

Peru

1. General trends

The Peruvian economy grew by 8.8% in 2010, driven by robust domestic consumer and investor demand and by a process of inventory restocking. This performance was observed at a time when inflation was low and the fiscal deficit and balance-of-payments current account deficit had narrowed.

Fuelled by the upturn in the global economy and improved access to various markets following the signing of several free trade agreements, more vibrant export growth will combine with strong domestic demand to bring GDP growth to around 7.1% in 2011. The expansion

of investment is expected to be led by projects in the mining and hydrocarbon sector, road, port and airport infrastructure works and energy infrastructure projects (hydroelectric plants, power generation and transmission lines, and wind farms).

2. Economic policy

(a) Fiscal policy

Vigorous economic growth in the first few months of 2010 prompted the authorities to start reverting the fiscal and monetary stimulus measures. In May, the government passed an emergency decree announcing measures for reining in fiscal spending. These included a cap on growth in fiscal spending in 2010, set at 3% of the nominal value of expenditure executed in 2009, a curb on the execution of public investment projects and limitations on the use of contingency reserve funds.

Nevertheless, fiscal spending continued to rise. In 2010, total central government expenditure increased by 11.1% in comparison with 2009 (non-financial expenditure was up by 12.1% and expenditure with interest, down by 2.1%). Non-financial expenditure reflected the increase in capital expenditure intended mainly for road infrastructure projects. Current expenditure rose by 6.5% (payroll expenses by 4.4% and expenditure on

procurement of goods and services by 16.5%). Current income grew by 22.8% in 2010. Tax revenues were up by 22.6%, following a 20.4% increase in general sales tax (GST) receipts—due to higher GST collections from imports—and a 26.8% rise in income tax receipts (mainly from corporate entities); non-tax revenue was up by 24.4%. In this context, the central government economic out-turn was a deficit equivalent to 0.4% of GDP and a primary surplus of 0.8% of GDP (compared with deficits equivalent to 1.9% and 0.6% of GDP, respectively, in 2009). The deficit was financed mainly through external disbursements and domestic borrowing.

With the economy continuing to perform strongly, the authorities announced their decision to reduce the public expenditure budget for 2011 and to credit US\$ 2 billion to the Fiscal Stabilization Fund out of the 2010 surpluses and the funds eliminated under the Fiscal Equilibrium Act 2011, which sought to streamline operations. Thus, the increase in public spending has been appreciably more moderate

since the start of 2011. The more restrained expenditure would seem to be concentrated in current expenditure, since for 2011 public investment as a percentage of GDP is expected to remain at much the same level as in 2010 (around 6%).

Available cumulative data for the first four months of the year indicate that central government non-financial expenditure decreased by 0.6% compared with the same period in 2010. The decline in expenditure is attributable to the sharper fall in capital expenditure (down 20%) and the sluggish growth in current expenditure. Current income recorded a 17.7% rise during the same period. In the first five months of 2011, some 31% of the budgeted resources had been committed, reflecting mainly the execution of expenditure at the national and regional government levels.

In 2010 and 2011, various tax rates were adjusted. In 2010, the reduction (from 0.06% to 0.05%) in the tax on financial transactions became effective and in the second half of the year, the customs duty drawback rate was cut (from 8% to 6.5%). In 2011, the tax on financial transactions was further reduced from 0.05% to 0.005% and the GST rate, from 19% to 18%. Both changes took effect on 1 March. In addition, tariffs were lowered for 3,401 items, bringing the average tariff in the first quarter of 2011 to 3.4% (down from 5% in December 2010). According to the Central Bank of the Republic of Peru, these measures will cost the government the equivalent of 1% of GDP.

Under the Fiscal Accountability and Transparency Act, the deficit for 2011 and 2012 must not exceed 1% of GDP and the increase in central government consumption expenditure, measured in real terms, must not exceed 4%. Moreover, since 2011 is an election year, the non-financial expenditure that can be executed during the first seven months of the year is limited to 60% of the annual total, while the deficit for the first half of the year must not exceed 50% of the deficit projected for the entire year. The Public Budget Financial Equilibrium Act 2011 introduced a new fiscal regulation for 2011, which states that a surplus equal to 2% of annual GDP must be generated during the first quarter.

