Peru economic outlook

1Q22

Updated to: January 21

Creating Opportunities

Key messages (I)

INTERNATIONAL CONTEXT

The global economy is currently in a phase in which growth is slowing down: although activity continues growing relatively robustly in the main geographies, the impetus has decreased, more than anticipated. Inflation, however, remains high, partly due to issues associated with the pandemic. Subsequently, the Fed has brought forward its plans to phase out its stimulus, which until now has had relatively limited impacts on financial markets.

Our baseline scenario for forecasts considers that global growth will continue to be relatively robust over the next two years, but lower than 2021 (6.1%) and likely to gradually taper off (4.4% in 2022 and 3.8% in 2023). Potential new waves of the coronavirus will have increasingly smaller impacts on activity due to the progress of vaccinations and the availability of better treatment. The bottlenecks in the global supply chains will ease over the next few quarters, especially during the second half of 2022, as global supply reacts and global demand eases. Inflation will remain high, particularly in the US, which will encourage central banks to react by reducing their stimulus (Fed in 2022: quick tapering, rate increases, reducing the balance sheet), thus controlling inflationary pressure - which will gradually decrease - and with a limited impact on financial volatility.

Key messages (II)

DOMESTIC CONTEXT

Domestically, activity has returned to its pre-healthcare crisis levels. There are, however, differences between sectors, some of which have not completely recovered because they continue to be affected by confinement measures (those that are most intensive in terms of physical contact) or because of social conflicts. With the growth figures for October and November and the indicators available for December, the GDP should have increased by between 2.5% and 3.0% year-on-year during the 4Q 2021, therefore, growth for the year should be around 13% (with the GDP exceeding its pre-pandemic level by around 1%).

Regarding employment, the trend is positive. Formal employment and payroll have recovered. However, as with activity, there are differences by sector and geographies (with Lima still lagging in the return to normality) and the number of underemployed workers is still high.

Entering 2022, the indicators for health deteriorated as a result of the third wave of coronavirus infections. However, the economic impact (more restrictive confinement measures) continues to be relatively moderate within a setting in which the vaccination program is progressing. However, the main activity indicators for the year indicate that this growth will lose its impetus. This is also something that occurred during the last few months of 2021 in a local context in which social conflicts were having an impact on mining activities; business confidence remained at low levels and the economic stimulus decreased.

Key messages (III)

BASELINE SCENARIO FOR FORECASTS AND PROJECTED GROWTH

Domestically, our baseline scenario considers that, in the health aspect, the third wave of infections at the beginning of 2022 will have a limited and passing impact on activity (confinement measures will not be as tough) due to the progress of the vaccination program. After this, capacity restrictions will once again tend to become normal.

Secondly, the baseline scenario incorporates a decreasing likelihood of an extreme (radical) political/economic scenario. The most radical proposals, in the most fundamental aspects, have not gained any significant headway. The risk remains, but less so. For example, the approval of a law and the pronouncement of the Electoral Board has reinforced that any constitutional reform must be approved by Congress before going to a potential referendum (this reduces the likelihood of a Constituent Assembly being formed). Support for the Executive has decreased. Subsequently, uncertainty and caution with regard to spending remains on the horizon for the foreseeable time, but gradually beginning to ease.

The baseline scenario also considers that new copper mines are entering their production phases (Quellaveco among them). However, there is a more sensitive negative impact of social conflicts in the sectors exploiting natural resources. Lastly, it is assumed that within a setting of inflationary pressures and in which the negative output gap is beginning to close, monetary stimulus will be removed in 2022.

Against this backdrop, we forecast that the Peruvian economy will grow 2.3% in 2022 and 3.0% in 2023.

Key messages (IV)

FISCAL

The fiscal deficit decreased significantly in 2021 from a level equivalent to 8.9% of GDP in 2020 to 2.6%, due to the high raw material prices, the rebound in activity, extraordinary tax debt payments, the moderation in spending (current, as a percentage of GDP), and better results of public companies.

The deficits forecast for the following years are not very different to those of 2021 because even though non-financial spending will taper off as the stimulus and fiscal support measures are phased out, the correction in raw material prices will also lead to revenue tapering off, whereas the interest expenditure will gradually increase. The forecast fiscal deficit over the coming years is consistent with a slightly upward trajectory in gross public debt, which we estimate will reach a level equivalent to around 40% of GDP heading into 2026 (26.8% in 2019 and 36.5% in 2021).

Key messages (V)

EXCHANGE RATES

In recent weeks, and despite the more hawkish tone shown by the Fed, domestic currency reversed the trend that it had shown during most of 2021 and rallied, supported by factors such as the progressive domestic recognition that it is less likely that there will be an extreme political/economic scenario (radical, with the formation of a Constituent Assembly), and the sustained increase in the domestic monetary policy rate, as well as a trade surplus that continues to be significant.

In 2022, we forecast that the PEN will weaken, but only to a limited extent: the Fed will withdraw its monetary stimulus, but domestically, the perception seems to continue to be that an extreme political/economic scenario is increasingly more unlikely, the Central Bank will continue increasing its policy rates, and the trade surplus will remain at high levels. Within this context, we estimate that the domestic exchange rate with the dollar will close the year at between 4.00 and 4.10 PEN/USD, whereas in 2023, when the Fed continues to phase out the monetary stimulus, it will trade at between 4.10 and 4.20 PEN/USD.

Key messages (VI)

INFLATION

Inflation rose significantly in 2021 (closing the year at 6.4%) due to the depreciation of the domestic currency and a sharp rise in the international trading prices of fuel and food.

We forecast that this will remain high over the coming months, at an average of around 6.5% during the first half of the year and will then tend to decrease as the weakening of the PEN in 2022 will be very restrained and the international trading prices of consumables will at least show some signs of a downward adjustment. However, it will not end the year within the target range of the Central Bank (3.4%), which will only happen in 2023 (2.3%).

MONETARY POLICY RATE

In light of the continuous deterioration of the inflationary panorama and the space that the recovery of economic activity provided, the Central Bank has been normalizing its monetary position. The policy rate reached 3.0% in January (0.25% in July).

This process will continue over the coming months, and we forecast that the benchmark rate will position itself at 4.50% during the second quarter, a level above what we estimate to be neutral, thus seeking to avoid an even greater persistence of inflation and despite the output gap continuing to be negative in 2022 (according to our estimates, in 2023 it will be much closer to having closed).

Key messages (VII)

RISKS

External: a much faster or disorderly monetary adjustment by the Fed (which generates turbulence in debt and emerging markets), a more significant slowdown in China than previously forecast, more significant or persistent bottlenecks in global supply chains than anticipated (due to the pandemic, energy transition, protectionism), social and geopolitical tension on several fronts.

Domestic: new coronavirus variants that are resistant to vaccines and treatment, the Executive managing to implement some of its more radical proposals, a shutdown of Congress or presidential vacancy, and a more sensitive negative impact stemming from social conflicts.

