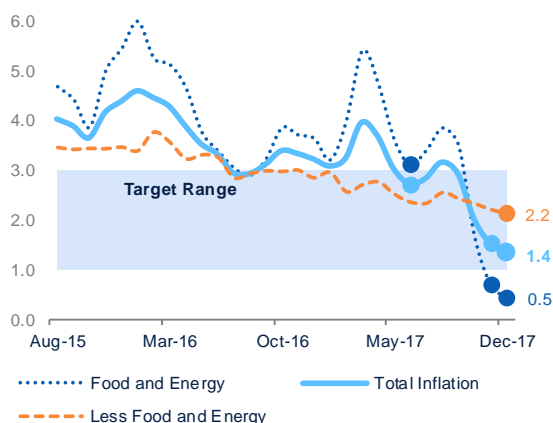


## 7. Inflation will bottom out at the end of this quarter, but will then tend to move towards the middle of the target range

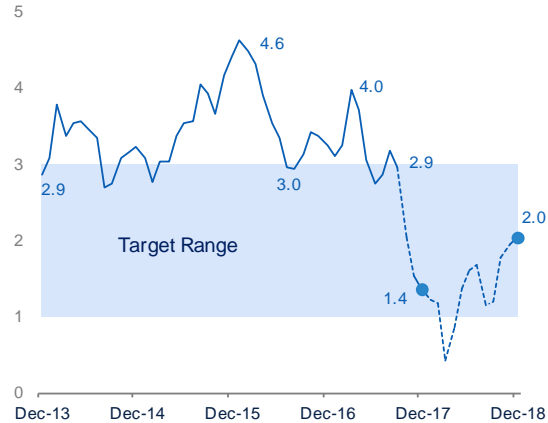
In the last quarter of 2017, inflation fell sharply, from 2.9% in September to 1.4% in December. The prices of some foodstuffs, which had risen temporarily with the impact of *El Niño Costero*, tended to return to normal. The latest inflation figure is the lowest for seven and a half years. Indicators of inflationary trends also showed a declining trajectory in the last few months and over the course of the year, probably as a reflection of the appreciation of the national currency and the weakness of economic activity.

**Figure 7.1** Inflation: total; without food and energy; and only food and energy (change % YoY)



Source: INEI (National Statistics Institute), Central Reserve Bank of Peru and BBVA Research

**Figure 7.2.** Inflation (change % YoY of the CPI)



Source: INEI (National Statistics Institute), Central Reserve Bank of Peru and BBVA Research

We estimate that the bulk of the food price corrections had already taken place. Even so, due to the high base for year-on-year comparison, inflation will continue to fall in the first quarter of 2018 and for a short time will be below the target range (see Figure 7.2). Later on, however, it will tend to move closer to the middle of the target range, which we estimate will reach towards year-end. This reflects four things. Firstly, that the rate of YoY food price increases, which fell sharply last year, will return to normal. Thus the projection assumes no supply-side shocks in this respect. Secondly, that the exchange rate will hold relatively steady, in contrast to what happened in 2017, when it fell (in terms of PEN per USD) by 4%, bringing inflation down with it. Thirdly, and rather containing price increases, although the economic activity will continue gaining traction, there will still be slacks in the economy. Lastly, and also partly offsetting the first two factors, the rate of YoY increase in the price of oil will slow in the middle part of this year, generating downward pressure on domestic inflation.

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