

Peru Economic Outlook

4Q21

Closing date: October 18

Key messages (I)



Global economic recovery

Our baseline scenario estimates that the recovery of global activity will continue in the coming quarters, with an expansion of 6.1% in 2021 and 4.8% in 2022, supported by the progress of vaccination against COVID-19 and economic policies that will remain expansionary. External tailwinds will continue to support the Peruvian economy. However, this global recovery will lose momentum due to negative supply shocks, such as bottlenecks in global output and rising energy prices. Supply shocks will also push inflation upward, leading central banks to lower monetary stimulus. With the moderation of global growth and adjustment of monetary conditions, metal prices will drop, although they will remain at attractive levels for mining investment.



Local

In the third quarter, the economy performed relatively well, better than expected. During that period, the third local wave of the pandemic did not materialize (although we cannot rule out the possibility that it may materialize in the coming months), which allowed the capacity of shopping centers and restaurants to continue to increase; it also favored the movement of people. In addition, liquidity measures (withdrawal of funds from AFP) continued to support household expenditure. However, deterioration in confidence brought about by political noise would have inhibited further recovery and anticipates a slowdown ahead.

Key messages (II)



Forecasts

On the local side, our baseline scenario considers four main elements. First, in the health sector, a possible third wave of infections, albeit with limited impact on activity. Then, in 2022, with the majority of the population already vaccinated, capacities will gradually return to their pre-pandemic levels, which will particularly benefit the production sectors that have so far been the most affected by isolation measures. This will provide an additional boost to activity.

Second, the baseline scenario considers a high and sustained level of uncertainty due to a context characterized by sustained political tensions, as well as low private-sector expectations for economic and other measures to be implemented by the government. All of this is already reflected in the levels currently recorded by consumer and business confidence indicators. Such an environment will lead to caution in private spending, especially in investment spending.

The baseline scenario also envisions that new copper mines will start production, which together account for around 20% of current extraction at full operational capacity (among them, Quellaveco). Finally, it is assumed that monetary and fiscal policies will continue to support activity, but to a lesser extent.

In this context, we expect the Peruvian economy to grow 12.2% in 2021 and 2.3% in 2022.

Key messages (III)



Fiscal

On the fiscal accounts side, the deficit, which reached a level equivalent to 8.9% of GDP in 2020, is expected to decline to 3.8% of GDP this and next year, and by 2023–2026 will be at an average level of 3.5%. Short-term deficit moderation will reflect the recovery of revenue, both from higher metal prices and the normalization of domestic demand, as well as more contained expenditure as requirements for addressing the health emergency decline. **This decrease in the deficit will not be enough to stabilize the public debt-to-GDP ratio over the next few years, which we estimate will follow an upward trajectory and will stand at around 42% by 2026. Thus, the risk of further cuts to the sovereign credit rating remains latent.**



Exchange rate

For the rest of this year, and during 2022, we anticipate that the exchange rate will continue to show episodes of volatility linked to the political scene and the start of the Fed's tapering. The weakening of the Peruvian currency caused by these two factors will be partly offset by a surplus trade balance, which will hit a record high in 2022. In this context, we estimate **that the local USD price will close 2021 between 4.00 and 4.10 soles per USD, while in 2022 it will close between 4.15 and 4.25 soles per USD.** It should be noted that our estimates suggest that the Peruvian currency is still undervalued (around 3.0%), meaning that an environment of greater political stability or significant improvement of macroeconomic fundamentals could be reflected in a strengthening of the Peruvian sol.

Key messages (V)



Inflation

We expect year-on-year inflation to be 5.3% by the end of this year and to remain on average close to 5.0% during the first half of 2022. Then, in the second half of next year, a favorable base effect, normalization in international prices for agricultural commodities, oil and gas, as well as lower exchange pressures, will allow inflation to return to the target range and close the year at 2.6%.



Monetary policy rate

The Central Bank will continue the process of normalizing the monetary position in the coming months in order to contain an unanchoring of inflationary expectations. In this context, we estimate that the reference rate will be 2.0% at the end of 2021 and 3.0% in 2022. Despite these adjustments to the reference rate, the monetary position will remain expansionary in the coming months.



Risks

(i) **External**: slower global growth or higher inflation; (ii) **Health**: an exacerbation of the health crisis due to the emergence of new, more resistant or contagious variants of COVID-19; and (iii) **Political scene**: tensions rise and lead to a greater deterioration in confidence than already observed.

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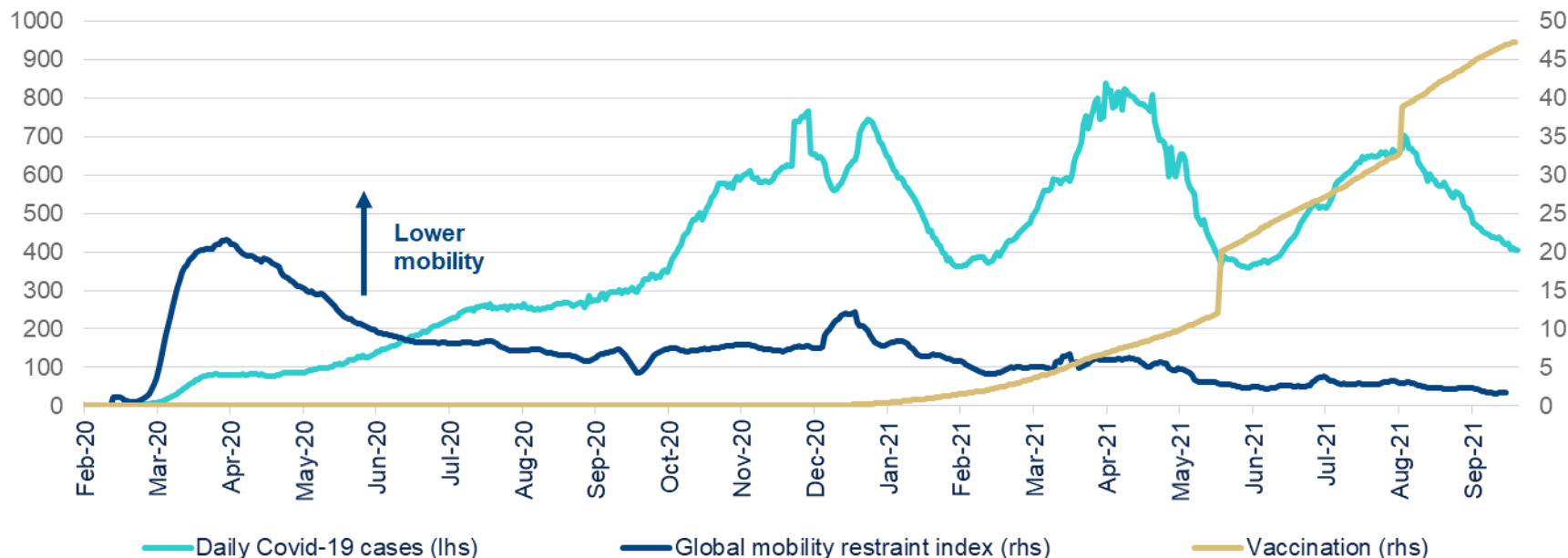
02

How are global activity
and the financial markets
evolving?

Vaccination has reduced the economic impact of waves of infection, but the Delta variant remains a concern, particularly in China and the US

WORLD: DAILY CODIV-19 CASES, POPULATION VACCINATED AND MOBILITY RESTRAINT INDEX (*)

(THOUSANDS OF CONTAGIONS, 7-DAY MOVING AVERAGE; SHARE OF THE POPULATION WITH AT LEAST ONE DOSE OF THE ANTI-COVID VACCINES; MOBILITY RESTRAINT: 7-DAY MOVING AVERAGE)



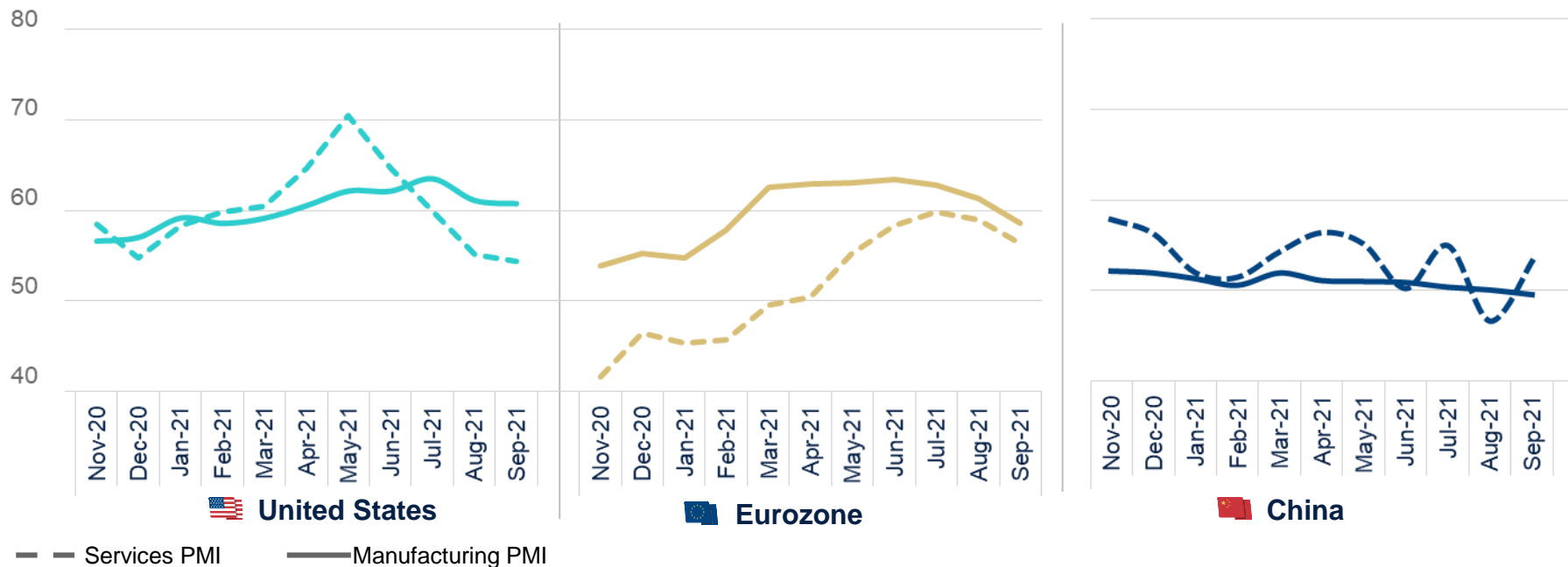
(*) The mobility restraint index reflects changes with respect to the period of reference (January 3 to February 6 2020). Higher values represent lower mobility.

Source: BBVA Research based on data by John Hopkins University, Google and Our World in Data.

Growth is slowing following a strong rise linked to the economic reopening in the first half of the year...

PMI INDICATORS

(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)

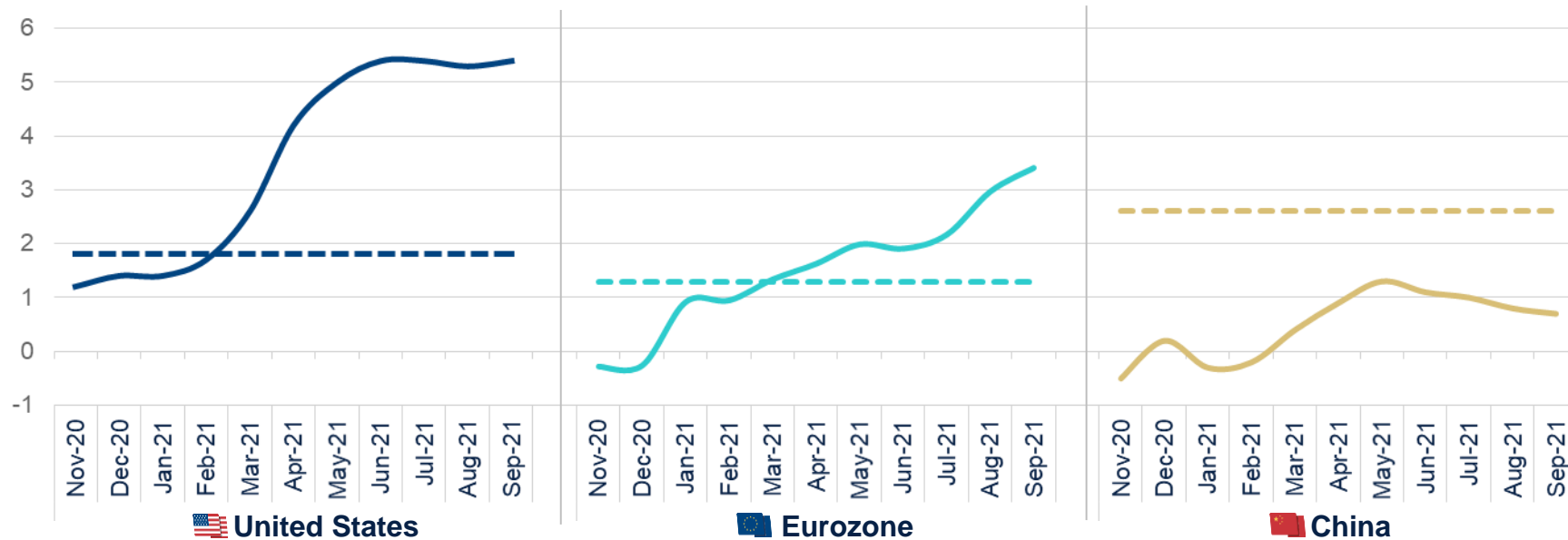


Source: BBVA Research based on data from Haver.

... while inflationary pressures continue, more acutely in the US.