BBVA Research

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International context: activity and financial markets

Global environment: growth moderation, with high inflation and earlier withdrawal of monetary stimuli

More persistent pandemic

Longer lasting bottlenecks

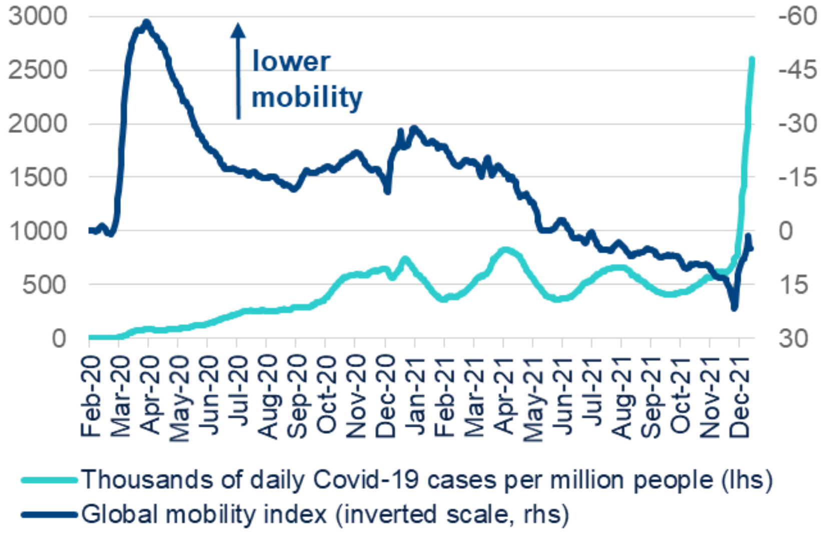
High inflation

Earlier withdrawal of stimuli

Slowdown in economic growth and higher financial volatility

The new variants of the coronavirus have increased infections, but with a limited negative effect due to vaccination

WORLD: DAILY CODIV-19 CASES AND MOBILITY RESTRAINT INDEX*
(7-DAY MOVING AVERAGE)

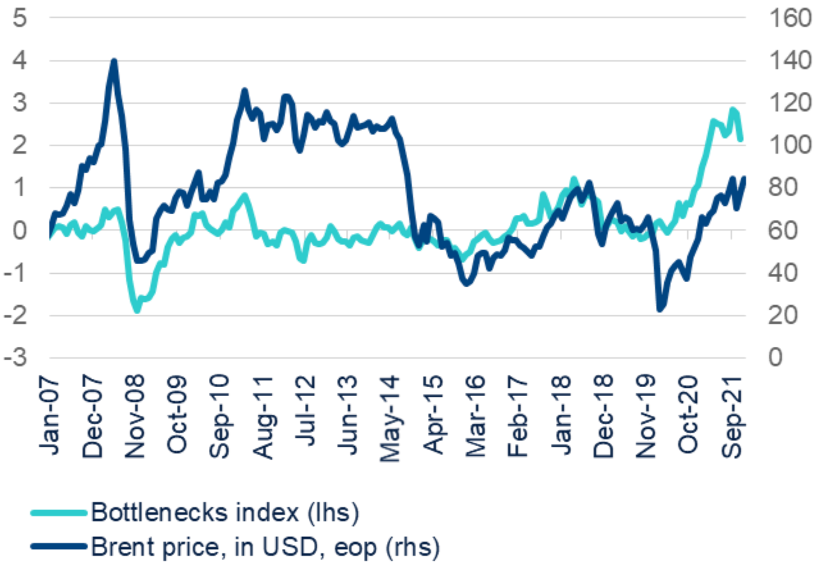


* The mobility index reflects changes with respect to the period of reference (January 3 to February 6 2020) based on retail and recreation mobility.
Source: BBVA Research based on data by John Hopkins University, Google and Our World in Data.

- New, highly contagious strains: coronavirus mutations in the context of incomplete vaccination.
- Strong increase in infections in Europe and more recently in the US and Latam.
- Limited impact on mobility, hospitalizations and mortality: widespread immunization in many countries.
- Increasing supply of vaccines and better treatments should allow greater control of the pandemic.
- Risk: new variants that evade vaccines.

Significant problems in global supply chains remain in place, but they could have peaked

SUPPLY BOTTLENECK INDEX (US) AND BRENT PRICE
(INDEX: 1998-2021 AVERAGE=0; BRENT PRICES:: IN USD)

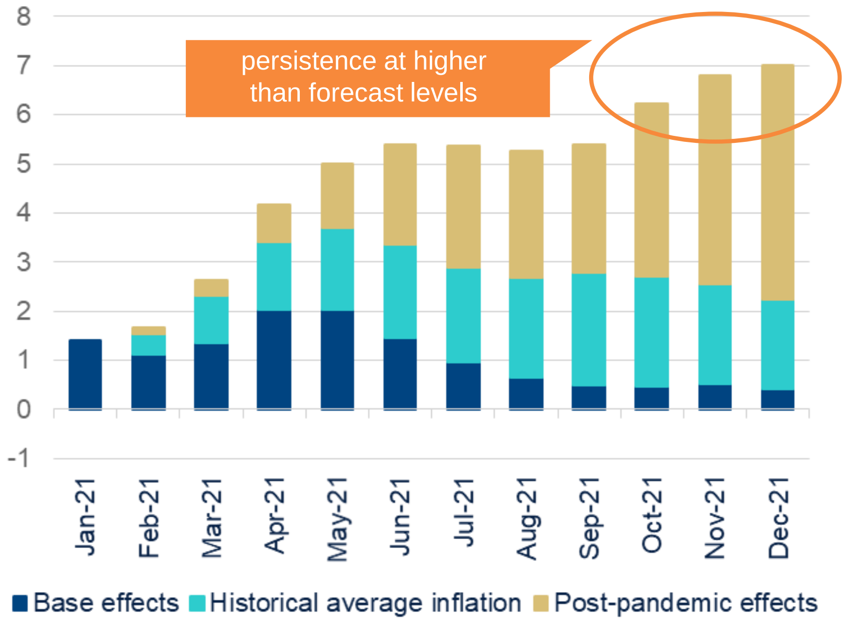


Source: BBVA Research based on data by Bloomberg.

- Production bottlenecks reflect an imbalance between a relatively robust demand and a relatively inelastic supply of goods.
- The problems are largely related to the pandemic, which means that they could be reinforced by the omicron strain.
- Energy transition policies, protectionism and geopolitical problems add complexity and put pressure on energy prices, which remain high despite the moderation in gas prices.
- Anyway, there are recent signs of moderation in bottlenecks, at least in manufacturing.

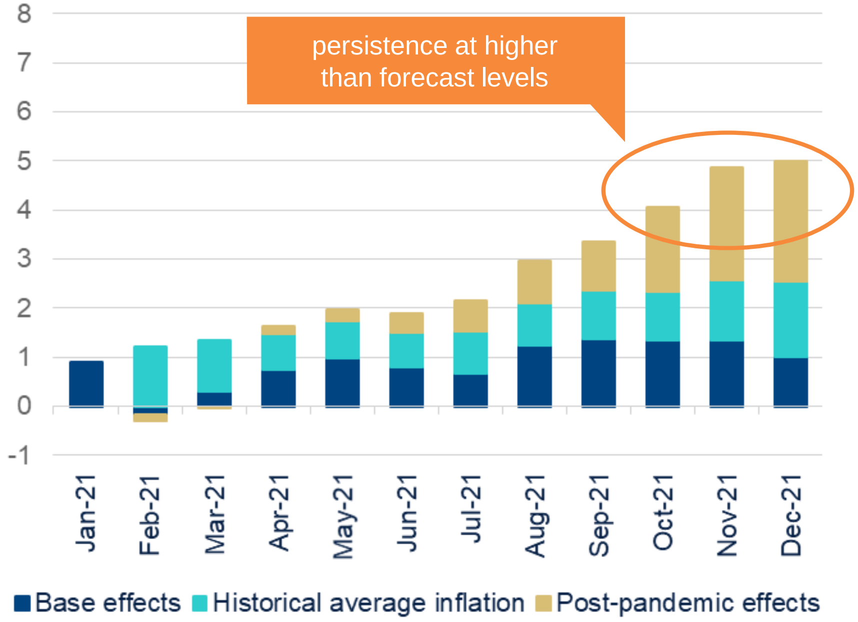
Inflation remains high, largely on pandemic-related issues (confinements, reopening, consumption composition, spending of accumulated savings...)

US : INFLATION
(CPI; Y/Y %)



Source: BBVA Research.

