CENTRAL RESERVE BANK OF PERU

Board of Directors

Germán Suárez Chávez
Chairman of the Board

Mario Tovar Velarde
Vice-Chairman

Alberto Benavides de la Quintana
Gianfranco Castagnola Zúñiga
Guillermo Castañeda Mungi
Alfredo Jalilie Awapara
Directors

CENTRAL RESERVE BANK OF PERU

Senior Officers

Javier de la Rocha Marie
General Manager

Marylin Choy Chong
Central Manager of Technical Affairs

Juan Ramírez Andueza
Manager of Credits and Financial Regulation

Luis Martínez Green
Deputy Manager of Credits

Mario Mesía Lizaraso
Deputy Manager of Financial Regulation and Evaluation

Carlos Ballón Avalos
Manager of International Operations

Jorge Patrón Worm
Deputy Manager of Foreign International Investments

Teresa San Bartolomé Gelicich
Deputy Manager of Foreign Currency Operations

Pacífico Huamán Soto
Manager of Treasury

Augusto Otero Castro
Deputy Manager of Custody

José Arturo Pastor Porras
Deputy Manager of Analysis And Programming of Bills and Coins

Arturo Handabaka García
Deputy Manager of the National Mint

Margarita Imano Konno
Administration Manager

Roberto Eslava Robles
Deputy Manager of Personnel

Saúl Paredes Zúñiga
Deputy Manager of Administrative Services

Jorge Bravo Benites
Legal Affairs

Armando Arteaga Quiñe
Central Manager of Administrative Affairs

Renzo Rossini Miñán
Manager of Economic Studies

Adrián Armas Rivas
Deputy Manager of the Monetary Sector

Gladys Choy Chong
Deputy Manager of the External Sector

Jorge Estrella Viladegut
Deputy Manager of the Public Sector

Teresa Lamas Pérez
Deputy Manager of the Real Sector

Susana Ishisaka Frukawa
Deputy Manager of Research and Global Analysis

Emilio Pallete Celi
Manager of Accounting and Supervision

Carmen Aguilar Mondoñedo
Deputy Manager of Accounting

Luis Valdivia Acevedo
Deputy Manager of Supervision

Luis Mosso Gonzáles
Systems Manager

Ricardo Chávez Caballero
Deputy Manager of Systems Development

Rolando Pacheco Campusano
Deputy Manager of Operations and Users' Support

Juan Carlos Pacheco Pacheco
Deputy Manager of Technical Services

José Ponce Vigil
Internal Auditor

Alberto Aquino Velaochaga
Supervisor

Romano Batagelj Cobolli
Systems Auditor

Pedro Arnillas Gamio
Consultant Attorney

Humberto Peirano Portocarrero
General Secretary

José Rocca Espinoza
Institutional Relations Office

Branch Heads

Arequipa
José Monzón García

Cusco
Javier Curo García

Huancayo
Jaime Esquivel Rodríguez

Iquitos
Raúl Castro Alegría

Piura
Carlos Alatrista Gironzini

Puno
Flavio Miraval Bedoya

Trujillo
Nelson Ruiz Cerdán (e)

INTRODUCTION

In 1999 the Peruvian economy began to show signs of recovery, after the adverse effects on the economy of the “El Niño” Phenomenon, the international financial crisis and the fall in the terms of trade in 1998. The economy's rebound is explained by sound macroeconomic fundamentals, such as inflation control and the reduction of the external deficit; the maintenance of a level of net international reserves that exceeds the amount of external liabilities with maturities shorter than one year; a floating exchange rate regime that relieves pressure on the balance of payments through fluctuations in the real exchange rate; the enforcement of prudential regulation aimed at strengthening the banking system; and a strict public sector management intended to ensure the attainment of fiscal equilibrium in the medium run. Such policies, combined with structural reforms, typically result in enhanced productivity and improved expectations about the economy's future.

