INTRODUCTION

After recording a growth rate of 5.8 percent in 2013, the Peruvian economy grew 2.4 percent in 2014. This decline in the pace of growth is explained by temporary shocks –which affected output in the primary sectors mainly– and added to a deterioration in the terms of trade for a third consecutive year and to the contraction of public investment.

The rate of inflation increased from 2.9 percent in 2013 to 3.2 percent in 2014, due mainly to rises in food prices and electricity rates (4.1 percent in the year). Inflation without food and energy prices –food and energy being items with high price volatility– fell from 3.0 percent in 2013 to 2.5 percent in 2014.

The global economy showed a growth rate of 3.3 percent –a slightly lower rate than in 2013–, reflecting the slowdown observed in most emerging market countries, on the one hand, and some economic recovery in the developed countries, associated with the recovery of consumption and employment, especially in the United States, on the other hand. Growth in the emerging market economies was affected by factors such as China's economic slowdown, the withdrawal of the US Federal Reserve asset purchase program, the drop of oil prices, and geopolitical events, which generated volatility in international financial markets, a drop in commodity prices, and depreciation pressures on the currencies of most of the emerging market countries.

In this context of adverse domestic and external factors, the actions of Banco Central de Reserva del Perú (BCRP) were aimed at maintaining inflation within the inflation target range. Thus, the BCRP reduced its monetary policy rate from 4.0 to 3.5 percent (lowering it by 25 basis points in both July and September), and continued reducing the rate of reserve requirements in domestic currency to support the credit cycle and encourage the dedollarization of credit. In addition to this, the BCRP also introduced a series of measures to tighten reserve requirements conditions according to the evolution of credit in dollars.

With these measures, the BCRP changed the previous scheme of reserve requirements –based on limits to the expansion of credit– for another scheme in which the rate of reserve requirements is set according to the evolution of credit in foreign currency. According to the new scheme, the financial entities that by June 2015 have not reduced their total balance of credit in dollars by at least 5 percent relative to the balance of credit in dollars they had in September 2013 –excluding loans for foreign trade operations– will be subject to additional reserve requirements. This requirement will increase to 10 percent in December 2015. Moreover, financial entities that fail to reduce their total balance of car loans and mortgage loans in dollars by at least 10 percent relative to their balance of these loans in dollars in February 2013 will also be subject to additional reserve requirements. This reduction requirement will increase to 15 percent in December 2015.

The evolution of the nuevo sol was influenced by signs of economic recovery in the United States and expectations regarding the beginning of the Federal Reserve cycle of interest rate hikes, which strengthened the dollar in international financial markets. In this context, marked also by political uncertainty in Greece, the sudden fall of oil prices and some geopolitical factors, the nuevo sol depreciated 6.4 percent against the dollar in nominal terms (this was mostly observed between August and December).

Influenced mainly by China's economic slowdown, the terms of trade continued to deteriorate during the year with a fall of 5.4 percent on average in 2014 and an accumulated decline of 13.2 percent since 2012. The 6.9 percent drop in export prices, explained mainly by the lower prices of copper and gold, was in part offset by a decline of 1.5 percent in the price of imports (the sharp decline in oil prices standing out in the last quarter).

Despite this deterioration in the terms of trade, the deficit in the current account of the balance of payments declined as a percentage of gross domestic product (GDP) from 4.2 percent in 2013 to 4.0 percent in 2014. This decline is explained by the fall in the volume of imports –resulting from slower growth and from the depreciation of the currency in real terms– and by increased external current transfers for extraordinary revenues (non-residents' income tax payments). Moreover, the financial account of the balance of payments showed a positive balance equivalent to 3.4 percent of GDP associated mainly with long-term private sector operations: foreign direct investment (FDI), placements of bonds in foreign markets, and long-term loans. The current account of the balance of payments continued to be financed by these operations, which amounted to 5.4 percent of GDP.

Reflecting to a great extent the increase in current spending observed in the year, the operations of the non-financial public sector recorded in 2014 a deficit of 0.3 percent of GDP after having recorded a surplus of 0.9 percent of GDP in 2013. On the other hand, in contrast, capital spending decreased due mainly to lower actual capital spending at the level of regional governments. As for tax revenues, the decrease observed in these revenues due to the economic slowdown registered in the period was offset by extraordinary revenues (non-residents' income tax on the sale of assets).