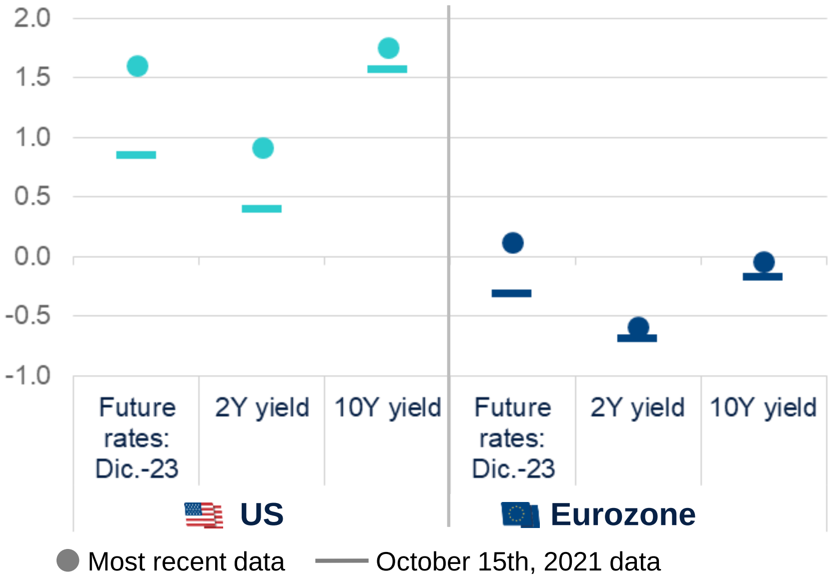
EUROZONE: INFLATION
(CPI; Y/Y %)



Source: BBVA Research.

Inflation has forced the Fed to bring forward its plans to withdraw stimulus and has caused a moderate adjustment in financial markets

POLICY RATES: MARKET EXPECTATIONS; SOVEREIGN BOND YIELDS *
(%)



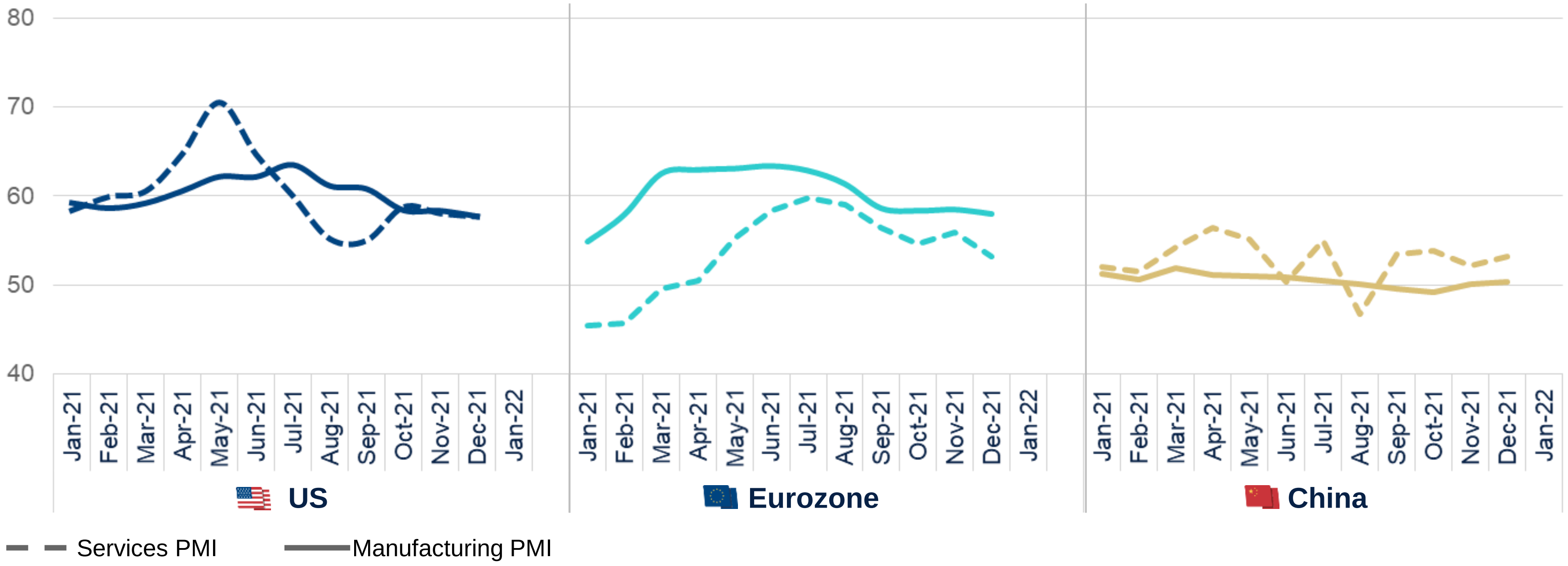
*: Market expectations for policy rates in Dec/23 implicit in future contracts. Eurozone yields: German bond yields. .
Source: BBVA Research based on data by Bloomberg.

- The Fed has started a more aggressive tapering and suggested that it will raise policy rates earlier and faster than expected.
- In the Eurozone, markets now discount earlier interest rate hikes, but the change in expectation has not been as sharp as in the US.
- The US 2-year yield has increased significantly, in contrast with the smaller increase of the 10-year yield; in Europe yields remain low.
- The Fed's shift towards a more rapid withdrawal of stimulus has caused a moderate rebound in volatility and in the US dollar.

Activity continues to expand in the main regions, but is slowing down more than expected

PMI

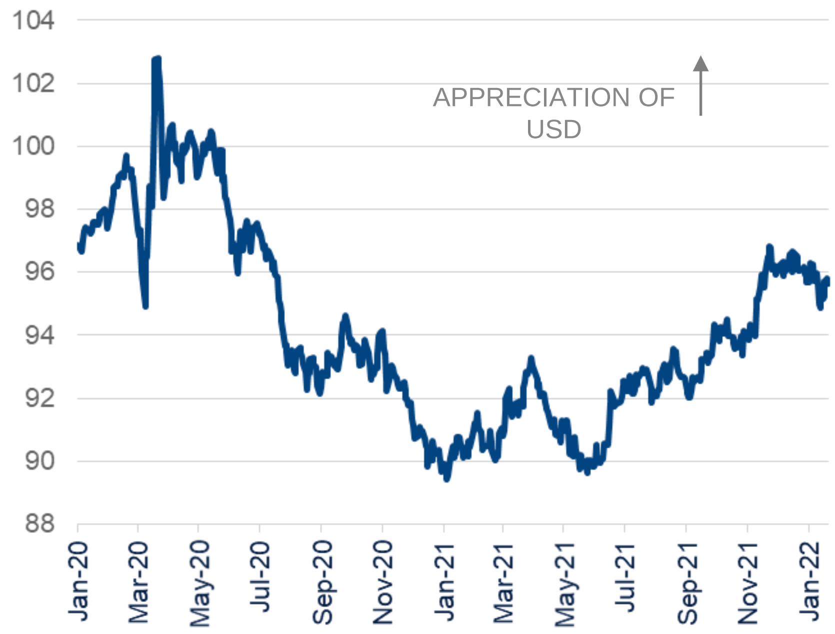
(HIGHER THAN 50: EXPANSION; LOWER THAN 50: CONTRACTION)



Source: BBVA Research based on data by Haver..

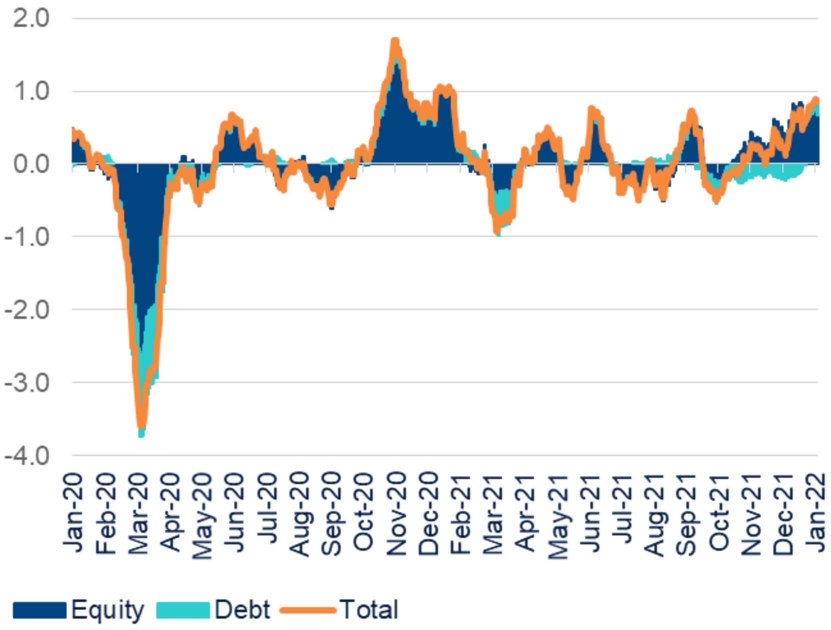
In spite of the more hawkish tone of the Fed, the dollar has weakened globally, and capital flows have returned to emerging economies…

DXY
(CONTENTS)



Source: BBVA Research, information from Bloomberg.