INFLATION: CPI

(% Y/Y, END OF PERIOD)

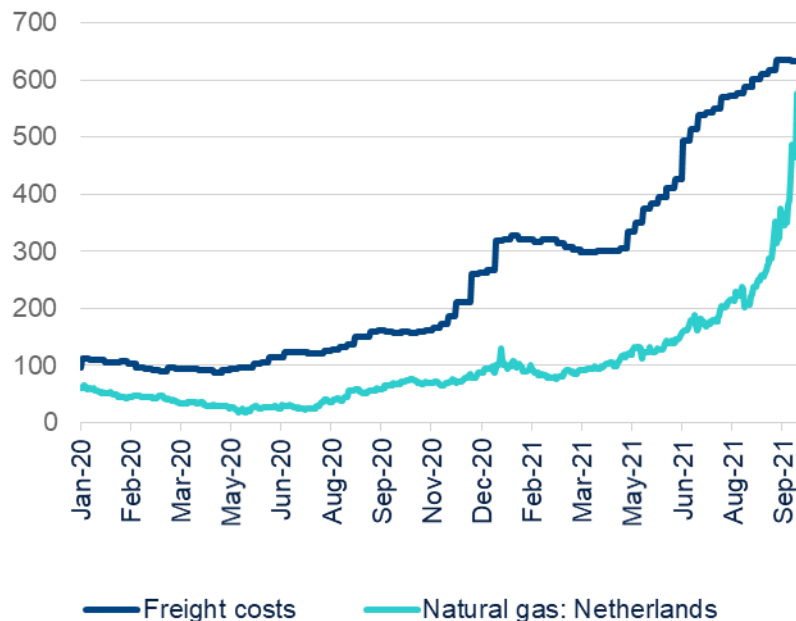


— Average 2010–2019 — Observed

Source: BBVA Research based on data from local statistical sources.

Global supply chain problems have contributed both to the slowdown in growth and to greater inflationary pressures

SEA FREIGHT RATE AND GAS PRICE (*) (INDICES)



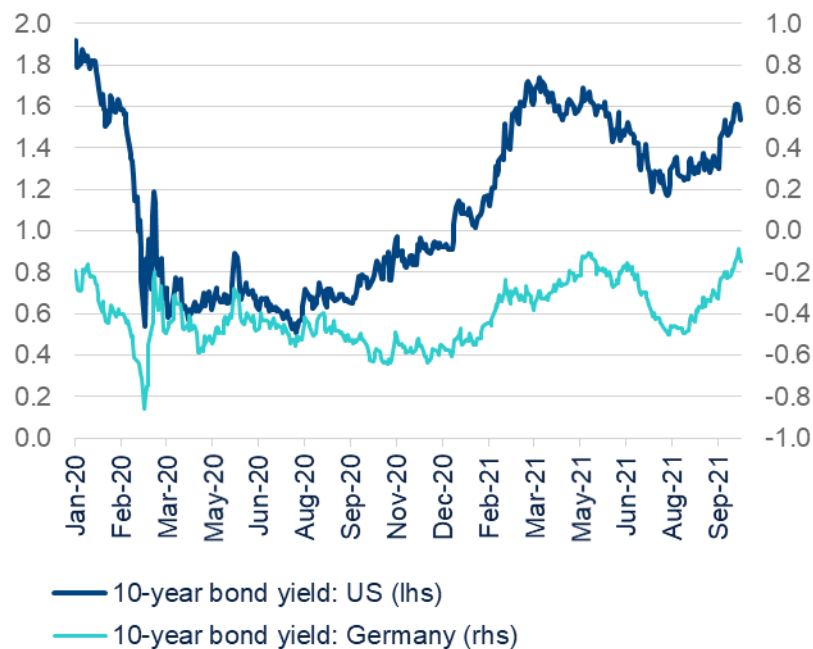
(*) Sea freight rate: composite global indicator. Dutch natural gas: future price.
Source: Bloomberg. Preparation: BBVA Research.

- More significant and persistent bottlenecks than expected, particularly in the manufacturing and transport sectors.
- In addition, the price of raw materials, especially in the **energy sector**, has risen significantly.
- A set of factors lies behind these strong and unexpected cost pressures:
 - supply rigidity, especially in response to spread of the Delta variant in China and the US.
 - shortage of workers in some sectors
 - demand resilience and rapid reopening
 - climate disruptions
 - energy transition policies
 - trade protectionism
 - geopolitical tensions

The Fed's announcement of the withdrawal of stimuli (tapering) as early as 2021 puts upward pressure on bond yields,...

10-YEAR BOND YIELD

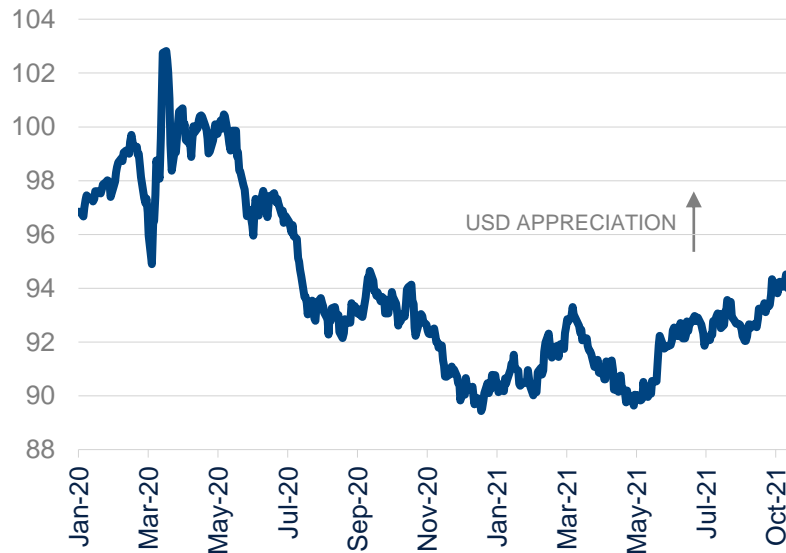
(%)



- US bond yields have increased given the prospect that the Fed will begin tapering somewhat earlier than expected and forecasts of higher inflation.
- The USD has appreciated against other currencies and emerging currencies.
- Capital flows to emerging markets have slowed.
- Financial volatility has remained relatively limited, despite the debt crisis of the Evergrande real estate group in China.

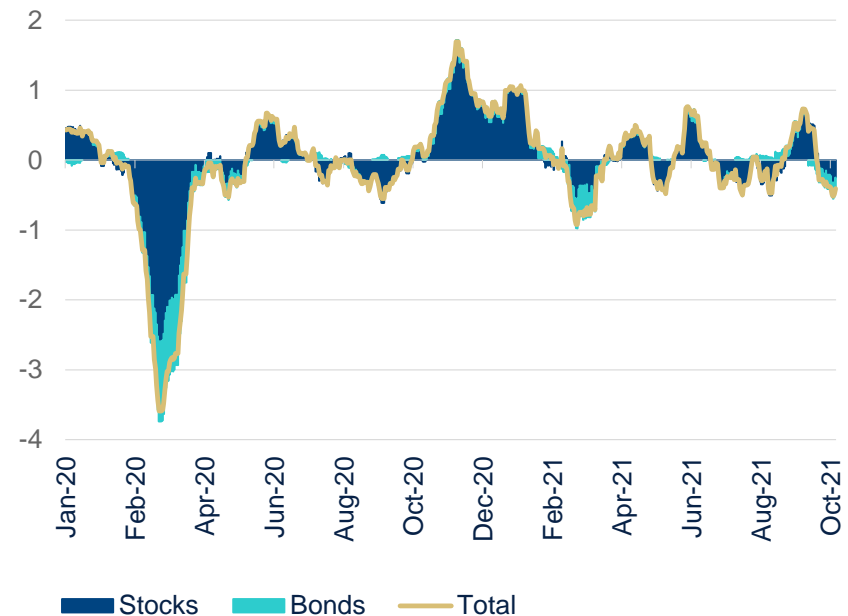
... supports the USD, induces moderation of capital inflows into EM and...

DXY
(INDEX)



Source: Bloomberg. Preparation: BBVA Research.

CAPITAL FLOWS TO EMERGING COUNTRIES
(USD BILLIONS, AVERAGE 28-DAY MOVING AVERAGE)

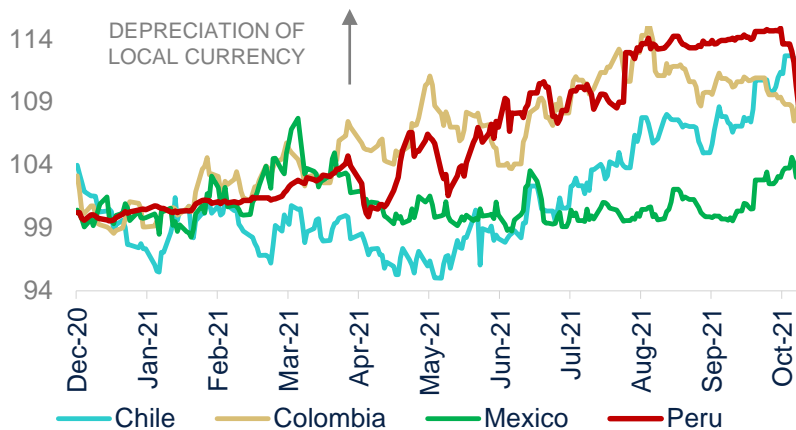


Source: Bloomberg and IIF. Prepared by BBVA Research.

... negatively affects currencies and asset prices in LatAm

LATAM: CURRENCIES VS. USD

(INDEX, DECEMBER 2020 = 100)

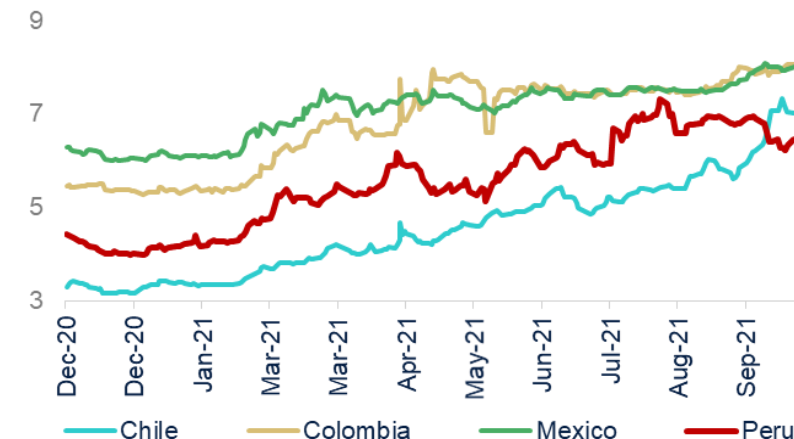


LATAM: CURRENCIES VS. USD

% change %	Chile	Colombia	Peru	Mexico
Current vs. End 2020 (10.18.2021) (12.31.2020)	14.9%	9.9%	9.1%	2.5%

LATAM: 10-YEAR SOVEREIGN BOND YIELDS

(POINTS)



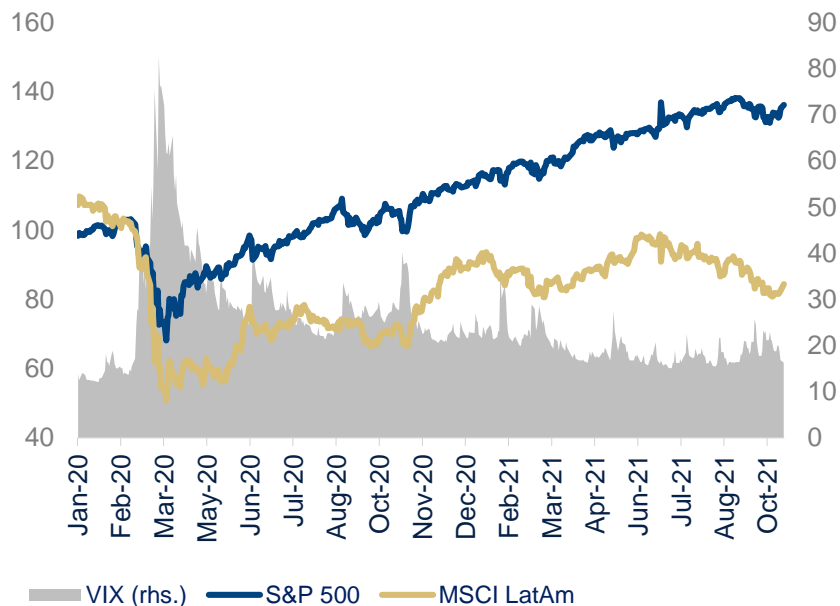
LATAM: CHANGE IN 10-YEAR SOVEREIGN BOND YIELDS

(bps)	Chile	Colombia	Peru	Mexico
Current vs. End 2020 (10.18.2021) (12.31.2020)	387	271	244	195

Relatively limited financial market volatility despite Evergrande crisis (no further transmission to LatAm markets observed)

KEY VOLATILITY INDICATORS

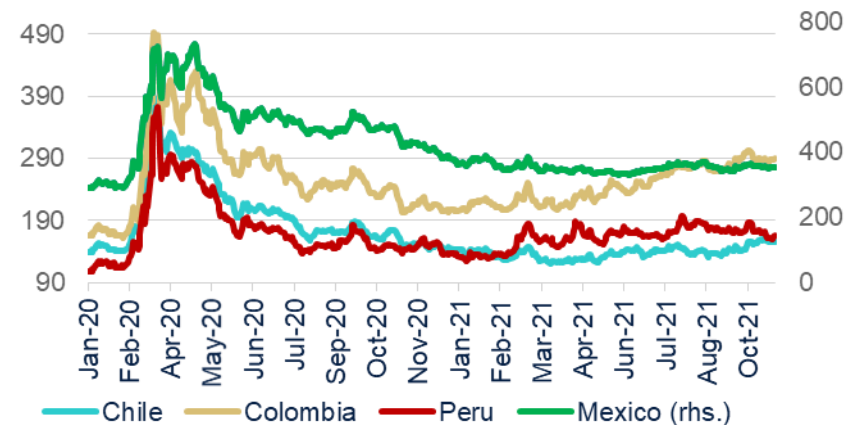
(INDEX, FEBRUARY 2020 = 100)



Source: Bloomberg. Preparation: BBVA Research.