Throughout 2010, the authorities carried out public debt administration operations designed to reduce the total and to improve its debt maturity profile and amortization schedule. In February, the government issued 32-year sovereign bonds totalling 550 million nuevos soles with an interest rate of 6.85%. In April, it carried out partial buyback or conversion operations on global 2012, 2015 and 2016 dollar bonds as well as 2014 global euro bonds, for an amount of US\$ 1.8 billion. In August, 2011, 2012, 2016 and 2017 sovereign bonds totalling US\$ 1.494 billion were swapped on the domestic market for global sovereign

bonds with maturity in 2020. Lastly, in November, 2050 global bonds totalling US\$ 1 billion were issued with a maturity date of 2050, at a rate of 5.625% interest; the 2020 sovereign bond was reopened for an amount of 4.196 billion nuevos soles. In 2011, the authorities announced that financing requirements would be met through bond issues on the domestic market.

Gross public debt, consisting mainly of medium- and long-term debt, fell from 27.2% in 2009 to 23.9% in 2010 (12.9% of external debt and 10.9% of internal debt).

(b) Monetary policy

In view of the country's robust economic performance, in May 2010, the Central Reserve Bank of Peru started to raise its benchmark rate as a precautionary measure. Thus, the rate increased from 1.25% to 3% in August, and remained stable at that level up to December 2010. In January, the Bank resumed the process with gradual monthly rises that brought the benchmark rate to 4.25% in May 2011.

In annualized terms, the average local currency corporate lending rate increased from 5.6% in August 2010 to 6.9% in May 2011¹ (while the foreign currency rate rose from 5.2% to 5.3%), and the 30-day deposit rates went up from 2.2% to 4.0% (at the same time, rates for foreign currency loans fell from 2.4% to 0.5%).

Throughout 2010 and the first part of 2011, the central bank continued to implement administrative measures in order to regulate the massive financial inflows into the Peruvian economy. In order to encourage financial entities to maintain a higher proportion of long-term instruments in their external credit mix, marginal reserve requirements were applied in 2010 to new or renewed external loans with repayment periods of under two years, and the balance of derivative operations by non-residents was taxed. Other measures were the increase in the minimum reserve requirement in local currency (from 6% in March 2010 to 9% in March 2011) and the rise in the marginal reserve requirement for deposits (from 12% in August 2010 to 25% in March 2011).

In the first quarter of 2011, the average legal reserve requirement in local currency and in foreign currency was raised by 0.25% in February and again by the same percentage in March. The reserve requirement was increased to incorporate the liabilities of foreign branches of the banks operating on the local market. Short-term external debt was reduced from 75% to 60% in line with the new regulation adopted by the Office of the Superintendent of Banks (SBV), which limits the net position of bank

¹ On the basis of the new computation methodology established by the Office of the Superintendent of Banks, Insurance Companies and Pension Fund Managers.

derivatives to 40% of equity or 400 million nuevos soles, whichever is greater. The legal reserve requirement for non-residents was maintained at 120%. The dollarization ratio of the financial system remained stable at 49%.

In December 2010, bank lending to the private sector increased by 14.1% compared with the December 2009 figure, and the 12-month rate of expansion to March 2011 was 15.9%. The acceleration in the loan rate is due mainly to the stronger growth in foreign currency loans (12.5% in the 12 months to December 2010 and 17.2% in the 12 months to March 2011). The rate of increase of local currency loans dipped slightly (from 18.6% in the 12 months to December 2010 to 17.6% in the 12 months to March 2011).

(c) Exchange-rate policy

The central bank intervened in the foreign exchange market throughout 2010 in a bid to tame the volatile exchange rate. In January and March 2010, the bank made dollar purchases worth a total of US\$ 2.34 billion, going on to purchase a further US\$ 5.082 billion between June and September. Between December 2010 and May 2011, it carried out sterilized interventions in the foreign

exchange markets by issuing redeemable certificates of deposits in dollars and making direct purchases on the interbank foreign exchange market.