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

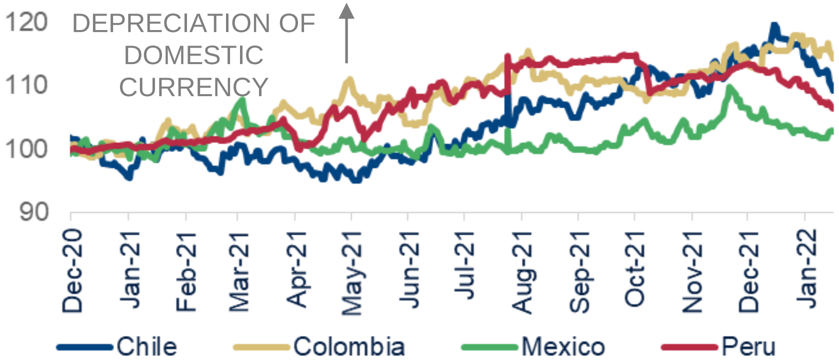


Source: BBVA Research, information from Bloomberg and the IIF.

… and currencies appreciate throughout the region, but risk premiums and returns on sovereign bonds increase

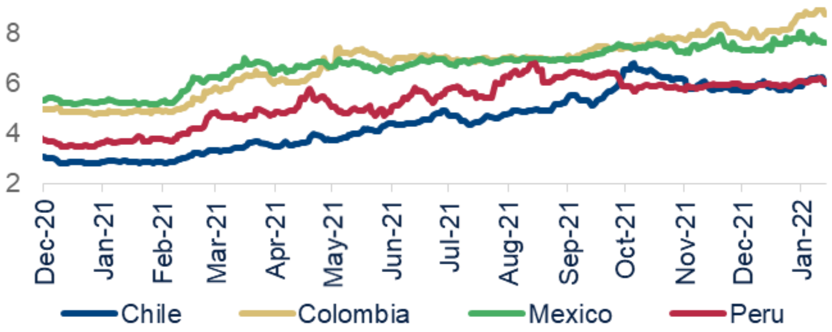
LATAM: DOMESTIC CURRENCIES VS USD

(INDEX, AVERAGE DECEMBER 2020 = 100)



LATAM: RETURNS ON 10-YEAR SOVEREIGN BOND

(%)



LATAM: DOMESTIC CURRENCIES VS USD

Change %	Peru	Chile	Colombia	Mexico
2021 year-end vs 2020 year-end	10.6%	19.7%	19.0%	3.1%
Current vs 2021 year-end (21/01/2022) (31/12/2021)	-4.2%	-6.3%	-3.1%	-0.3%

LATAM: CHANGE IN RETURNS ON 10-YEAR SOVEREIGN BOND

Bp	Colombia	Chile	Peru	Mexico
2021 year-end vs 2020 year-end	330	295	240	231
Current vs 2021 year-end (21/01/2022) (31/12/2021)	64	20	14	9

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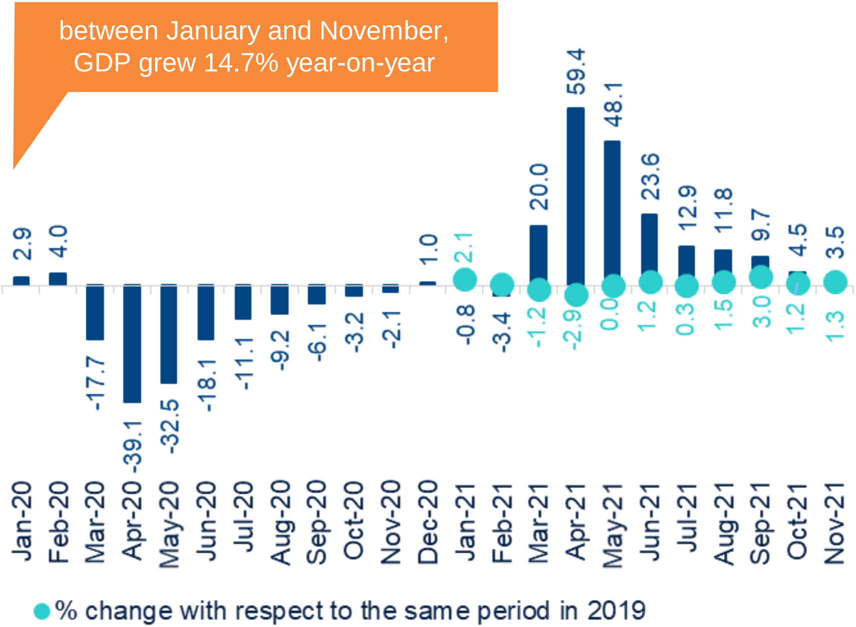
02

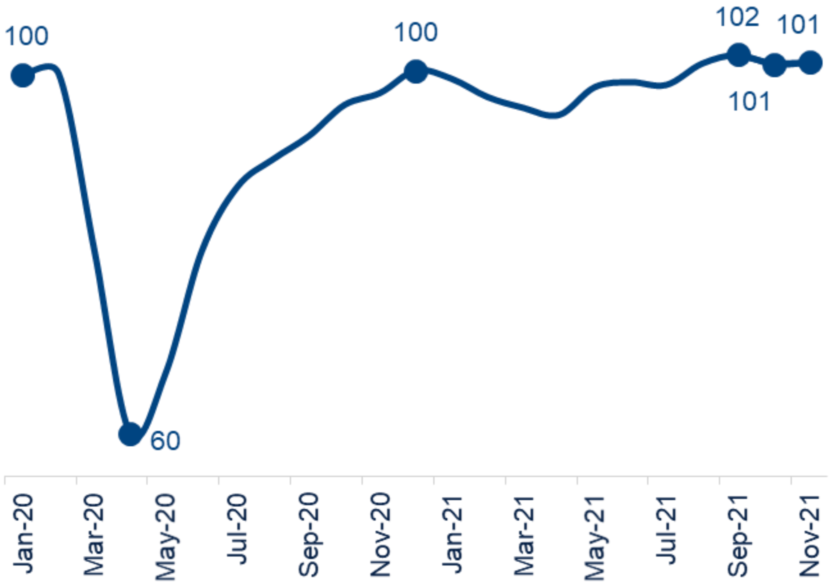
Domestic context: activity, employment and financial markets

Activity has returned to its pre-pandemic levels...

GDP
(% CHANGE YOY)



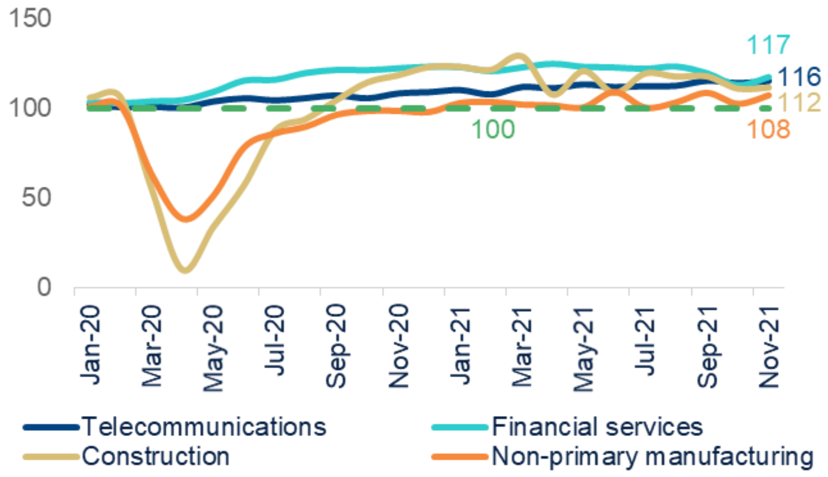
GDP
(NON-SEASONAL LEVEL, INDEX, FEBRUARY 2020 = 100)



Source: BBVA Research, information from INEI and BCRP.