LATAM: EMBI

(POINTS)



LATAM: EMBI (POINTS)

	Colombia	Peru	Chile	Mexico
Current (10.18.2021)	291	172	161	356
End 2020 (12.31.2020)	206	132	144	361
Bps: Current vs. End 2020	85	40	17	-5

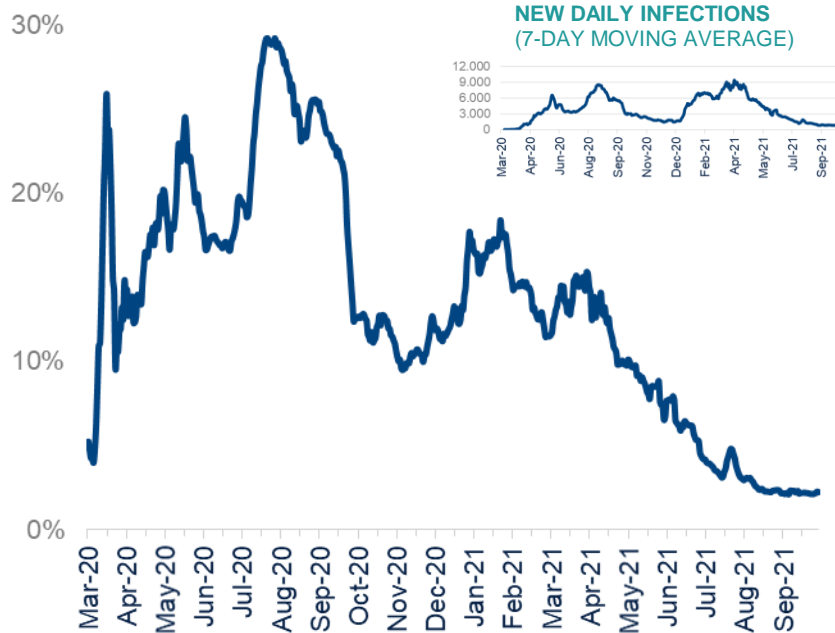
Source: Bloomberg. Preparation: BBVA Research.

03

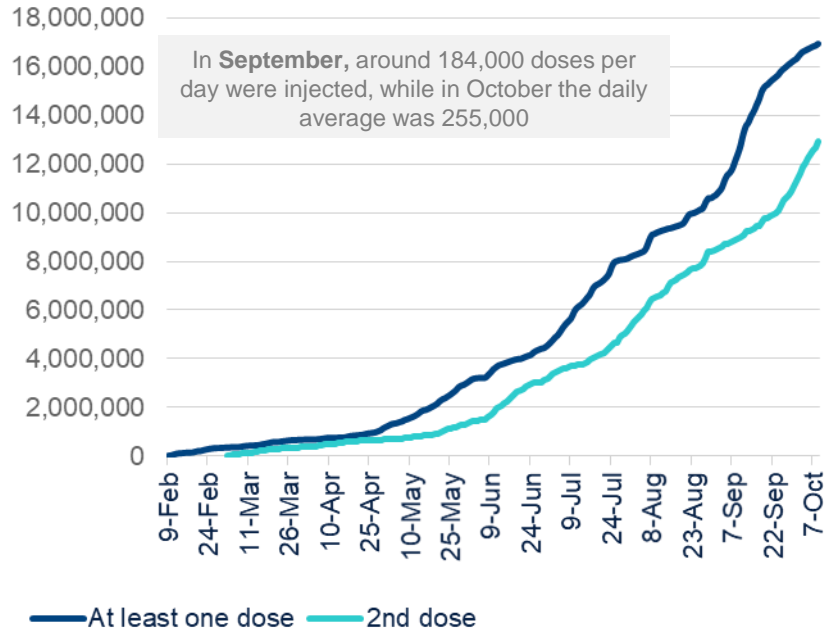
How is local activity evolving?

Health indicators linked to COVID-19 are currently developing favorably and the vaccination process continues to progress

DAILY TESTS WITH POSITIVE RESULTS (% OF TOTAL, 7-DAY MOVING AVERAGE)

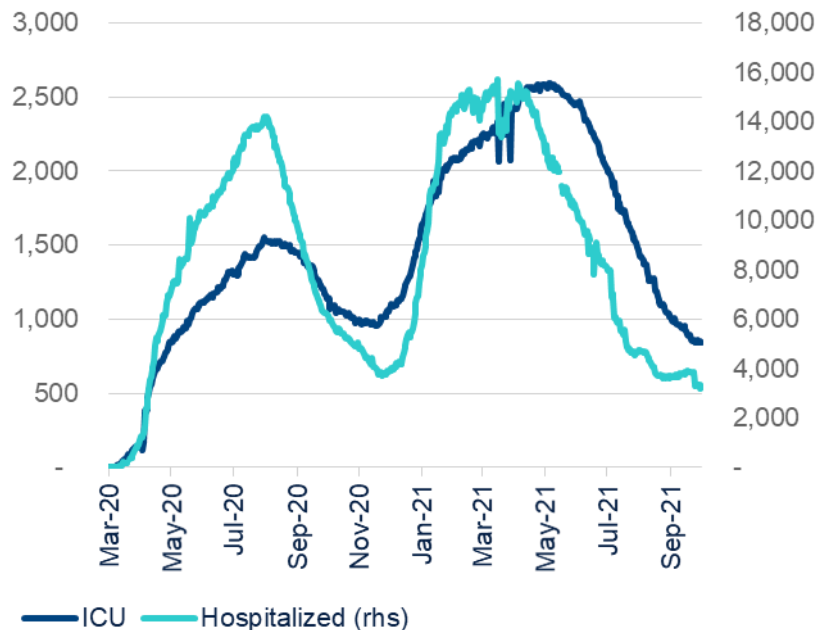


PROGRESS OF VACCINATION PROCESS (NO. OF PERSONS)



The number of hospitalizations and deaths per day has fallen steadily

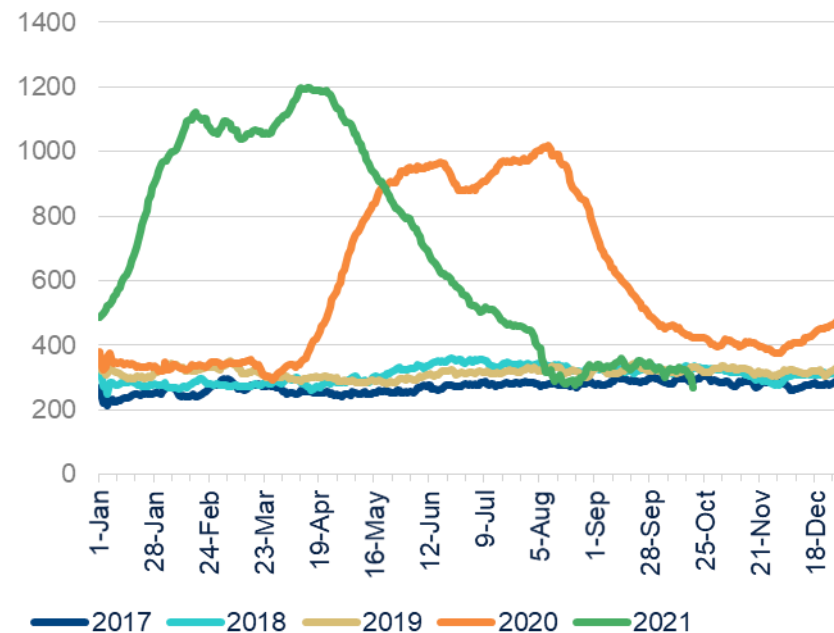
NO. OF PERSONS HOSPITALIZED FOR COVID-19



Source: Ministry of Health of Peru. Prepared by BBVA Research.

DEATHS PER DAY

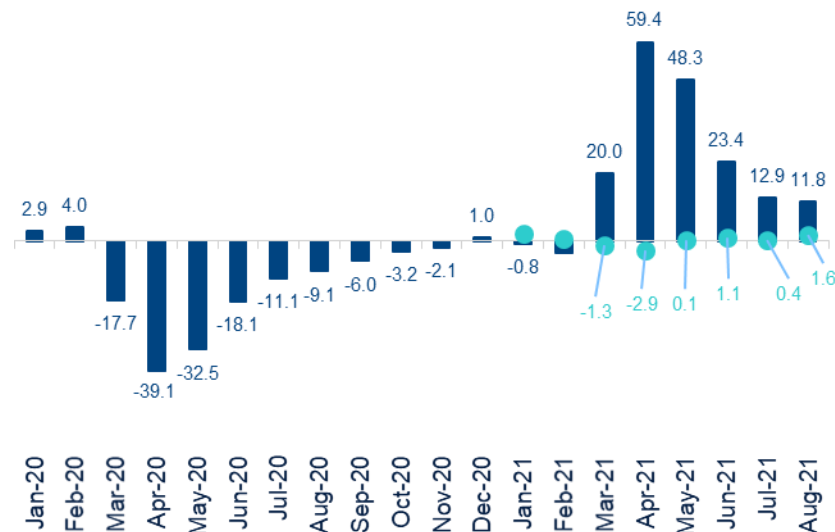
(ROLLING AVERAGE FOR LAST SEVEN DAYS)



Source: Ministry of Health of Peru. Prepared by BBVA Research.

On the activity side, it continues to show relatively favorable performance...

GDP (YOY % CHANGE)



● Var.% regarding the same period in 2019

GDP BY PRODUCTIVE SECTOR

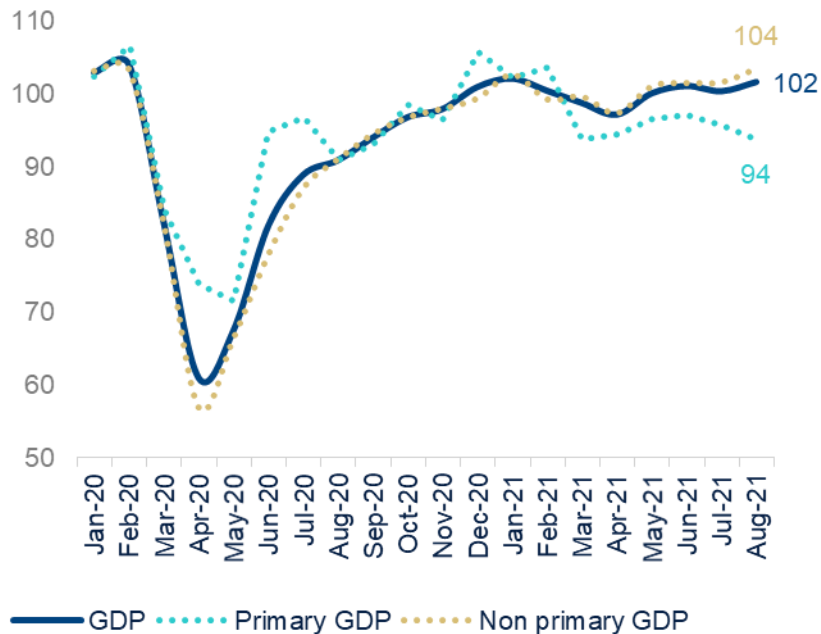
	% change relative to the same period 2020			% change relative to the same period 2019		
	Jun 21	Jul 21	Aug 21	Jun 21	Jul 21	Aug 21
Agriculture	8.9	11.1	6.0	7.6	5.9	3.4
Fisheries	-37.7	-41.4	-29.9	-7.6	-25.8	-28.1
Mining and Hydrocarbons	7.8	-0.9	3.1	-7.9	-7.2	-8.7
Metal mining	7.1	1.4	5.1	-7.5	-5.2	-6.0
Hydrocarbons	11.9	-13.6	-8.4	-10.1	-18.0	-23.4
Manufacturing	19.1	6.7	11.6	4.6	-2.0	0.5
Electricity and water	15.2	7.1	5.9	2.9	1.8	3.2
Construction	90.7	37.4	25.5	8.8	20.2	18.0
Trade	38.1	13.3	9.9	-0.4	1.4	1.5
Other services	21.3	15.3	13.1	-0.7	-0.6	2.0
Financial services	6.2	5.1	2.8	22.6	21.9	23.1
Telecommunications	5.9	7.6	6.5	12.2	12.7	12.9
Accommodation and restaurants	225.9	124.2	96.8	-46.8	-36.8	-22.8
GDP	23.4	12.9	11.8	1.1	0.4	1.6
Primary GVA	2.4	-1.2	3.0	-3.0	-4.4	-6.3
Non-primary GVA¹	30.2	16.7	13.7	1.5	1.6	3.5

1: Excludes import duties and taxes.

... even accelerating at the margin...

