation Report.
1/ Forecast.
2/ Differential between GDP and trend GDP (in % of trend GDP).
3/ Survey on expectations to the analysts and financial entities carried out at the time of publication of the respective Inflation Report. Data observed in the case of depreciation for 2019 and 2020, and the average of expectations throughout year in case of inflation have been considered.
4/ Includes net direct investment, portfolio investment and private sector's long term disbursement.