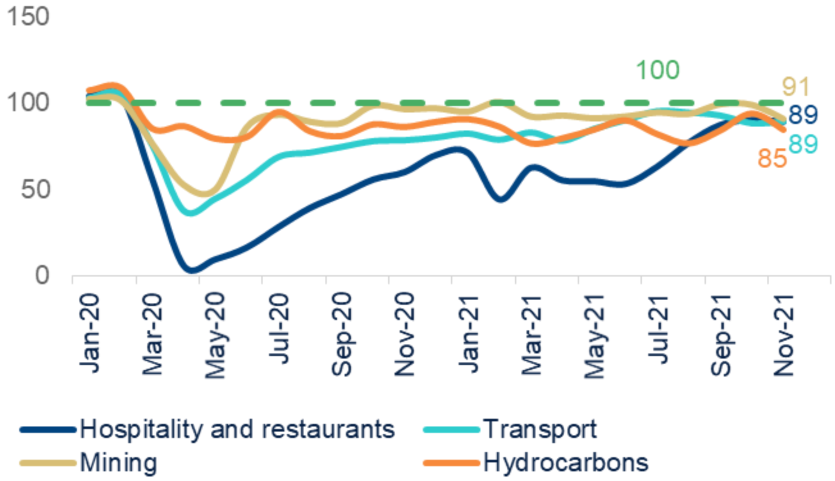
… but at the sectoral level the return to normality continues to be disparate

GDP BY SECTOR: SELECTED ACTIVITIES
(INDEX, 100 = LEVEL DURING THE SAME PERIOD IN 2019)



Sectors such as telecommunications services benefited from the situation. Others were favored by the monetary and fiscal stimulus and the measures supporting families and businesses.

GDP BY SECTOR: SELECTED ACTIVITIES
(INDEX, 100 = LEVEL DURING THE SAME PERIOD IN 2019)



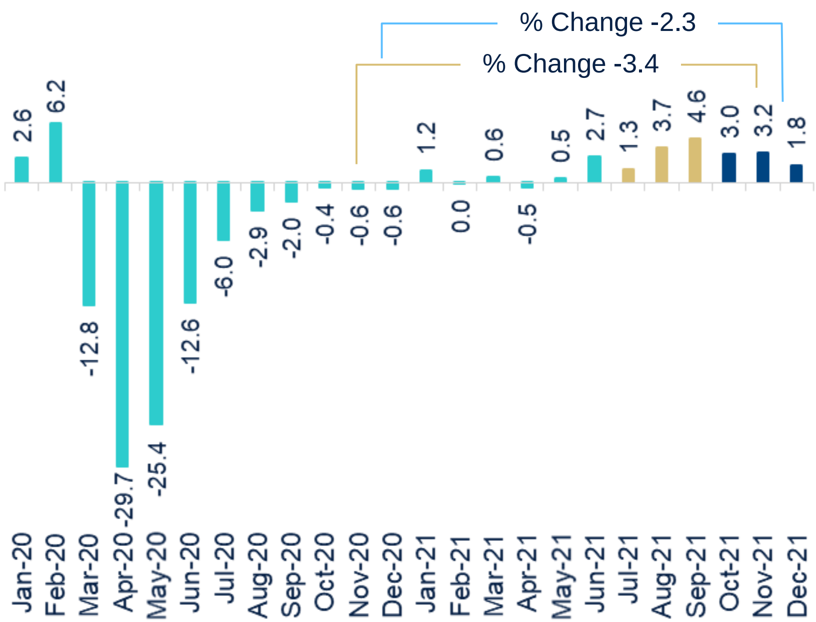
Confinement measures continue to affect the activity of sectors that are more physical contact intensive (services such as accommodation, restaurants, transport), which impedes them from returning to normality. Social conflicts affect others.

Source: BBVA Research, information from INEI and BCRP.

The indicators available for December indicate that, on balance, GDP is losing steam

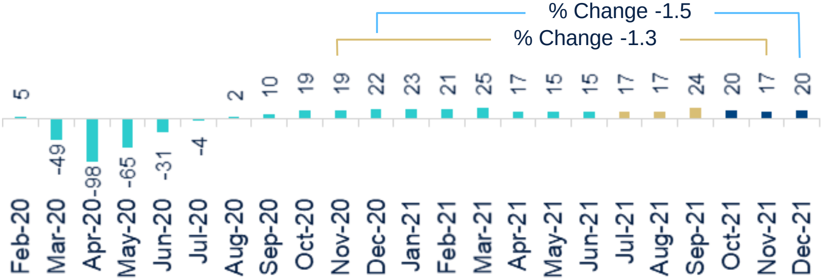
ELECTRICITY PRODUCTION

(% CHANGE COMPARED TO THE SAME PERIOD OF 2019)



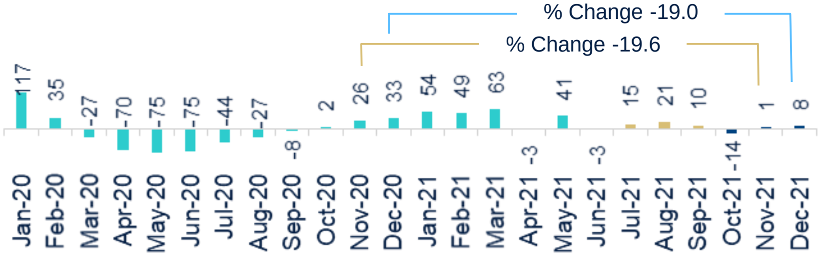
DOMESTIC CEMENT CONSUMPTION

(% CHANGE COMPARED TO THE SAME PERIOD OF 2019)



PUBLIC INVESTMENT

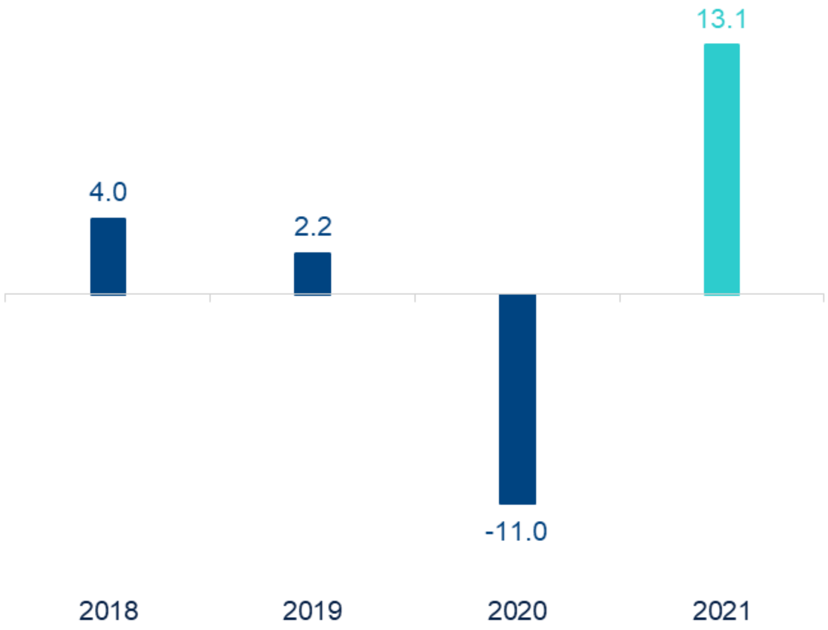
(% CHANGE COMPARED TO THE SAME PERIOD OF 2019)



Source: BBVA Research, information from COES and BCRP.

We estimate that activity grew 13.1% in 2021, a strong expansion that…

GDP
(% CHANGE YOY)



Source: BBVA Research, information from BCRP.