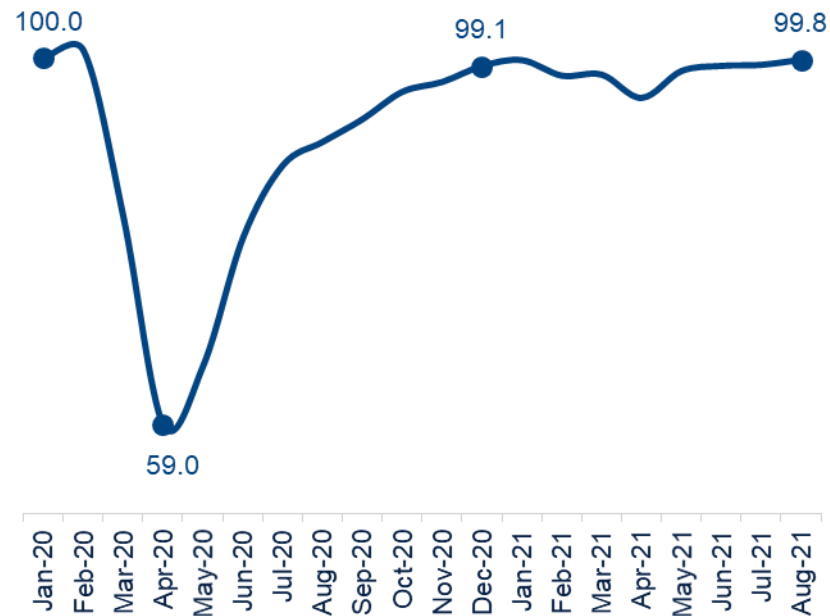
GDP

(LEVEL COMPARED TO SIMILAR PERIOD IN 2019)



GDP

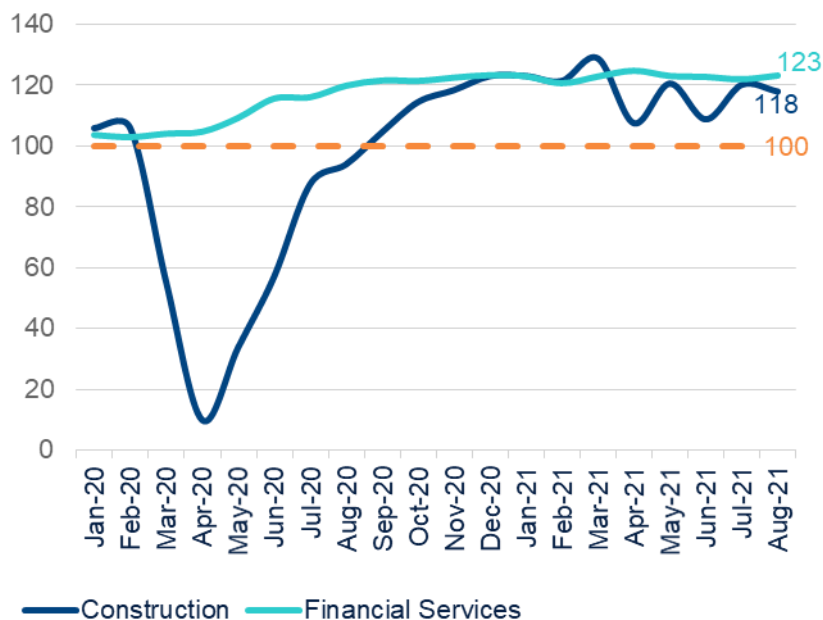
(SEASONALLY ADJUSTED LEVEL, INDEX, FEBRUARY 2020 = 100)



... although with heterogeneity at the sectoral level (slower normalization in activities most affected by isolation measures)

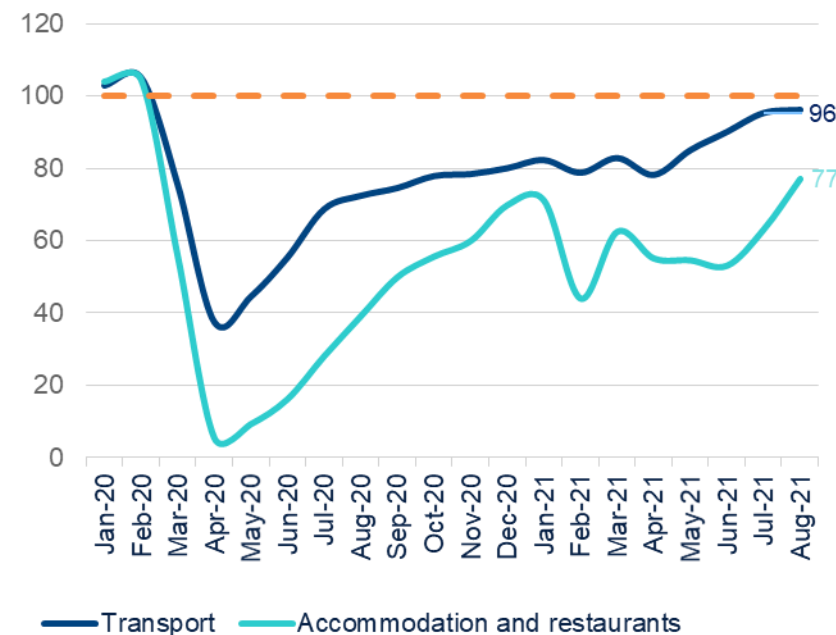
SECTORAL GDP: SELECTED ACTIVITIES

(INDEX, 100 = LEVEL IN SAME PERIOD 2019)



SECTORAL GDP: SELECTED ACTIVITIES

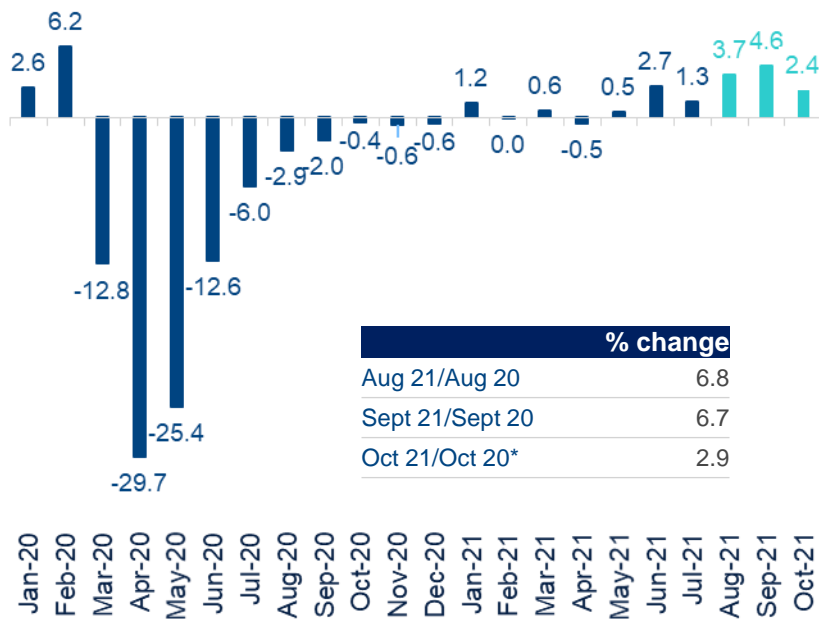
(INDEX, 100 = LEVEL IN SAME PERIOD 2019)



High-frequency indicators show that the economic expansion trend continued in September, with a surprising upturn in 3Q21

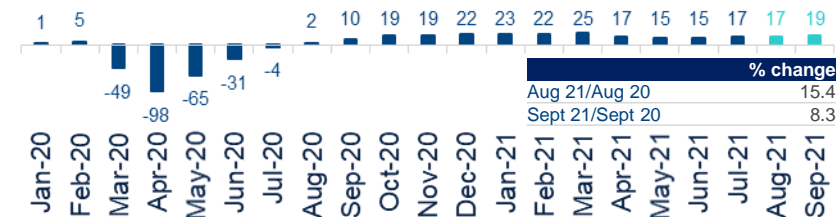
ELECTRICITY PRODUCTION

(YoY % COMPARED TO THE SAME PERIOD IN 2019)



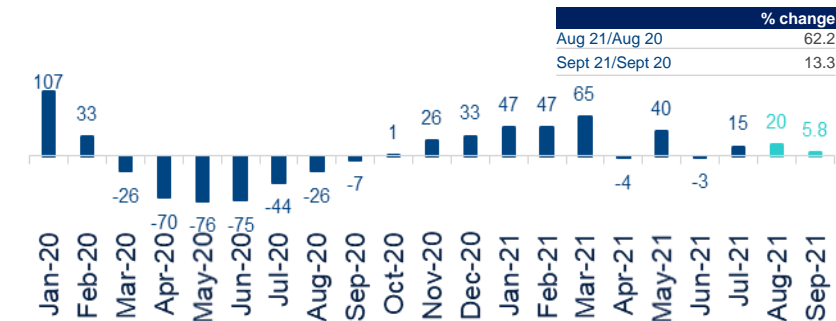
DOMESTIC CEMENT CONSUMPTION

(YoY % COMPARED TO THE SAME PERIOD IN 2019)



PUBLIC INVESTMENT

(YoY % COMPARED TO THE SAME PERIOD IN 2019)



* Considers first 19 days of October.

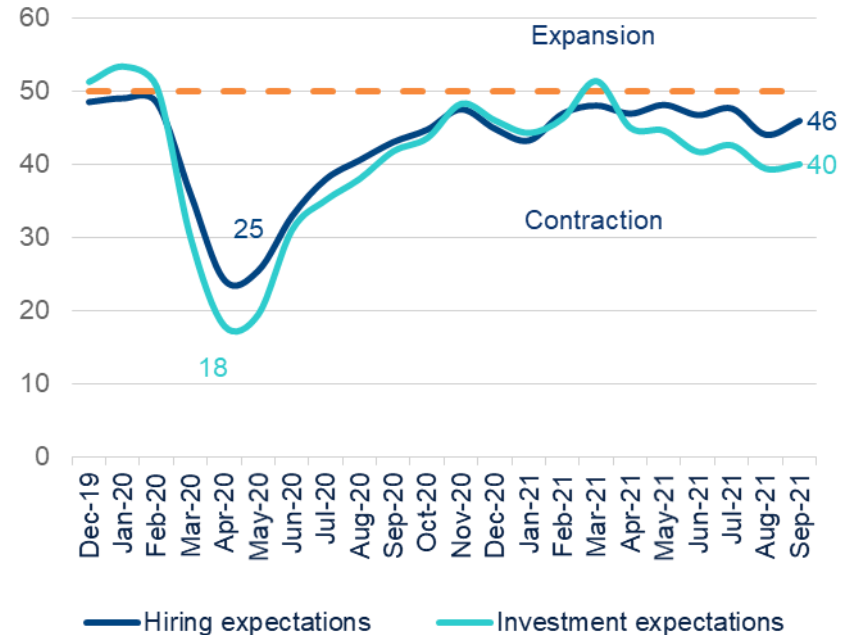
Source: COES and BCRP. Prepared by BBVA Research.

More forward-looking indicators of expenditure (business confidence), weakened by political noise, anticipate a loss of momentum in activity

BUSINESS CONFIDENCE (POINTS)



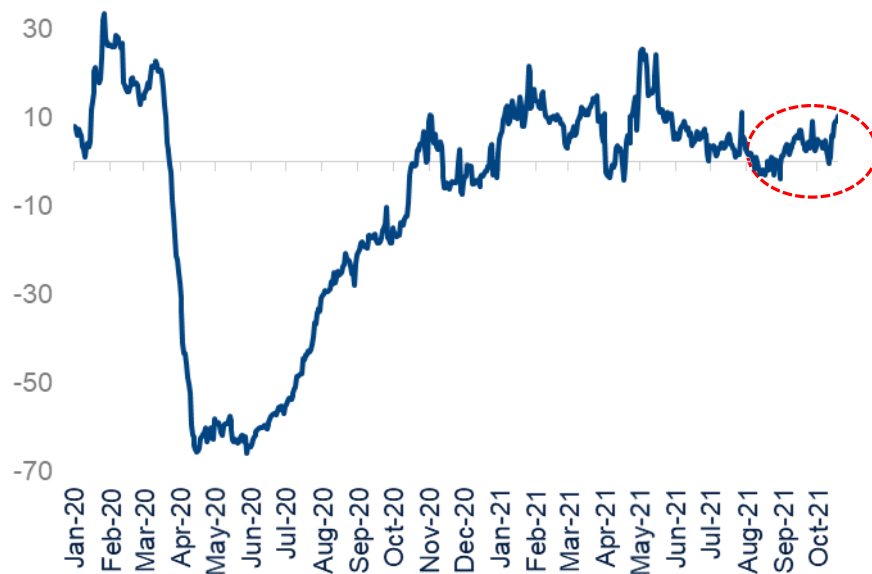
CONFIDENCE TO INVEST AND HIRE (POINTS)



In this vein, high-frequency (real-time) indicators linked to investment show a slowdown since August

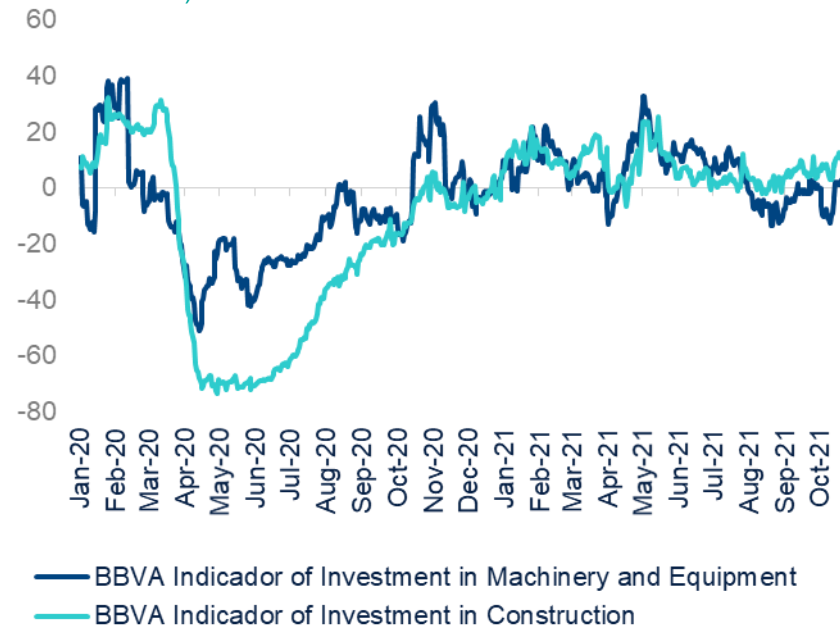
BBVA BIG DATA INVESTMENT INDEX ¹

(YOY % CHANGE VS. THE SAME PERIOD OF 2019, IN REAL TERMS)



BBVA BIG DATA INVESTMENT BY COMPONENT INDEX ¹

(YOY % CHANGE VS. THE SAME PERIOD OF 2019, IN REAL TERMS)



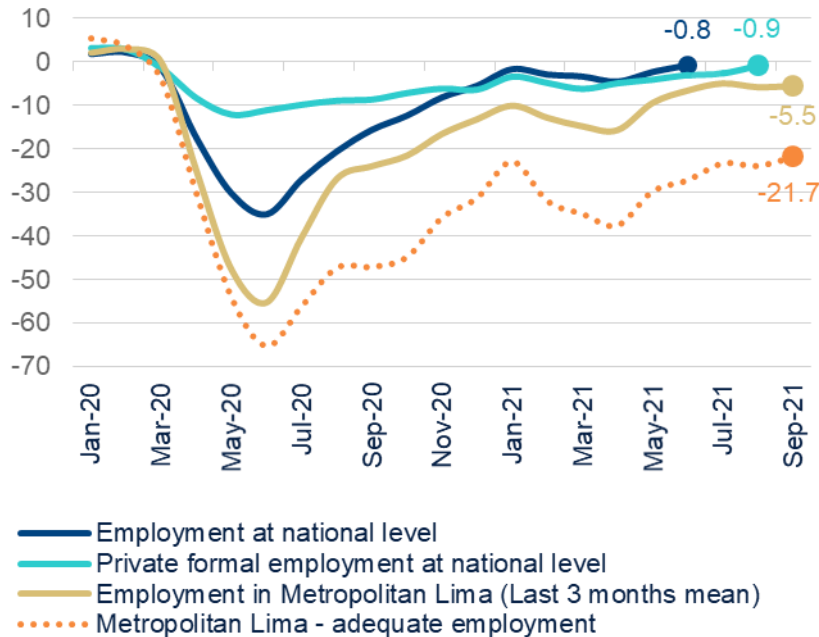
1: Information as at October 18, 2021. Average last 28 days. Information on income into selected company accounts is used.