Between December 2009 and December 2010, the nuevo sol appreciated by 2.2% in nominal terms against the dollar (6.2% in annual average terms), while the real effective multilateral exchange rate declined by 2.1% (down 4.1% in annual average terms). Between December 2010 and March 2011, the local currency maintained its upward trend, before sustaining a slight reversal in April.

(d) Trade policy

The free trade agreement between China and Peru entered into force on 1 March 2010 and, in July, Peru signed a free trade agreement with the European Free Trade Association (EFTA). In March 2011, a free trade agreement was signed with the Republic of Korea and in April the European Union signed a free trade agreement with Peru and Colombia, which will enter into force in 2012. Also in April, Mexico and Peru concluded their negotiations for a trade integration agreement. Negotiations for a free trade agreement between Japan and Peru are still under way.

3. The main variables

(a) Economic activity

In 2010, GDP grew by 8.8% in relation to 2009, driven by the expansion of the non-primary sectors, in particular non-primary manufacturing (16.9%), construction (17.4%) and commerce (9.7%). The activity of the primary sectors increased by 1.1%, thanks to the buoyancy of the hydrocarbon sector. Domestic demand expanded by 12.8% in the same period.

On the demand side, gross domestic investment grew by 34.8%, boosted by the increase in gross fixed investment (23%), both public (26.5%) and private (22.1%), and by the process of restocking. Total consumption grew by 6.5%, with government consumption up sharply (10.6%) and private consumption also higher (6%). The substantial growth in domestic demand was reflected in

a 23.8% surge (in constant prices) in imports of goods and services. By contrast, export volumes of goods and services grew by just 2.5%.

Economic activity remained buoyant in the first quarter of 2011. GDP was up by 8.8% compared with the same period in 2010. This is attributable to the strong performance of the fisheries sector (16.2%) and to growth in manufacturing (12%), construction (8.1%), commerce (10%) and other services (9.4%). Gross domestic investment expanded by 25.2% during the same period owing to the significant increase in restocking, since gross fixed private investment increased by 15.4% and gross fixed public investment declined by 6.3%, the first year-on-year decrease since 2004. The surge in domestic demand (10.7%) was reflected in the increase in imports (13.5%). Exports of goods and services fell by 3.4%.