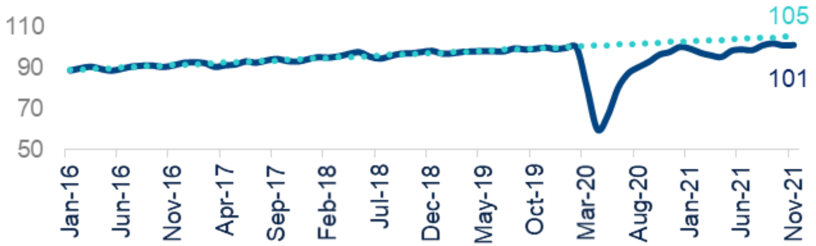
The strong growth in activity in 2021 includes:

- A natural rebound due to the low base for a year-on-year comparison: the confinement measures to contain the spread of the coronavirus were less restrictive this year.
- A favorable international setting: low interest rates, plenty of liquidity, strong rebound in global activity and, increased terms of trade.
- Domestically, the economic stimulus (fiscal and monetary), measures that increase liquidity of families (release of AFP and CTS, Government bonds), and the good progress of the vaccination process.
- All of the above more than compensated for the uncertainty generated by the electoral process and subsequent change of Government.

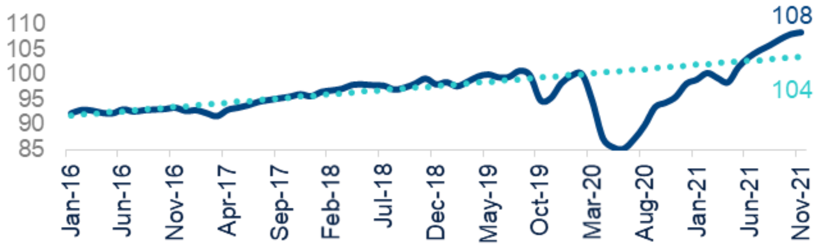
… however, does not manage to return it to the pre-pandemic crisis trend

GDP
(NON-SEASONAL LEVEL, INDEX FEB.20 = 100; AND TREND[1/])

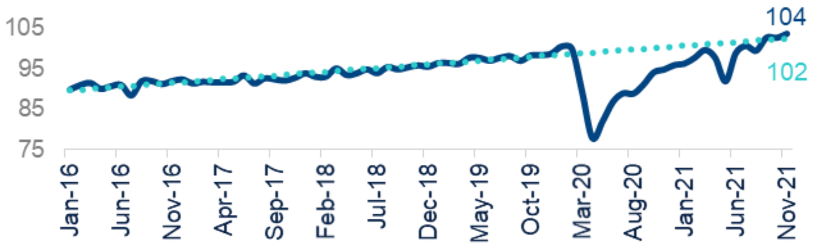
PERU



CHILE



COLOMBIA



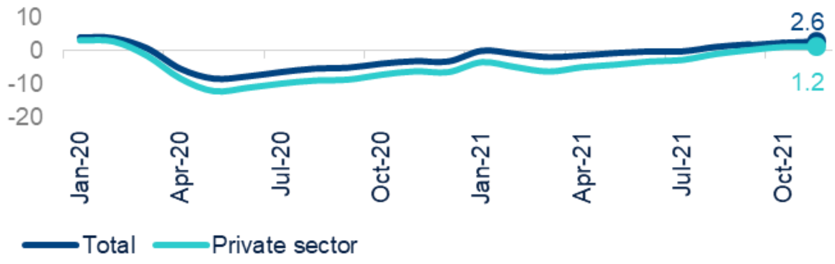
	Underlying CPI (% CHANGE YOY) Dec.21	Current account deficit (% of GDP, accumulated for 4 quarters) 3Q21
Peru	3.2%	1.2%
Chile	6.4%	3.5%
Colombia	4.4%	5.1%

1: The lineal trend is calculated for the period 2016-2019 (pre-healthcare crisis).
Source: BBVA Research, information from BCRP and official statistics of other countries.

In terms of employment, the trend remains positive… although different behavior has been registered at sector and geographic level

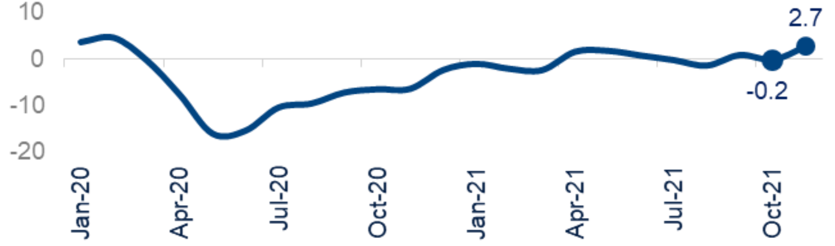
FORMAL EMPLOYMENT (ELECTRONIC PAYROLL)

(% CHANGE COMPARED TO SIMILAR PERIOD IN 2019)



FORMAL EMPLOYMENT PAYROLL

(ADJUSTED FOR INFLATION, % CHANGE COMPARED TO THE SAME PERIOD OF 2019)



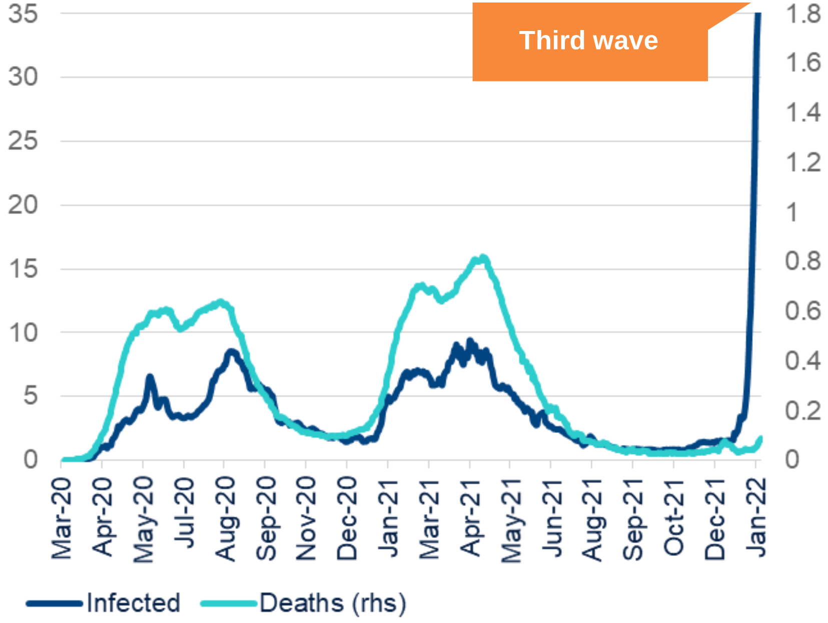
Source: BBVA Research, information from BCRP.

- Formal employment recovered in 2021, as did the payroll, in line with the return to normality of economic activity.
- But, there are differences in the recovery…
  - … at sector level: formal employment in sectors such as livestock farming and construction exceeded pre-healthcare crisis levels, whereas others such as services have been left behind.
  - ... by geographic area: in the northern regions, where there is a concentration of livestock export activity, the return to normality of formal employment proceeded faster than in those where services are more important (Lima).
- The national EAP (economically active population) had yet to exceed the pre-pandemic levels at the end of 3Q21; the employment rate has not recovered.
- The number of underemployed workers remained high at the end of 2021, exceeding pre-pandemic levels. Main characteristics of underemployed workers: they receive a salary that is below the minimum benchmark.