Source: BBVA. Preparation: BBVA Research.

The labor market also continues to recover... although more recent data (Lima) suggest that normalization may be losing traction

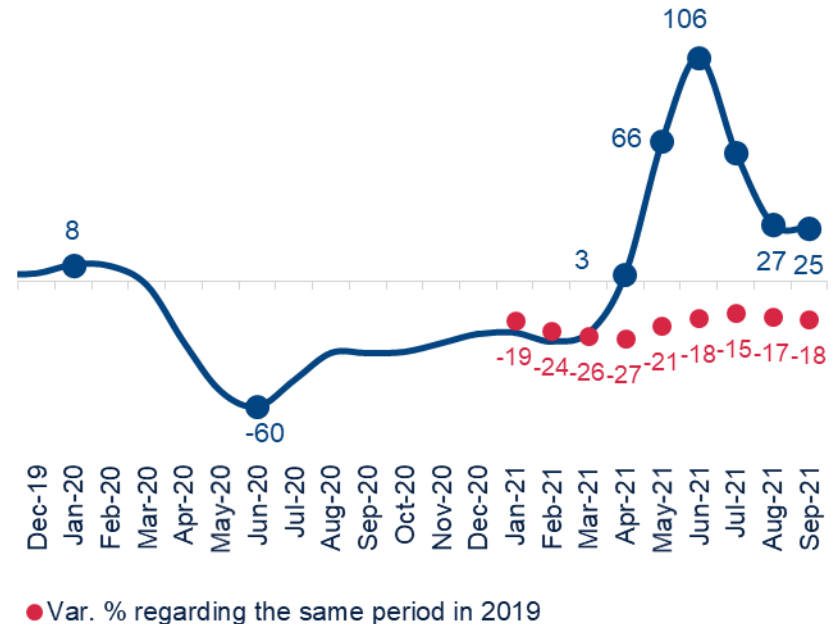
EMPLOYMENT

(Y/Y % COMPARED TO THE SAME PERIOD IN 2019)



TOTAL WAGE BILL IN LIMA

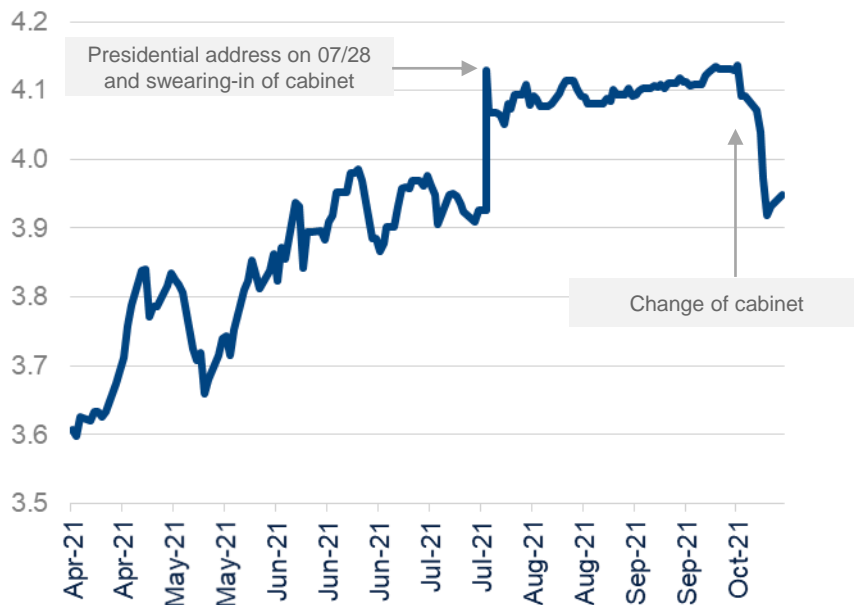
(ADJUSTED FOR INFLATION, THREE-MONTH MOVING AVERAGE, CHANGE % COMPARED TO THE SAME PERIOD IN 2019)



The political environment also weakened local financial assets... but with the change of cabinet there was some reversal in these downward pressures

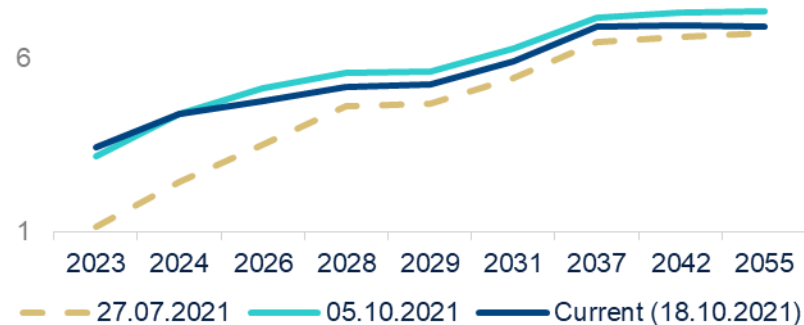
EXCHANGE RATE

(PEN PER USD)



SOVEREIGN BOND YIELD CURVE

(%)



SOVEREIGN BOND YIELDS

(%)

	2023	2024	2026	2028	2029	2031	2037	2042	2055
07.27.21	1.14	2.45	3.54	4.64	4.73	5.44	6.50	6.64	6.73
10.05.21	3.19	4.43	5.16	5.60	5.65	6.28	7.21	7.33	7.38
Current: 10.18.2021	3.43	4.35	4.78	5.22	5.32	5.95	6.91	6.96	6.91

(Bps)

10.05.21 vs. 07.27.21	205	197	162	96	93	84	71	69	65
10.18.21 vs. 10.05.21	24	-7	-38	-38	-33	-34	-30	-37	-46

04

Quarterly review of macroeconomic forecasts

4.1. GDP and economic activity

External environment: recovery will continue, but with less momentum from supply shocks, which will put pressure on inflation and central banks

KEY ASSUMPTIONS OF THE EXTERNAL ENVIRONMENT

Bottlenecks



Greater than expected impact on economic activity (-) and inflation (+); these could extend until mid-2022.

Economic policy



Expansionary fiscal and monetary policies in the G3 despite the onset of gradual stimulus withdrawal (Fed tapering in 4Q21 and rate hikes starting in 4Q22).

Coronavirus pandemic



Gradual return to "normality" continues; future infection outbreaks will have less impact on the economy.

Activity and inflation



Robust growth, although somewhat weaker than previously estimated, relatively high inflation, although it will lose strength from 2022.

Financial markets



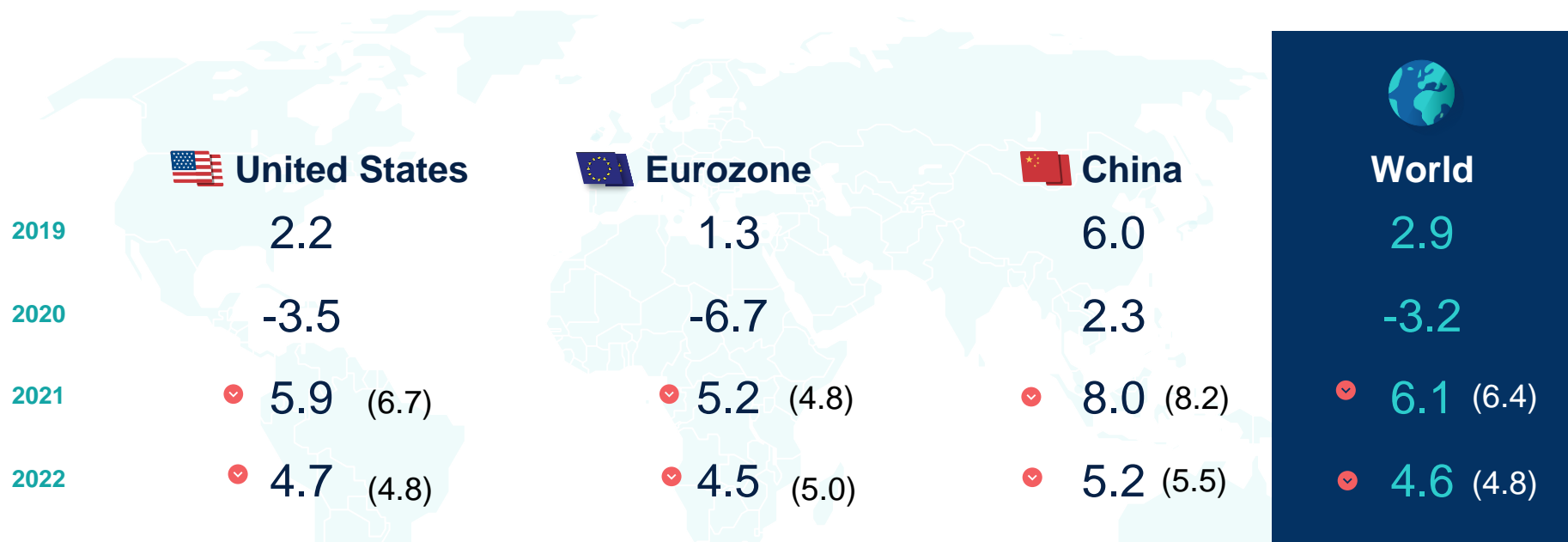
Risk assets pressured by the Fed's withdrawal of monetary stimuli; a USD that has appreciated somewhat more than expected.

Emerging economies



Complex environment: delayed exit from the pandemic, inflation pressuring central banks, lower global liquidity; commodity prices: positive for exporters.

Less robust global growth due to supply shocks and a somewhat faster slowdown in China



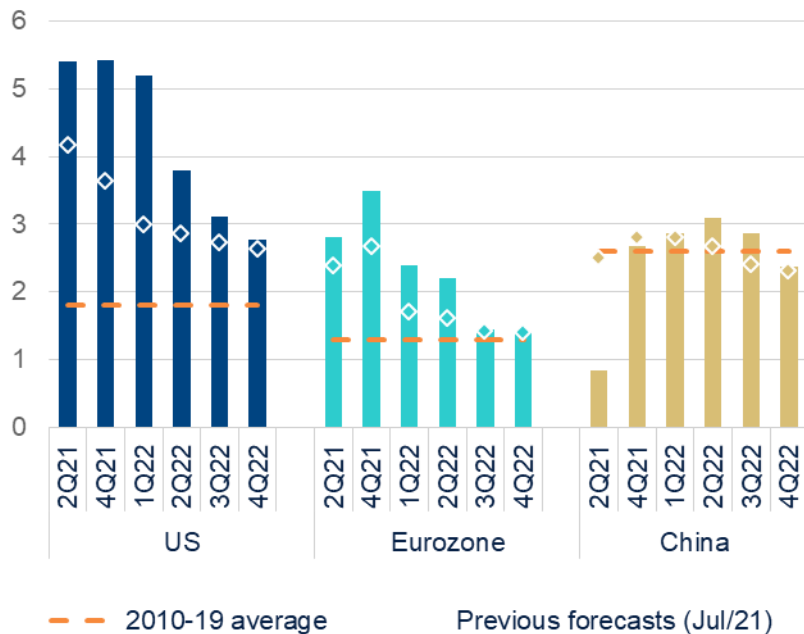
▼ Outlook revised downward. Previous forecast (July) in parentheses.

Source: BBVA Research.

Inflation will be higher temporarily, but will slow gradually in 2022

INFLATION

(CPI, QUARTERLY AVERAGE, YoY % CHANGE)

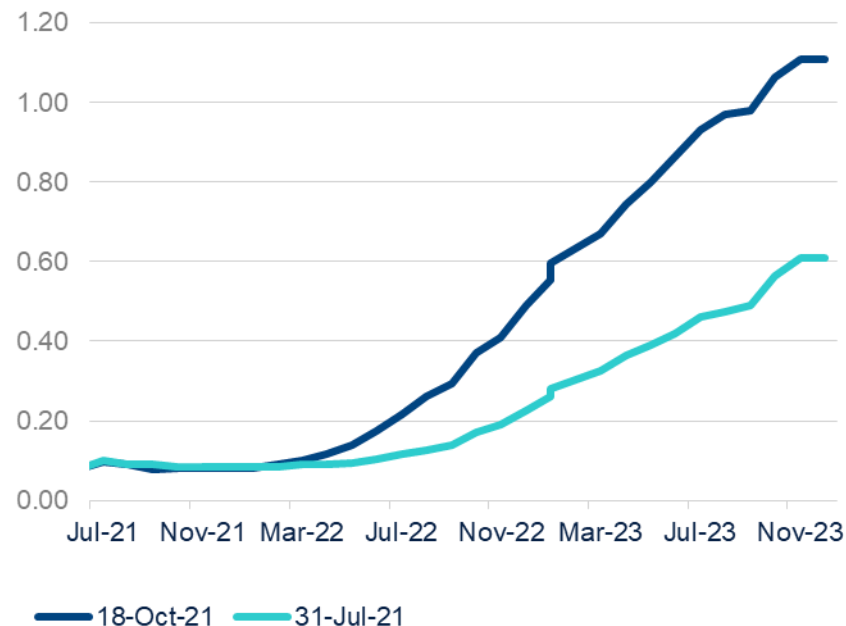


- The more favorable base effects, the expected transient nature of supply shocks and the absence of generalized wage pressures should see **inflation moderation from 2022**.
- However, **risks are skewed upward**. Anchoring expectations will be key.
- **Chinese** inflation remains low due to positive base effects, but rising production costs and energy prices will create upward pressure in the coming quarters.
- **Inflation forecasts have been revised upward** from estimates in July for the US and Eurozone.

Monetary policy in the US: Fed begins the withdrawal of stimuli with tapering from 4Q21 and rate increases within a year

FED RATE IMPLIED IN FUTURES

(%)



Tapering:

- Employment took a surprising drop in September, but not enough to prevent the Fed from starting tapering soon.
- Fed minutes (September 21–22) point in this direction.
- Job creation will likely be more favorable in October.
- Tapering should end in mid-2022.