Table 1
PERU: MAIN ECONOMIC INDICATORS

	2002	2003	2004	2005	2006	2007	2008	2009	2010 ^a
Annual growth rates^b									
Gross domestic product	5.0	4.0	5.0	6.8	7.7	8.9	9.8	0.9	8.8
Per capita gross domestic product	3.6	2.6	3.6	5.5	6.4	7.6	8.5	-0.3	7.5
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	6.1	2.3	0.1	5.3	8.0	3.5	7.2	1.7	3.2
Mining	12.0	5.5	5.3	8.4	1.4	2.7	7.6	0.6	-0.1
Manufacturing	5.7	3.6	7.4	7.5	7.5	11.1	9.1	-7.2	13.6
Electricity, gas and water	5.5	3.7	4.5	5.6	6.9	8.5	7.8	1.2	7.7
Construction	7.7	4.5	4.7	8.4	14.8	16.6	16.5	6.1	17.4
Wholesale and retail commerce, restaurants and hotels	3.2	2.9	5.9	6.0	10.3	9.5	12.4	0.2	9.1
Transport, storage and communications	3.7	4.9	6.4	8.5	9.2	18.9	10.0	0.4	6.7
Financial institutions, insurance, real estate and business services	4.9	4.1	3.9	6.5	7.5	9.4	10.2	4.6	8.0
Community, social and personal services	3.7	5.0	3.8	5.3	5.8	4.5	5.1	7.1	7.0
Gross domestic product, by type of expenditure									
Consumption	4.4	3.4	3.7	5.1	6.6	7.9	8.0	3.9	6.5
General government	-0.0	3.9	4.1	9.1	7.6	4.3	2.1	16.5	7.9
Private	4.9	3.4	3.6	4.6	6.4	8.3	8.7	2.4	6.3
Gross capital formation	3.0	4.7	4.5	8.9	26.5	26.3	29.5	-18.1	35.5
Exports (goods and services)	7.5	6.2	15.2	15.2	0.8	6.1	9.9	-3.9	5.4
Imports (goods and services)	2.3	4.2	9.6	10.9	13.1	21.3	26.2	-16.2	28.0
Percentages of GDP									
Investment and saving^c									
Gross capital formation	18.4	18.4	18.0	17.9	20.0	22.9	27.2	22.5	26.4
National saving	16.4	16.9	18.0	19.3	23.2	24.3	23.1	22.6	24.9
External saving	2.0	1.5	-0.0	-1.4	-3.1	-1.4	4.1	-0.2	1.5
Millions of dollars									
Balance of payments									
Current account balance	-1 110	-949	19	1 148	2 872	1 460	-5 318	211	-2 315
Goods balance	321	886	3 004	5 286	8 986	8 503	2 569	5 951	6 750
Exports, f.o.b.	7 714	9 091	12 809	17 368	23 830	28 094	31 018	26 962	35 565
Imports, f.o.b.	7 393	8 205	9 805	12 082	14 844	19 591	28 449	21 011	28 815
Services trade balance	-994	-900	-732	-834	-737	-1 192	-2 056	-1 144	-2 037
Income balance	-1 457	-2 144	-3 686	-5 076	-7 562	-8 359	-8 774	-7 484	-10 053
Net current transfers	1 019	1 209	1 433	1 772	2 185	2 508	2 943	2 887	3 026
Capital and financial balance ^d	2 120	1 510	2 436	264	349	8 864	8 773	1 696	13 271
Net foreign direct investment	2 156	1 275	1 599	2 579	3 467	5 425	6 188	5 178	7 113
Other capital movements	-36	235	837	-2 315	-3 118	3 438	2 586	-3 482	6 157
Overall balance	1 010	561	2 456	1 411	3 221	10 324	3 456	1 907	10 956
Variation in reserve assets ^e	-851	-515	-2 442	-1 472	-3 209	-10 391	-3 512	-1 943	-10 975
Other financing	-158	-46	-13	60	-12	67	57	36	19
Other external-sector indicators									
Real effective exchange rate (index: 2000=100) ^f	95.9	99.9	100.0	101.1	104.0	104.1	100.3	99.9	96.4
Terms of trade for goods (index: 2005=100)	82.4	85.6	93.2	100.0	127.3	132.0	114.4	108.1	127.7
Net resource transfer (millions of dollars)	505	-680	-1 263	-4 752	-7 225	572	56	-5 752	3 236
Total gross external debt (millions of dollars)	27 872	29 587	31 244	28 657	28 897	32 894	34 838	35 731	40 236
Average annual rates									
Employment									
Labour force participation rate ^g	62.9	63.2	62.3	62.5	64.0	63.5	66.4	68.4	70.0
Open unemployment rate ^h	9.4	9.4	9.4	9.6	8.5	8.4	8.4	8.4	7.9
Visible underemployment rate ⁱ	20.6	19.0	18.1	17.8	16.4	16.5	15.6	15.4	14.5
Annual percentages									
Prices									
Variation in consumer prices (December-December)	1.5	2.5	3.5	1.5	1.1	3.9	6.7	0.2	2.1
Variation in wholesale prices (December-December)	1.7	2.0	4.9	3.6	1.3	5.2	8.8	-5.1	4.6
Variation in nominal exchange rate (Annual average)	0.3	-1.1	-1.9	-3.4	-0.7	-4.4	-6.5	2.9	-6.2
Variation in average real wage	4.6	1.6	1.1	-1.9	1.2	-1.8	2.2	3.1	2.6
Nominal deposit rate ^j	3.2	2.9	2.4	2.7	3.4	3.5	3.3	2.8	1.5
Nominal lending rate ^k	23.3	20.2	18.7	17.9	17.1	16.5	16.7	16.0	19.0

Table 1 (concluded)