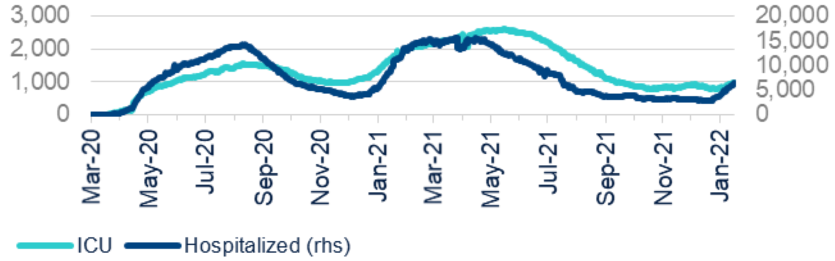
At the beginning of 2022, the health indicators deteriorated within the context of the third wave: infections and hospital admissions increased

NEW INFECTIONS AND DEATHS DUE TO COVID-19

(THOUSANDS OF PEOPLE PER DAY, SEVEN-DAY MOVING AVERAGE)



NO. OF COVID-19 HOSPITALIZATIONS



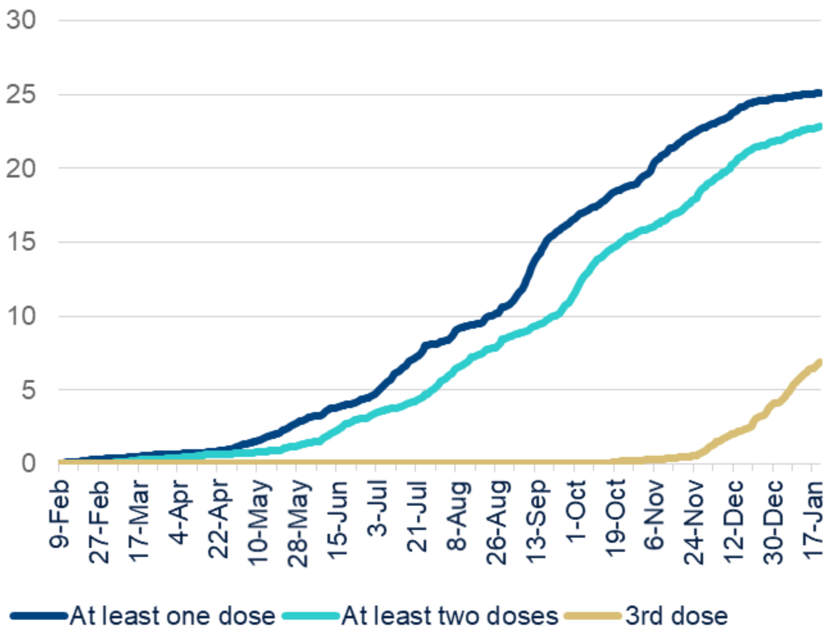
DAILY TESTS WITH A POSITIVE RESULT

(% OF THE TOTAL, SEVEN-DAY MOVING AVERAGE)

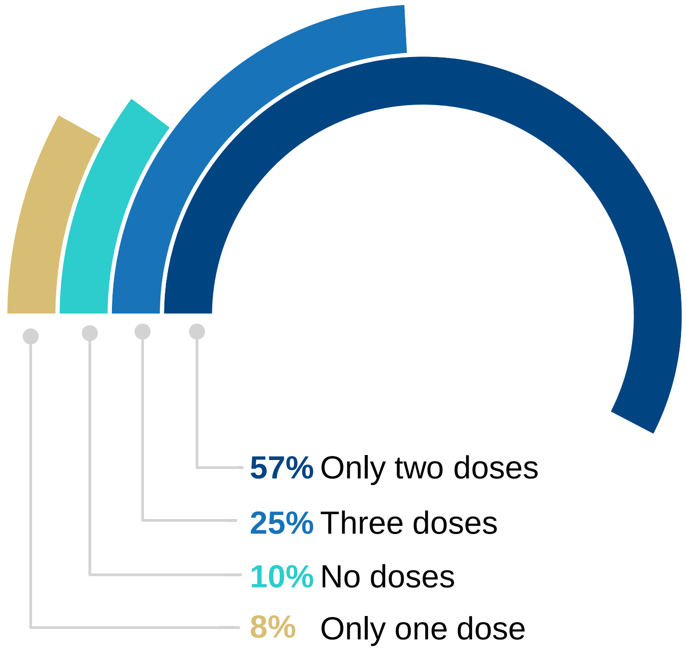
Source: BBVA Research, information from Ministry of Health of Peru.

Meanwhile, the vaccination program continues, which moderates the sanitary (ICU hospitalizations, deaths) and economic impact of this third wave

PROGRESS OF THE VACCINATION PROCESS
(MILLIONS OF PEOPLE)



PROGRESS OF THE VACCINATION PROCESS[1]
(% OF THE TARGET POPULATION)

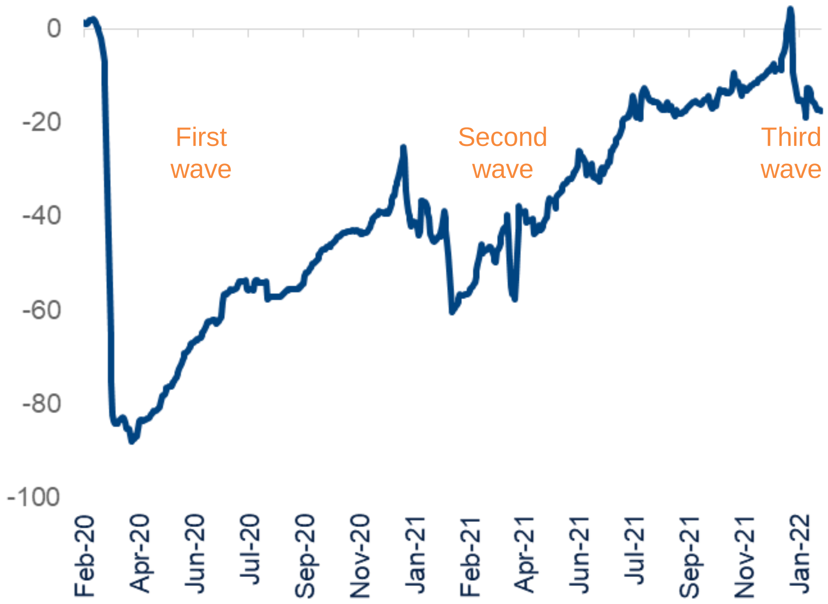


1: The target population is 28.2 million. Taking into account people aged 12 and over.
Source: BBVA Research, information from the Ministry of Health of Peru.

Meanwhile, the vaccination program continues, which moderates the sanitary (ICU hospitalizations, deaths) and economic impact of this third wave

MOBILITY OF PEOPLE TRANSPORT STATIONS

(INDEX, 0 = PRE-PANDEMIC)



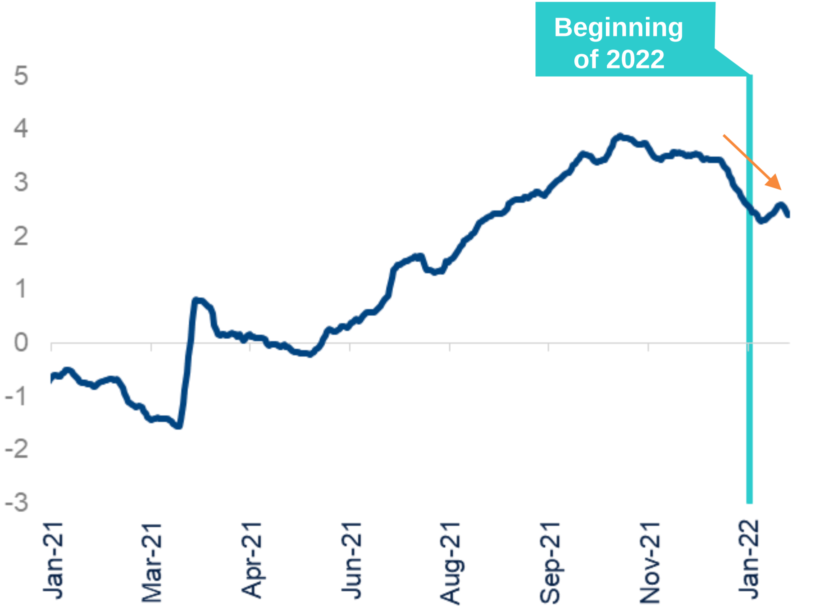
1: Information as at 21 January.
Source: Google Mobility.