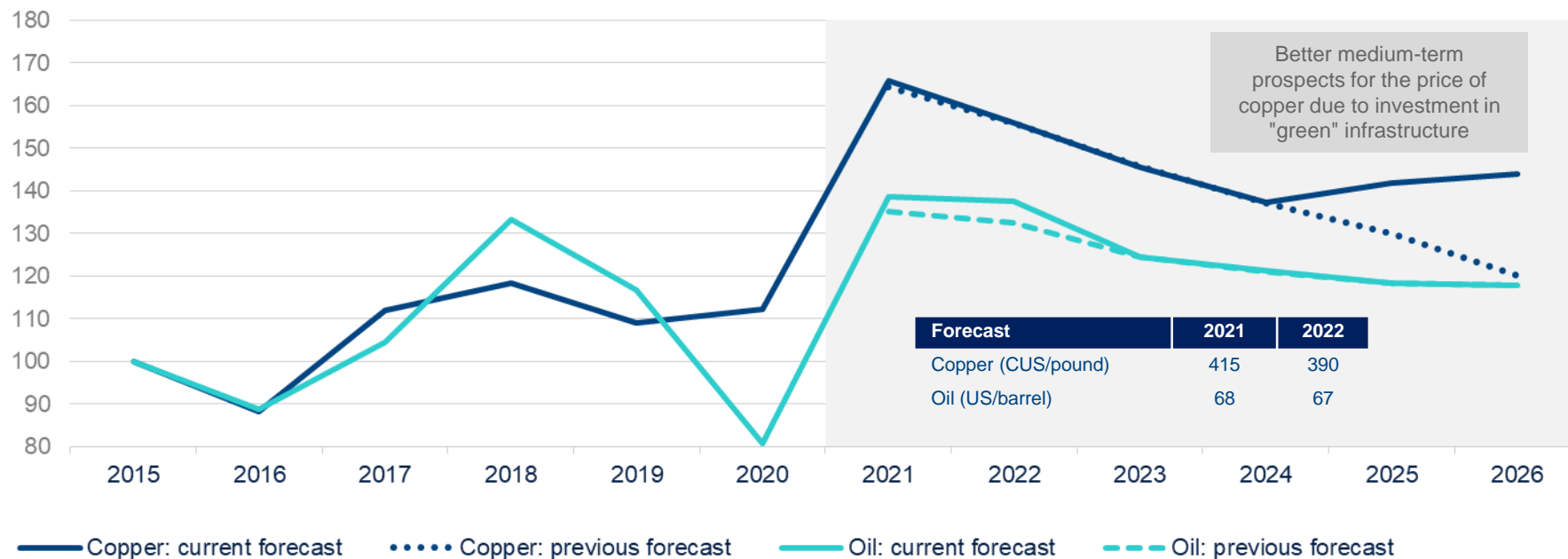
Fed rate increases:

- Inflation will remain high in the short term, above 2.5% even in 4Q22 (slightly higher than the FOMC projection).
- The start of the upward cycle of rates is contingent on the achievement of challenging objectives, such as full employment.
- However, the balance between the labor market and the price outlook suggests that rate increases will begin in 4Q22 (1Q23 estimated in July).

Raw materials: copper will show some decline next year (higher supply), but will remain at attractive levels for mining investment

COMMODITIES: ANNUAL AVERAGE PRICE

(INDEX: 2015 AVERAGE = 100)



Key assumptions on the local front



COVID-19

Third wave of infections, although with a contained impact on activity. Then, at the beginning of 2022, with most of the population already vaccinated, capacities will start to normalize. A group of benefiting production sectors will be one of the drivers of growth in 2022.



Political context

Distrust and doubts about the quality of public policies. In this context, caution in private spending, especially investment spending, will drag down growth in 2022. Relative order at the macroeconomic level.



Economic policies

Monetary and fiscal policies will continue to support activity thereafter, but to a lesser extent.



Mining production

New copper mines start production and gradually reach full operational capacity.



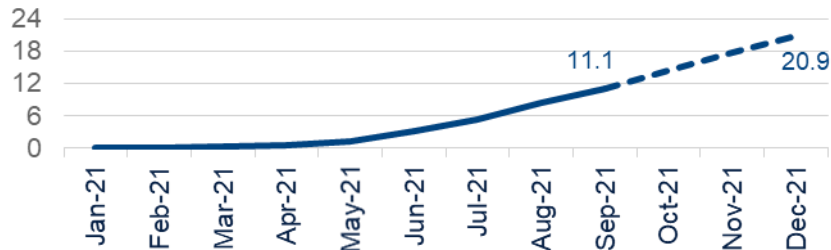
It is assumed that at the beginning of 2022, with most of the population already vaccinated, capacities will start to normalize

NUMBER OF VACCINES PURCHASED (MILLIONS OF DOSES)

Laboratory	
Sinopharm	24
Pfizer ¹	68.9
Covax Facility	15
AstraZeneca	13.8
Gamaleya	20
Moderna	20
Total	161.7

1: Includes 2 million doses donated by the US

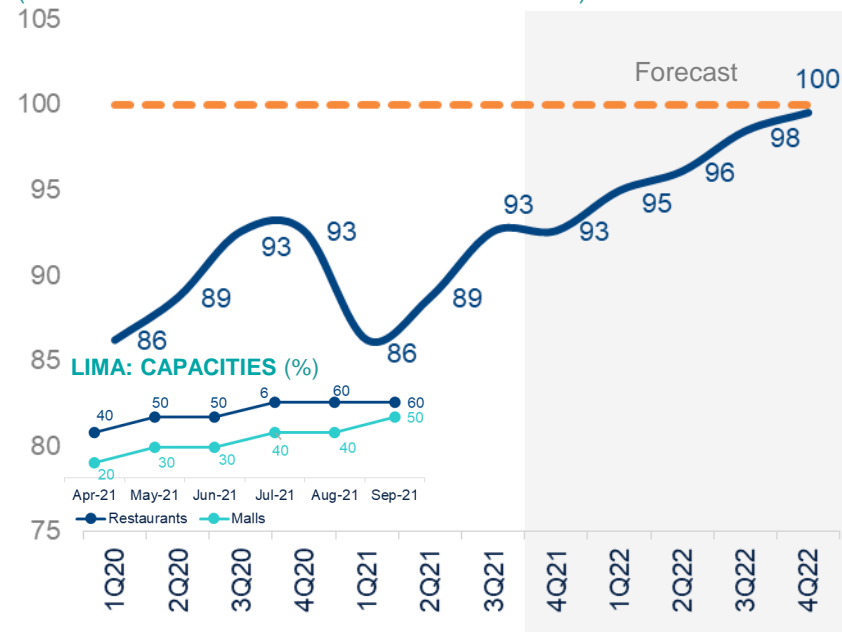
NUMBER OF VACCINATED PEOPLE* (MILLIONS OF PEOPLE)



* Considers two doses per person and official announcements of vaccine arrivals.
Source: Media and INEI. Preparation: BBVA Research.

INDEX COMPOSED OF ACTIVITIES MOST AFFECTED BY ISOLATION MEASURES*

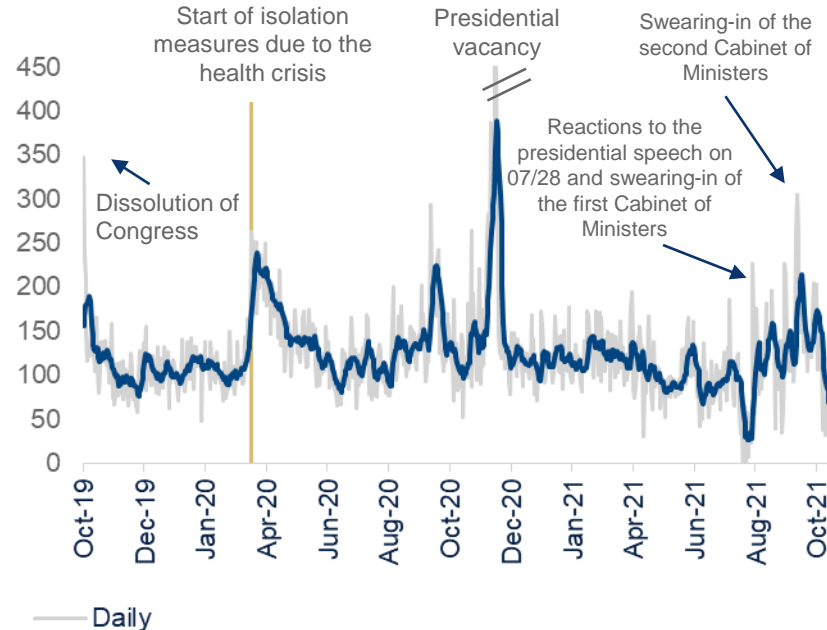
(LEVEL AS % OF THE SAME PERIOD IN 2019)



* Includes trade, accommodation and restaurants, transport, and business services, sectors that together account for 22% of GDP.

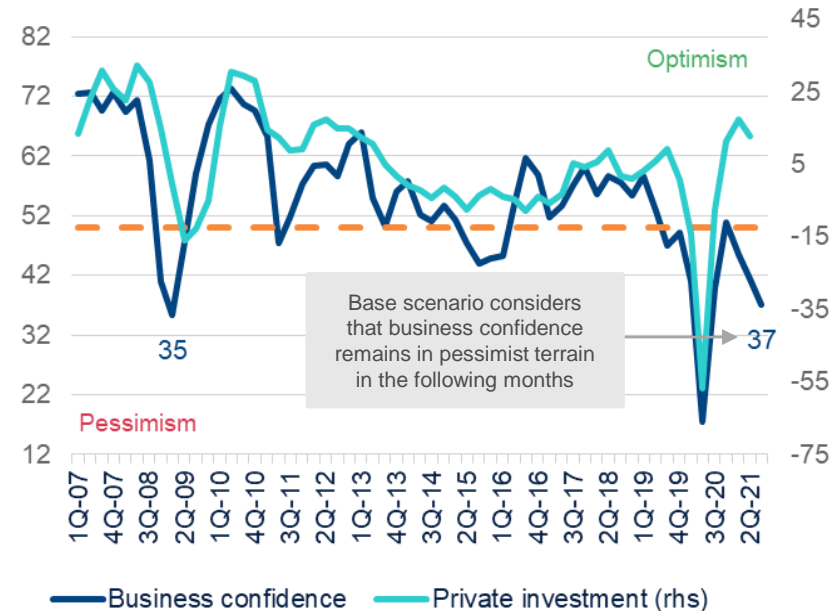
Uncertainty sustained by political tensions induces caution over private spending, particularly investment spending

POLITICAL TENSION INDICATOR¹ (FEB 2020 = 100, SEVEN DAY AVERAGE)



1: Information as at October 15.
Source: GDELT and Central Bank of Peru. Preparation: BBVA Research.

BUSINESS CONFIDENCE AND PRIVATE INVESTMENT¹ (POINTS AND YoY % CHANGE)

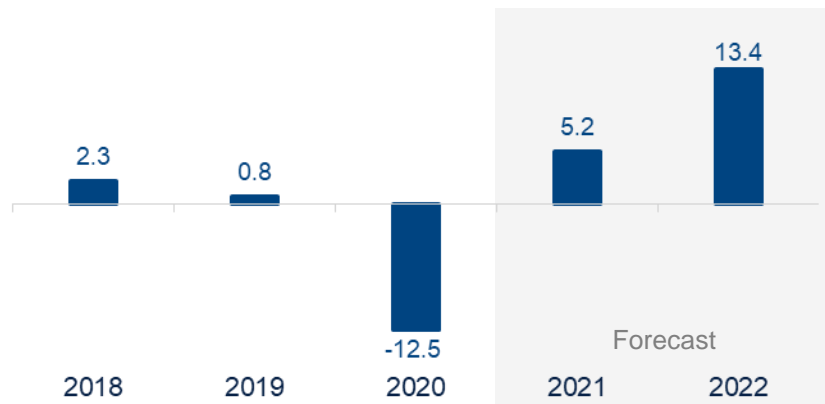


1: For 2021, the change in private investment has been considered in comparison with the same period in 2019.

The forecasting scenario assumes that new copper mines will start production and gradually reach full operational capacity

COPPER PRODUCTION

(YoY % CHANGE)



COPPER PRODUCTION

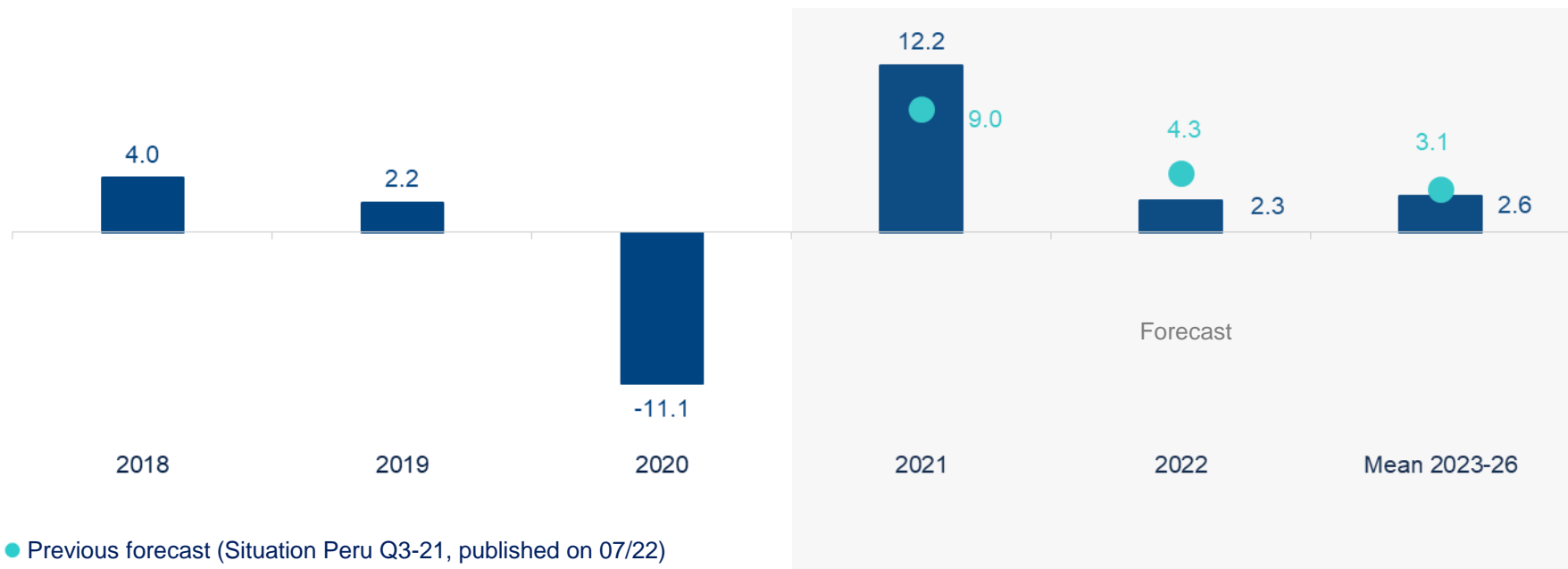
(MILLIONS OF MT)

2018	2019	2020	2021	2022
2.4	2.4	2.1	2.3	2.6

- The baseline scenario incorporates copper production of 2.3 million MT in 2021, which increases to 2.6 million MT in 2022 (13%).
- These figures assume that Mina Justa reaches full operational capacity soon and that Quellaveco enters production in the second half of 2022. It should be noted that the mines entering this stage, operating at full capacity, produce an amount equivalent to 20% of current copper extraction.
- It is also assumed that the copper production of some large mines will continue to be affected by social conflicts.