The economic performance was not homogeneous, because the sectors that had been severely hit by the “El Niño” Phenomenon in 1998 -fishing, the primary-resource industry and agriculture- grew significantly in 1999. It should be noted that the growth of the mining sector reflected the continuous and significant investment process that has taken place recent. Gross Domestic Product (GDP) increased by 1,4 percent, driven by the 14,0 percent growth of the primary sectors. In contrast, the non-primary sectors fell by 0,9 percent, reflecting a 2,6 percent reduction in domestic demand. Like in other deceleration episodes, in 1999 private investment reacted more unfavorably than other components of domestic demand, falling by 16,3 percent. However, the recovery that started in the fourth quarter of the year resulted in a growth rate of almost 4,0 percent for GDP and domestic demand.

The monetary policy developed by the Central Bank drove accumulated inflation to 3,7 percent, the lowest rate in the last 40 years. This result was attained thanks to strict control of the monetary base, which grew by 6,7 percent on average, compared with 12,5 percent in the previous year.

However, end-of-year growth of the monetary base was greater than in 1998 (17,0 versus 5,5 percent), which is explained by the increased demand for currency in circulation associated with the Y2K effect. It should be stressed that during the year, financial institutions and the Central Bank developed contingency plans and conducted rehearsal tests to face possible computing system failures.

During 1999, many non-financial firms had problems in fulfilling their bank obligations, which resulted in a rise in non-performing loans. Because of this, the banks' credit policy continued to be cautious, since the fourth quarter of 1998, with a preference for low-risk clients. It should be noted that credit decreased in 1998 due to the fall of the banks' short-term foreign liabilities. Consequently, policy measures in 1999 were different from those applied in 1998, when the system faced a lack of liquidity denominated in foreign currency. Programs applied by the government in 1999 to support the banking system have been aimed at improving financial institutions' management indicators and asset quality, and to facilitate the debt-restructuring processes of firms. As a result, in 1999 the banking system went through a consolidation process, which included the merging of eight firms in four, the entrance of a new company, the conversion of a bank into a financial company, the absorption of two financial companies by two banks and the liquidation of one bank.

The foreign sector position was strengthened during 1999. This was reflected in the reduction of the current account deficit from 6,4 percent of GDP in 1998 to 3,5 percent in 1999, due to the reduction of the trade deficit from US $2 466 million in 1998 to US$ 616 million in 1999. The 6,2 percent growth of exports was associated with the 14,0 percent increase in the volume of traditional exports, especially from the fishing and mining sectors. On the other hand, imports diminished by 18,2 percent as a result of the reduction of domestic demand. The current account deficit was funded by a significant long-term private capital inflow, while short-term capitals diminished. This behavior largely explains the US$ 780 million decrease in net international reserves in 1999. However, at the end of the year the stock of net international reserves reached US$ 8 404 million, equivalent to 15 months of imports, 5 times the monetary base, 64 percent of the total liquidity of the banking system and 1,2 times the maturity of public and private debt in the following year.

The contraction of domestic demand was reflected in a smaller tax collection which, together with the wage increase in favor of public sector employees and pensioners in April, contributed to an increase in the fiscal deficit from 0,8 percent of GDP in 1998 to 3,0 percent in 1999. This result was associated with the deterioration of the primary balance, which shifted from 1,2 percent of GDP surplus in 1998 to an 0,8 percent deficit in 1999. This mainly reflected the central government deficit, which grew by 1,8 percentage points due to the smaller tax collection and the greater non-financial expenditure, associated with the wage increase, above mentioned.

With the purpose of institutionalizing sound long-term fiscal management, the Fiscal Responsibility and Transparency Law was approved in December 1999. The Law intends to contribute to economic stability and sustained growth through a fiscal framework that limits the fiscal deficit and the growth of public expenditure, and mantains a degree of flexibility for economic slowdowns.

In summary, in 1999 the Peruvian economy started to recover from the severe exogenous shocks that affected production and the revenues of firms and households in 1998. The recovery was not homogeneous, but since the fourth quarter of the year there was a greater dynamism in the activities dependent on the domestic market. The experience of the last two years has shown the importance of sound macroeconomic fundamentals and structural reform in reversing negative expectations about economic performance.