	2002	2003	2004	2005	2006	2007	2008	2009	2010 ^a
	Percentages of GDP								
Central government									
Total revenue	14.5	15.0	14.9	15.8	17.7	18.2	18.1	15.6	17.0
Current revenue	14.4	14.8	14.8	15.7	17.5	18.1	18.0	15.5	16.8
Tax revenue	12.1	12.9	13.1	13.6	15.2	15.6	15.4	13.4	14.5
Capital income	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.2
Total expenditure	16.6	16.7	16.2	16.5	16.1	16.4	15.9	17.3	17.0
Current expenditure	14.6	14.8	14.4	14.7	14.1	14.2	13.6	13.6	12.7
Interest	2.0	2.0	1.8	1.8	1.8	1.6	1.4	1.2	1.1
Capital expenditure	2.0	1.9	1.8	1.9	2.0	2.1	2.4	3.7	4.3
Primary balance	-0.1	0.3	0.6	1.1	3.4	3.4	3.6	-0.4	1.1
Overall balance	-2.1	-1.7	-1.3	-0.7	1.6	1.8	2.2	-1.7	0.0
Central government public debt	43.2	43.4	40.1	36.9	30.1	26.2	24.1	23.4	21.3
Domestic	6.7	6.4	6.3	7.7	6.9	8.3	8.1	8.2	8.8
External	36.5	36.9	33.7	29.2	23.2	17.9	16.0	15.2	12.6
Money and credit^k									
Domestic credit	13.4	13.2	12.9	13.9	14.6	17.8	14.7	18.5	20.2
To the public sector	-4.8	-4.1	-4.3	-3.4	-3.6	-5.3	-7.1	-5.7	-6.2
To the private sector	30.1	28.7	27.0	28.7	28.6	33.1	33.6	35.5	37.6
Others	-11.8	-11.4	-9.9	-11.3	-10.5	-10.0	-11.7	-11.3	-11.1
Liquidity (M3)	26.1	24.7	24.0	25.8	24.3	26.8	29.9	30.4	33.0
Currency outside banks and local-currency deposits (M2)	9.1	9.4	10.8	11.7	12.0	14.5	15.9	16.9	20.1
Foreign-currency deposits	17.1	15.3	13.2	14.1	12.4	12.4	14.0	13.4	12.9

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Preliminary figures.

^b Based on figures in local currency at constant 1994 prices.

^c Based on figures in local currency expressed in dollars at current prices.

^d Includes errors and omissions.

^e A minus sign (-) denotes an increase in reserves.

^f Annual average, weighted by the value of goods exports and imports.

^g Economically active population as a percentage of the working-age population, Lima metropolitan area.

^h Percentage of the economically active population, Lima metropolitan area.

ⁱ Percentage of the working population, Lima metropolitan area.

^j Market lending rate, average for transactions conducted in the last 30 business days (FTAMN).

^k The monetary figures are end-of-year stocks.

(b) Prices, wages and employment

In the 12 months of 2010, the inflation rate, as measured by the Lima consumer price index, stood at a cumulative figure of 2.1% (compared with 0.2% in 2009), reflecting a 2.9% rise in food and beverages prices and a 12.2% rise in fuel prices. In the first five months of 2011, inflation continued to trend upwards. The rate for the 12 months to May 2011 was 3.9% (4.6% for food and beverages). Despite the steeper price rises, the central bank estimates that inflation will remain within the target range (2% ± 1%), albeit close to the ceiling of this range. The achievement of this target could be jeopardized by a further escalation in food, raw material and fuel prices or a sharper increase in domestic spending.

In 2010 average unemployment stood at 7.9%, (8.4% in 2009). This reduction is due both to the decline in the female unemployment rate (from 10.4% in 2009 to 9.6% in 2010) and in the male unemployment rate (from 6.7%

in 2009 to 6.4% in 2010). The average employment rate stood at 64.5% (compared with 62.7% in 2009) and the average wages remained at similar levels to those observed in 2009. Urban employment across the country in enterprises with more than 10 workers increased by 4.2% in 2010, reflecting the higher employment generated by enterprises with 50 or more workers and employment in commerce. In metropolitan Lima, while these trends have been maintained, job creation was stronger, growing at an average of 6.2% during the year.

In the first four months of 2011, the unemployment rate, at 9.0%, was very similar to the level recorded in the same period of 2010 (9.1%). Average monthly income for this period registered a 6.9% rise compared with the same period in 2010. The monthly minimum living wage, which had been held constant at 550 nuevos soles since January 2008, increased by 30 nuevos soles in December 2010 and subsequently by 20 nuevos soles in February 2011 (a 9.1% increase overall).