In this context, we expect GDP to grow by around 12.2% in 2021 and 2.3% next year

GDP
(YoY % CHANGE)



The growth forecast has thus been revised upward in 2021 and downward in 2022

Upward revision in
2021 growth



Better execution so far this year introduces an upward revision of two percentage points. The surprise upturn is concentrated in the third quarter (growth close to 10.0% year-on-year). While slowdown is expected in the latter part of the year, the fourth quarter begins with a higher level, implying a further point of growth for 2021.

In the third quarter, the political environment did not affect private spending as much as anticipated and the third wave did not materialize, which has allowed for increased capacity in shopping centers and restaurants, and also favored the movement of people. In addition, liquidity measures (withdrawal of funds from AFP and CTS) continue to support household expenditure.

Downward revision in
growth for 2022



Political environment. A scenario of higher political tensions is assumed compared to the previous forecast. Context of uncertainty affecting private spending decisions.

Less favorable external context. Growth forecasts for the main geographies are revised downward. Fed initiates the reduction of monetary stimulus sooner.

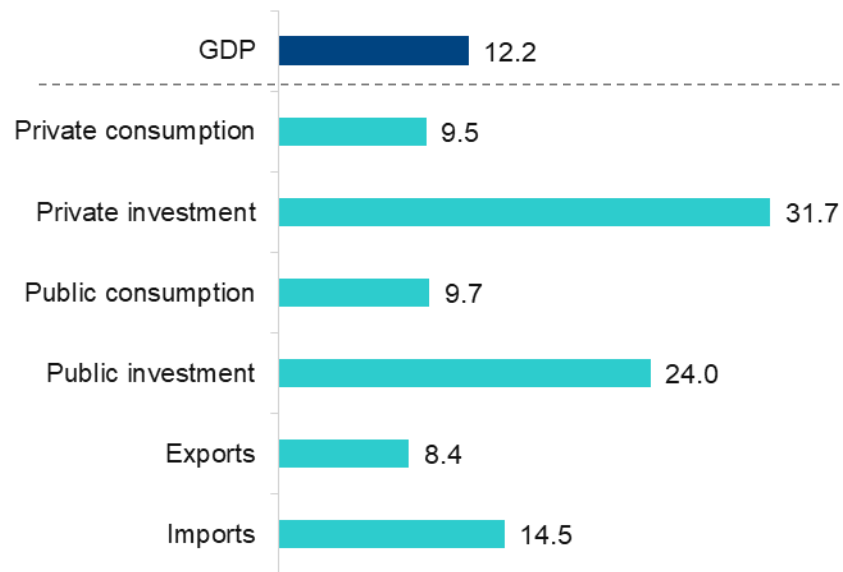
Less push for mining production due to social conflicts in some large mines.

Accelerated normalization of the monetary position. On the contrary, a somewhat slower withdrawal of fiscal support.

On the expenditure side, private investment rebounds sharply in 2021, but falls close to 10% next year due to caution regarding political noise

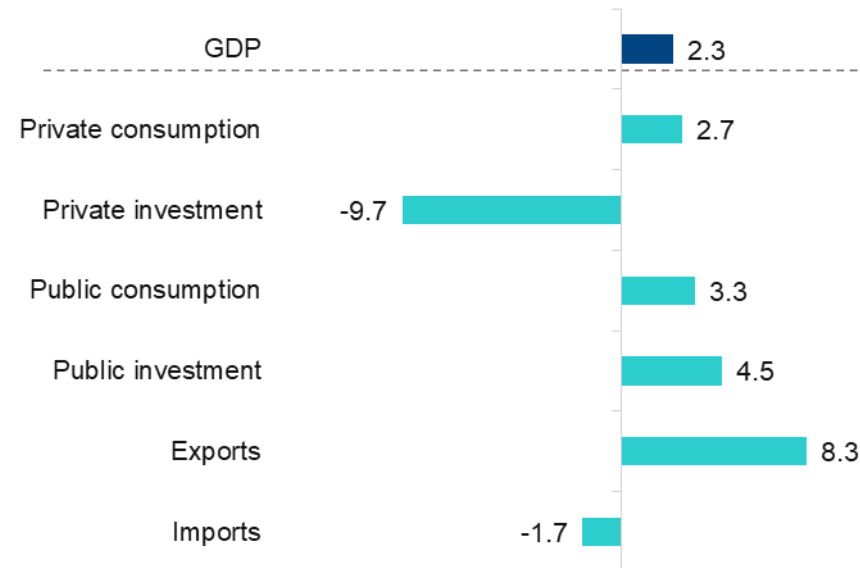
EXPENDITURE-SIDE GDP 2021

(YoY % CHANGE)



EXPENDITURE-SIDE GDP 2022

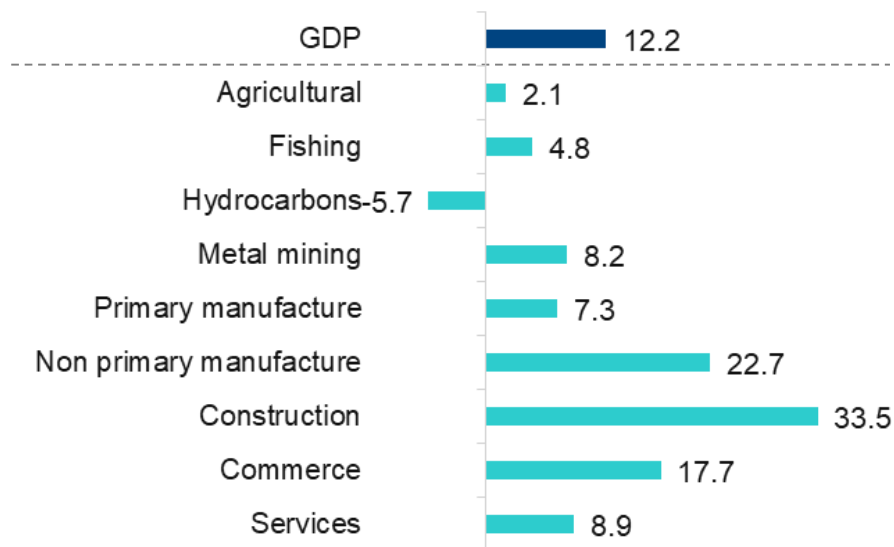
(YoY % CHANGE)



On the sectoral side, a boost in Construction and Non-primary Manufacturing in 2021, and recovery of Hydrocarbons and Metal Mining in 2022

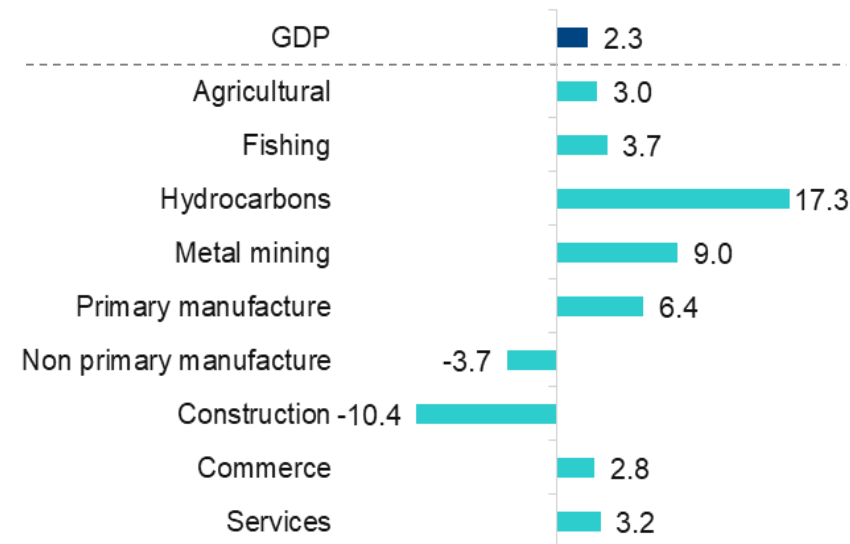
SECTORAL GDP IN 2021

(Y/Y % CHANGE)



SECTORAL GDP IN 2022

(Y/Y % CHANGE)



04

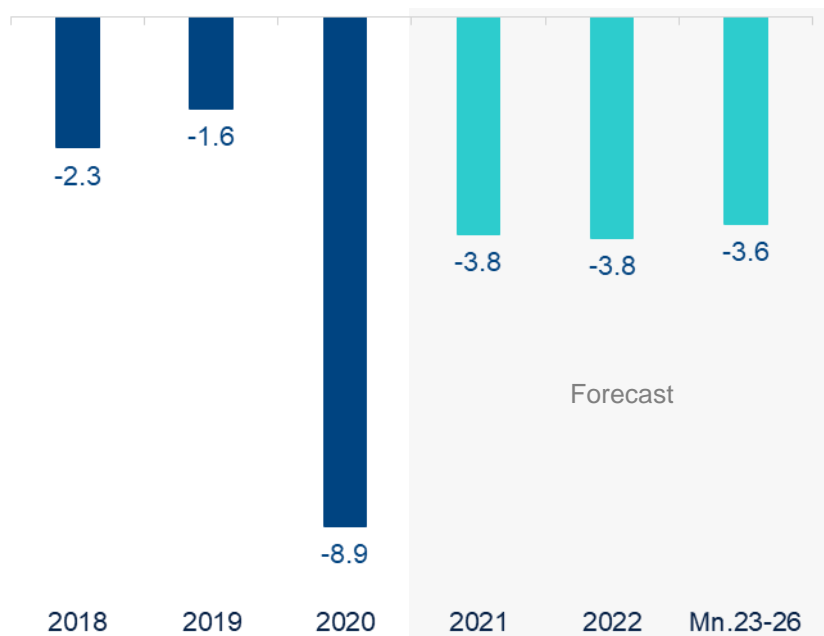
Quarterly review of macroeconomic forecasts

4.2. Fiscal result and public debt

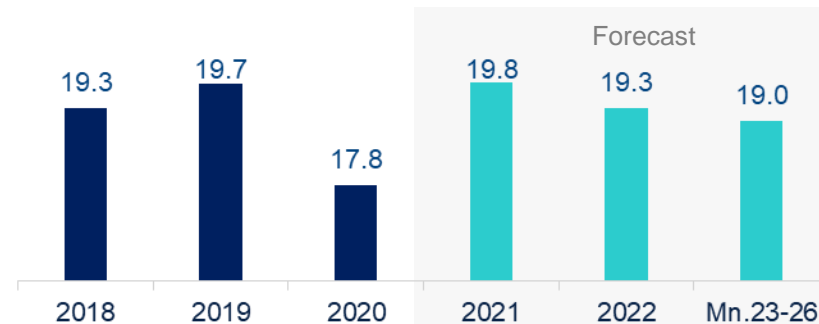
Fiscal scenario: a major decline in the government deficit for 2021, but adjustment will be much more gradual going forward

FISCAL BALANCE

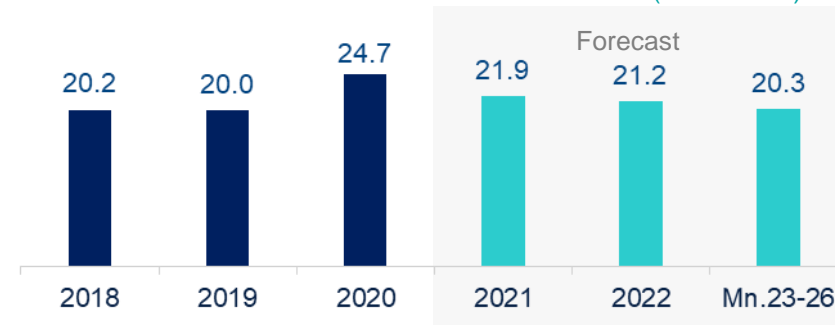
(NON-FINANCIAL PUBLIC SECTOR, % OF GDP)



CENTRAL GOVERNMENT REVENUE (% OF GDP)

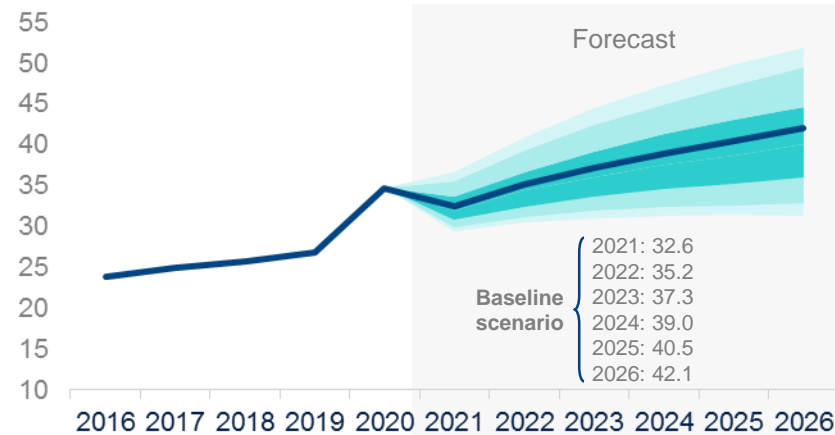


CENTRAL GOVERNMENT EXPENDITURE (% OF GDP)



