INTRODUCTION

After showing a strong recovery in 2021, the global economy slowed its rate of growth in 2022. Despite the improved epidemiological outlook observed in most countries, the pace of activity was slowed by geopolitical conflicts such as the outbreak of war between Ukraine and Russia, the emergence of new supply shocks and rising inflation. As a result, **global economic activity** grew by 3.4 percent, recording a lower rate than that observed in 2021 (6.2 percent). Even taking this slowdown into account, in 2022 the GDP growth rate of several countries was in line with their long-term growth rate and, in many cases, activity was close to or above its potential level. This reflected demand pressures that, together with supply shocks, had an impact on inflation and led central banks to begin or continue to withdraw monetary stimulus.

Some factors that constrained production in 2021 lessened their impact on global activity by mid-2022. For example, international freight rates reversed their upward trend and international food prices began to fall, influenced by higher expectations for future production and a moderation in fertilizer price increases, although they did not completely reversed compared to the previous year or the pre-pandemic situation. In this scenario of persistent supply shocks and geopolitical conflicts, the **terms of trade** –the ratio between the average price of our exports and our imports– fell by 10.5 percent, partially reversing the increase recorded in the previous two years (9.1 percent in 2020 and 12.0 percent in 2021), mainly due to the increase in the price of industrial inputs, hydrocarbons and food imports.

The contraction in the terms of trade –the largest annual decline since 2008–, together with higher freight costs, led the **current account deficit of the balance of payments** to widen from -2.2 percent of GDP in 2021 to -4.0 percent in 2022. The above factors affected the trade balance and increased the services balance deficit, respectively. This was offset by lower profit payments to companies with foreign direct investment (FDI) in the country. The deficit was partly financed by an increase of 3.8 percent of GDP in the net debit position of the financial account, mainly through the reinvestment of profits of companies with FDI in the country and private loan disbursements. The negative difference between financing requirements and net inflows resulted in a reduction of US$ 6,612 million in n**et international reserves**, which registered a cumulative balance of US$ 71,883 million at the end of 2022, an amount equivalent to 29.4 percent of GDP.

Activity in the **Peruvian economy** recovered by 2.7 percent in 2022, exceeding pre-pandemic levels and allowing for continued positive progress in employment. Private consumption was the main driver of growth due to the dynamism of the labor market, which allowed for higher employment and incomes and was reflected in the progress of non-primary sectors such as trade and services. Public investment –especially by regional and local governments– and exports also contributed to the year's growth. However, two factors limited this pace of GDP growth: on the one hand, private investment contracted, affected by the deterioration of business confidence in the economy. On the other hand, the growth of private consumption slowed down as a result of the impact of inflation on household spending and lower consumer confidence.

The positive impact of the recovery in economic activity on tax revenues and lower pandemic-related expenditures led the **budget deficit** to decline from 2.5 percent of GDP in 2021 to 1.7 percent in 2022. **The gross debt of the non-financial public sector** increased from S/ 314.9 billion in 2021 to S/ 317.4 billion at the end of 2022: the nominal increase is due to higher domestic debt following the placement of government bonds. As a percentage of GDP, the debt fell from 35.9 to 33.8 percent due to high nominal GDP growth.

A confluence of domestic and external factors caused **inflation** to continue the upward trend observed since mid-2011, remaining above the target range of 1-3 percent. External factors included higher food, fuel, and fertilizer prices, while domestic factors included climate disruptions and higher inflation expectations due to the magnitude and persistence of supply shocks on inflation. These factors pushed up the year-on-year inflation rate to a peak of 8.81 percent in June 2022, after which it gradually declined to 8.46 percent in December.

In response to rising inflation and inflation expectations, the BCRP continued the withdrawal of the monetary stimulus initiated in 2021, raising the **policy rate** by 500 basis points throughout 2022 to a level of 7.50 percent. The real interest rate, i.e. the rate that subtracts inflation expectations from the nominal interest rate, stood at 2.82 percent in December 2022. This put the monetary policy stance in contractionary territory, above the neutral level of the real interest rate, which is estimated at 1.50 percent. The decisions taken by the BCRP were aimed at ensuring that inflation expectations return to the target range, thus avoiding a delayed reaction that could have triggered even higher inflation, increasing the potential impact on economic activity.

The **balance of liquidity injection operations** in domestic currency decreased from S/ 56.7 billion at the end of 2021 to S/ 39.3 billion at December 31, 2022, mainly due to the amortization of government-backed repos of the credit portfolio guaranteed by the Reactiva Perú program (S/ 20.1 billion). For its part, the growth rate of total credit to the private sector increased from 4.0 percent per year in 2021 to 4.6 percent per year in 2022. As a percentage of GDP, the balance of credit to the private sector represented 44.3 percent, lower than the previous year (45.8 percent), although above the pre-pandemic level (42.8 percent).