Table 2
PERU: MAIN QUARTERLY INDICATORS

	2009				2010 ^a				2011 ^a	
	I	II	III	IV	I	II	III	IV	I	II ^b
Gross domestic product (variation from same quarter of preceding year) ^c	1.9	-1.2	-0.6	3.4	6.1	10.0	9.6	9.2	8.8	...
Goods exports, f.o.b. (millions of dollars)	5 407	6 162	7 174	8 218	7 924	8 164	9 299	10 178	10 017	3 380 ^d
Goods imports, c.i.f. (millions of dollars)	4 883	4 827	5 330	5 970	6 336	6 610	7 815	8 054	8 186	3 095 ^d
International reserves (millions of dollars)	30 961	30 822	32 163	33 175	35 305	35 382	42 502	44 150	46 177	46 353
Real effective exchange rate (index: 2000=100) ^e	100.9	98.9	99.9	100.0	96.8	95.3	95.2	98.5	98.5	101.6
Unemployment rate	9.3	8.5	7.8	7.9	9.2	7.6	7.6	7.2	9.4	...
Consumer prices (12-month percentage variation)	4.8	3.1	1.2	0.2	0.8	1.6	2.4	2.1	2.7	3.1
Producer prices, national products; (12-month percentage variation)	2.7	-2.3	-6.2	-5.1	-0.5	2.5	3.5	4.6	5.8	6.1
Average nominal exchange rate (nuevos soles per dollar)	3.2	3.0	3.0	2.9	2.9	2.8	2.8	2.8	2.8	2.8
Average real wage (variation from same quarter of preceding year)	...	-0.4	...	6.5	...	5.3
Nominal interest rates (annualized percentages)										
Deposit rate ^f	3.5	3.2	2.6	2.1	1.4	1.3	1.6	1.8	2.0	2.6
Lending rate ^f	17.2	16.3	15.6	15.0	19.7	19.2	18.2	18.7	18.6	18.5 ^d
Interbank interest rate	6.4	4.2	1.6	1.2	1.1	1.4	2.3	3.0	3.4	4.1
Sovereign bond spread (basis points) ^g	425	272	205	165	149	215	174	163	171	189
Stock price index (national index to end of period, 31 December 2000=100)	764	1 081	1 253	1 172	1 252	1 157	1 479	1 934	1 817	1 785
Domestic credit (variation from same quarter of preceding year)	-12.5	7.0	18.0	30.6	37.8	29.8	21.1	23.9	15.7	5.3 ^d
Non-performing loans as a percentage of total credit	1.4	1.6	1.6	1.6	1.7	1.7	1.6	1.5	1.5	1.5

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Preliminary figures.

^b Data to May.

^c Based on figures in local currency at constant 1994 prices.

^d Data to April.

^e Quarterly average, weighted by the value of goods exports and imports.

^f Market lending rate, average for transactions conducted in the last 30 business days (FTAMN).

^g Measured by JP Morgan's EMBI+ index to end of period.

(c) The external sector

In 2010, merchandise exports increased by 32% (owing to a 29.9% rise in prices and a 1.6% expansion in volumes); at the same time, imports of goods were up by 37.1% (a 10.1% rise in prices and a 24.5% increase in volumes). The outcome was a trade surplus of US\$ 6.75 billion, although this was not sufficient to offset the increase in the services deficit and the income deficit. The latter was due to higher repatriations of profits and dividends to the rest of the world. As a consequence, the current account balance showed a deficit of US\$ 2.135 billion (equivalent

to 1.5% of GDP). In the first quarter of 2011, merchandise exports remained buoyant (up 26.7%) owing to the growth in exports, both traditional (23.5%) and non-traditional (37.5%). Imports were up by 29.2% in the same period.

In 2010, the terms of trade improved by 17.9% on average in relation to the average 2009 value (10.4% in the first quarter of 2011, compared with the same period of 2010). As a percentage of GDP, the external debt, consisting mainly of long-term debt, stood at 26.3% in December 2010 (28% in December 2009). In December 2010, net international reserves stood at US\$ 44.15 billion (US\$ 46.18 billion in March 2011).