... and will not be enough to stabilize the public debt ratio. Fiscal consolidation will require increased tax collection and more containment of public expenditure

GROSS PUBLIC DEBT FORECAST (% OF GDP)



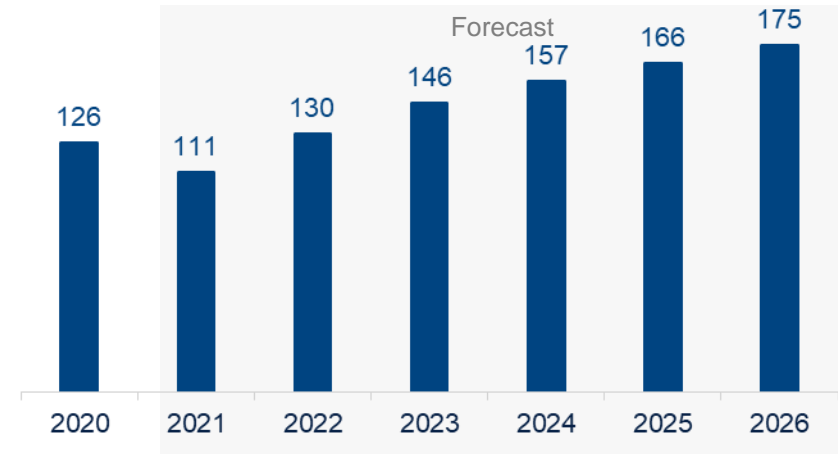
— Baseline scenario

Likelihood around the baseline scenario (percentage)

- 80% likelihood that debt will be between 32% and 53% by 2026
- 70% likelihood that debt will be between 33% and 50% by 2026
- 50% likelihood that debt will be between 37% and 45% by 2026

Source: BCRP. Forecast: BBVA Research.

NET PUBLIC DEBT AS A SHARE OF TAX REVENUES* (%)



Possible additional expenditure demands: Executive withdrew the application for unconstitutionality against the law on the administrative service contracts regime and collective bargaining in the public sector.

Political tensions between the factors that led to sovereign credit rating cuts

RISK RATING (AND OUTLOOK) FOR PUBLIC DEBT IN FOREIGN CURRENCY

	S&P	Moody's	Fitch
Peru	BBB+	Baa1	BBB
Chile	A	A1	A-
Colombia	BB+	Baa2	BB+
Mexico	BBB	Baa1	BBB-
Brazil	BB-	Ba2	BB-

Stable perspective  Negative perspective 
 Stable perspective with any downgrade between
 january and october of 2021 

SOVEREIGN CREDIT RATING DOWNGRADE

- A reduction in the sovereign credit rating will induce higher interest rates thereafter for the Peruvian government and for the economy in general.
- Moody's: cut from A3 to Baa1. Increased political risk and weakened capacity to implement economic policy.
- Fitch: cut from BBB+ to BBB. Political climate will affect growth.
- S&P: rating is maintained at BBB+, but outlook deteriorates from stable to negative. Fragmented political environment and difficult social legacy of the pandemic will affect growth and debt metrics.

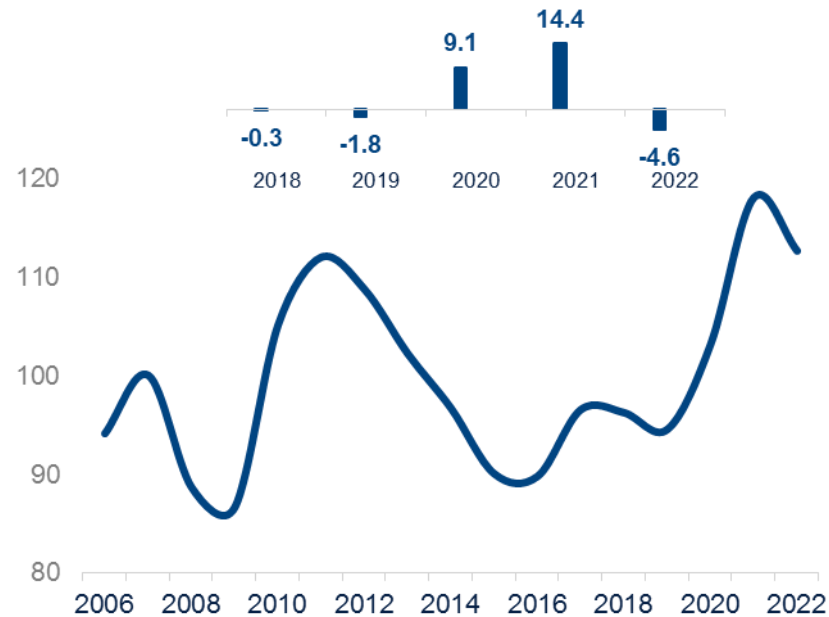
04

Quarterly review of macroeconomic forecasts

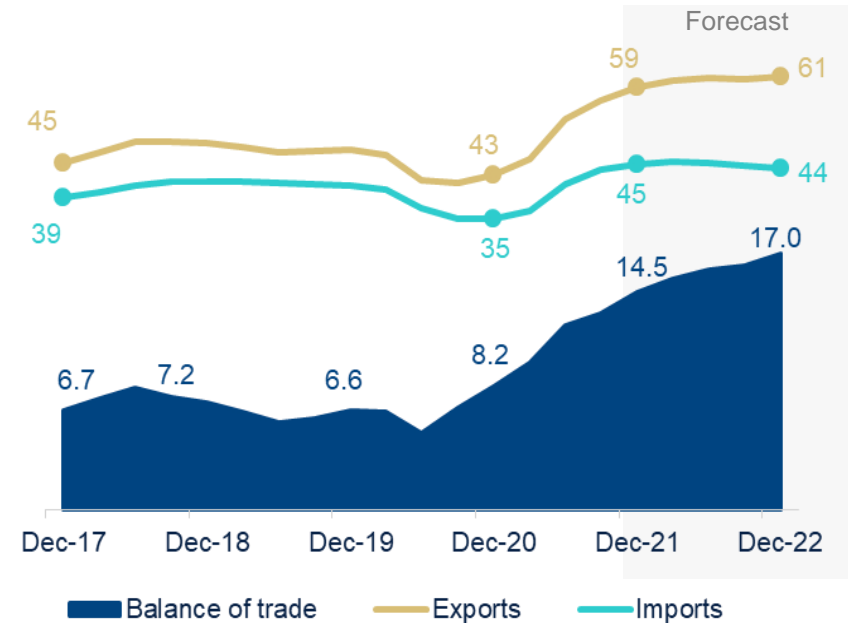
4.3. External sector and exchange rate

Significant trade surplus in 2021 and 2022 mainly due to higher metal prices

TERMS OF TRADE (LEVEL AND YoY % CHANGE)



TRADE BALANCE (USD BILLION, ACCUMULATED OVER THE LAST FOUR QUARTERS)



The exchange rate will end the year in a range from 4.0 to 4.1 PEN per USD

EXCHANGE RATE (PEN PER USD)



Source: Bloomberg. Forecast: BBVA Research.

- For the rest of this year, and during 2022, we anticipate that the exchange rate will continue to show episodes of volatility linked to the political scene and the start of the Fed's tapering. The weakening of the Peruvian currency induced by these two factors will be partly offset by the surplus in the trade balance, which will hit a record high in 2022.
- In this context, we estimate that the local USD price will close 2021 between 4.00 and 4.10 soles per USD, while in 2022 it will close between 4.15 and 4.25 soles per USD.
- It should be noted that our estimates suggest that the Peruvian currency is still undervalued (around 3.0%), meaning that an environment of greater political stability or significant improvement of macroeconomic fundamentals could be reflected in a strengthening of the Peruvian sol.

04

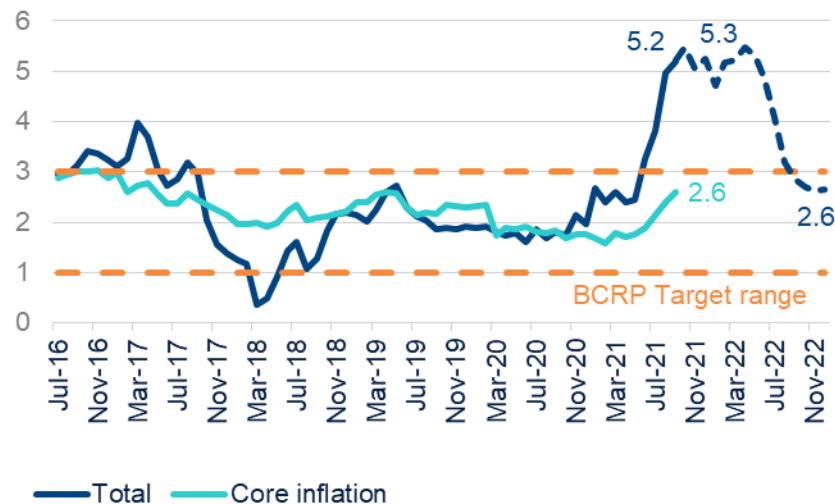
Quarterly review of macroeconomic forecasts

4.4. Inflation and monetary policy

Inflation will be temporarily above the target range, likely until mid-2022

INFLATION

(YoY % CHANGE IN CPI)



Source: BCRP. Forecast: BBVA Research.

DETERMINING FACTORS IN INFLATION FORECAST

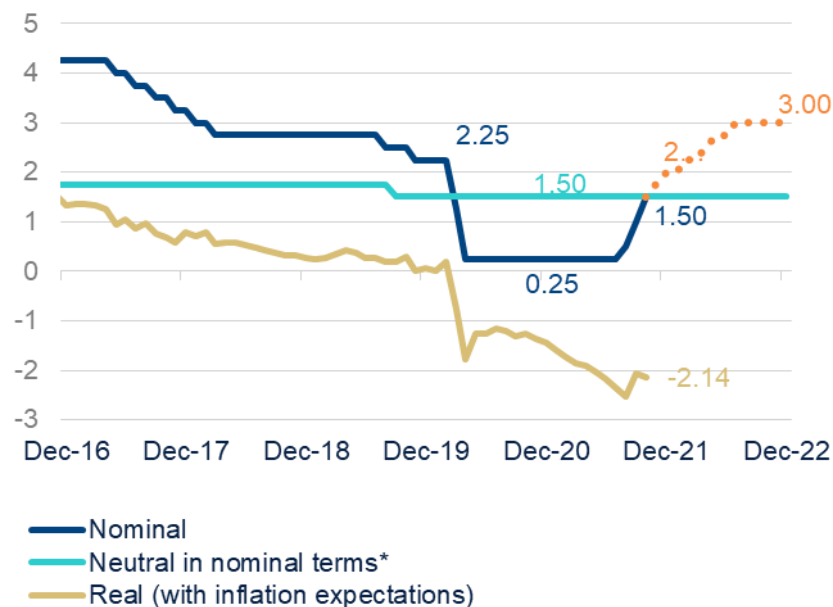
- The PEN year-on-year depreciation rate will stabilize in the remaining months of 2021 and ease in 2022.
- International food commodity prices will correct downward. Oil, gas and diesel will do the same later.
- Output gap still negative in 2021 and 2022, but closing.
- Reopening of sectors most affected by isolation measures will push some prices up.
- Inflation will close 2021 somewhat above 5%, but will fall back in 2022 (to 2.6%), more clearly in the second half of that year.

In the short term, inflation is higher than in the previous forecast. It will soon reach a peak, but will then remain outside the target range. It will only return to this range in the second half of 2022.

Monetary policy: faster normalization of the reference rate

REFERENCE INTEREST RATE

(%)






* The neutral rate was re-estimated in the September 2019 Inflation Report, from 1.75% to 1.50%. Own estimates point to a value of close to 1.25%, providing less in the way of monetary stimulus. Source: BCRP. Forecast: BBVA Research.

- The Central Bank has been responding to rising inflation and the unanchoring of inflation expectations (from 2.6% in June to 3.6% in September) with monetary policy rate adjustments (+50 pbs in each of the last two months). Positive surprise from the activity has created space.
- We expect the policy rate to reach a level of 2.0% by year-end and 3.0% by the end of 3Q22 (still expansionary given expected growth decline).

05

Main risks

Chief risks to forecasts

		RISKS	BIAS PLACED ON ACTIVITY
External		Slower growth Higher inflation	Stagflation? Negative
Health		Progress in the vaccination process New coronavirus variants	Positive Negative
Political		Increased political tensions Social conflicts	Negative

06

Summary of forecasts

Macroeconomic forecasts: summary

	2019	2020	2021 (f)	2022 (f)
GDP (YoY % change)	2.2	-11.0	12.2	2.3
Domestic demand (excluding inventories, YoY % change)	3.0	-8.7	14.0	0.4
Private spending (YoY % change)	3.3	-10.5	14.1	-0.3
Private consumption (YoY % change)	3.0	-8.7	9.5	2.7
Private investment (YoY % change)	4.5	-16.5	31.7	-9.7
Public spending (YoY % change)	1.1	0.8	13.1	3.6
Public consumption (YoY % change)	2.2	7.2	9.7	3.3
Public investment (YoY % change)	-1.5	-15.5	24.0	4.5
Exchange rate (vs. USD, eop)	3.36	3.60	4.00–4.10	4.15–4.25
Inflation (% Y/Y, eop)	1.9	2.0	5.3	2.6
Monetary policy interest rate (% eop)	2.25	0.25	2.00	3.00
Fiscal balance (% GDP)	-1.6	-8.9	-3.8	-3.8
Balance of payments: checking account (% GDP)	-0.9	0.8	-1.8	0.6
Exports (USD billion)	48.2	42.9	59.5	61.5
Imports (USD billion)	41.1	34.7	45.0	44.3

(f) Forecast. Forecast closing date: October 18, 2021.

Source: BBVA Research.

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Peru Economic Outlook

4Q21

Closing date: October 18