- The third wave has led to some areas of the country, including Lima, to implement tougher confinement measures:
  - Reduced maximum occupancy in different businesses
  - Extension of curfew times
- At least for the moment, these measures are less restrictive than those implemented during the first two waves of infections.

Main activity indicators for 2022? In general, they continue to indicate a loss of momentum…

ELECTRICITY PRODUCTION

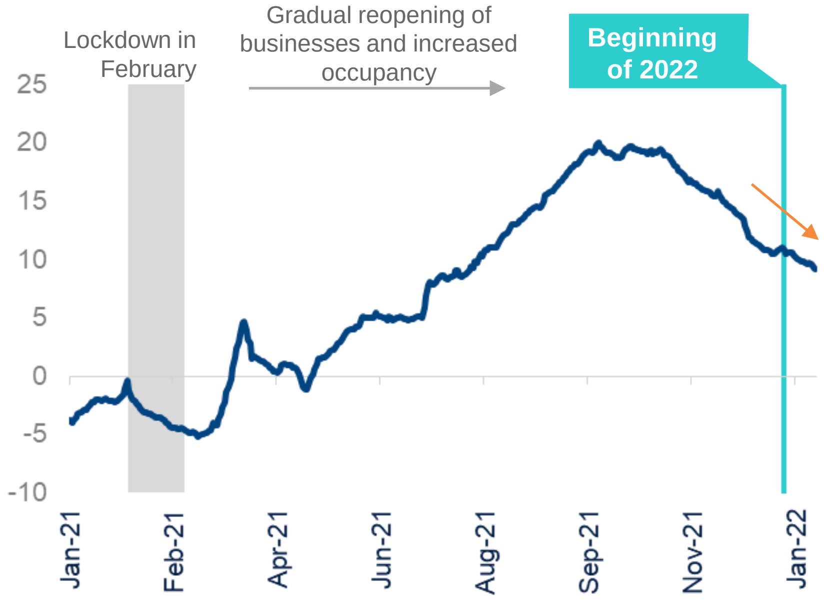
(THREE-MONTH MOVING AVERAGE, % CHANGE COMPARED TO THE SAME PERIOD PRE-PANDEMIC[1/])



1: The figures for 2021 are compared with those of the same period in 2019 and those for January 2022 with the same period in 2020.
Source: BBVA Research, with information from COES.

BBVA BIG DATA INDEX ON CONSUMPTION[1/]

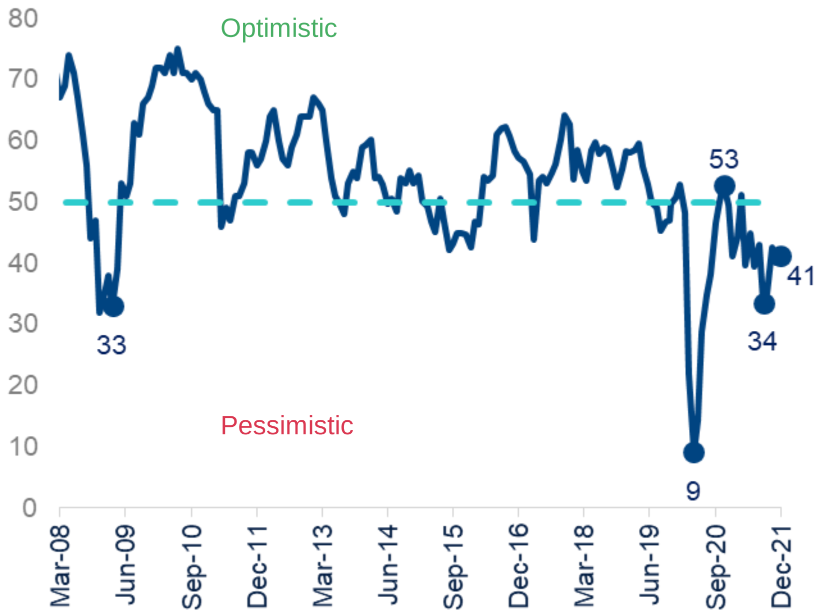
(IN REAL TERMS, THREE-MONTH MOVING AVERAGE, % CHANGE COMPARED TO THE SAME PERIOD PRE-PANDEMIC[2/])



1: Information from payments into the accounts of selected companies used.
2: The figures for 2021 are compared with those of the same period in 2019 and those for January 2022 with the same period in 2020.
Source: BBVA Research, with information from BBVA.

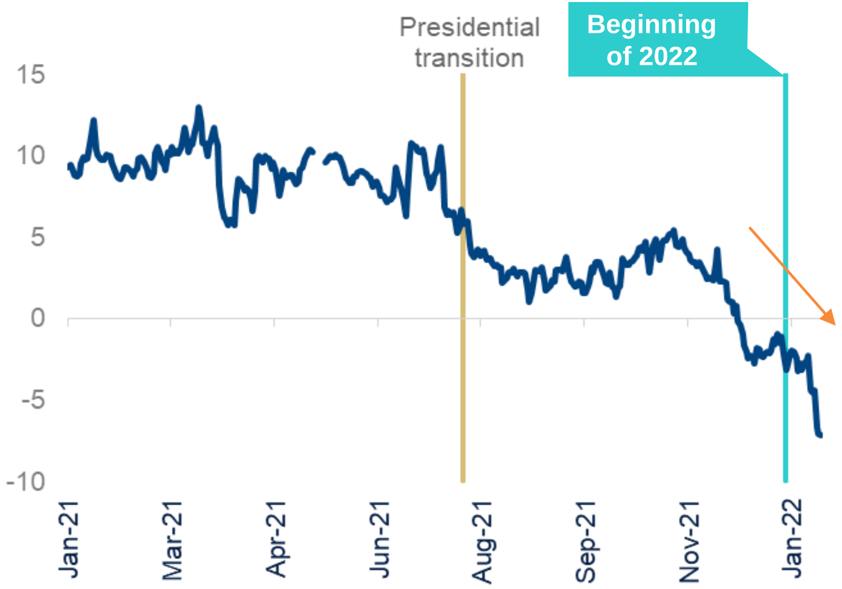
… in an environment in which business confidence remains at the pessimistic zone

BUSINESS CONFIDENCE
(POINTS)



Source: BBVA Research, information from BCRP.

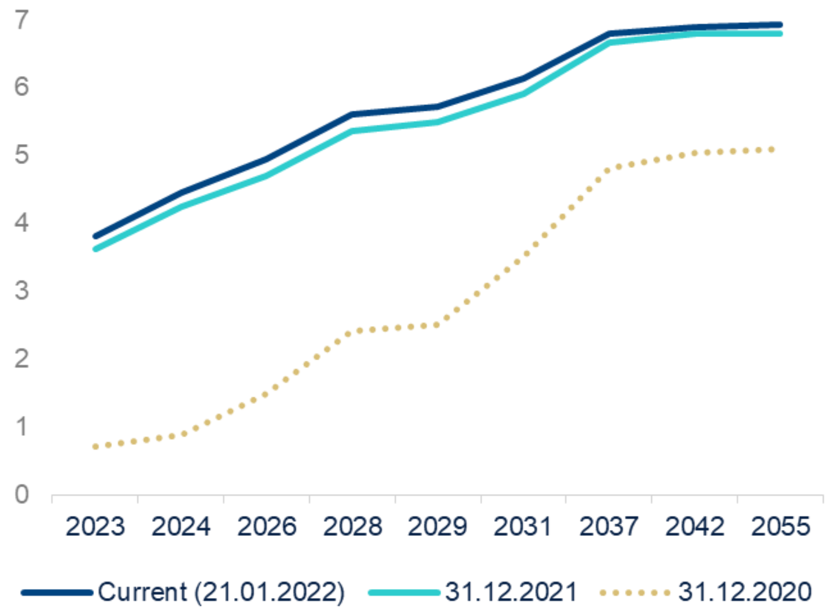
BBVA BIG DATA INDEX ON CONSUMPTION[1/]
(IN REAL TERMS, THREE-MONTH MOVING AVERAGE, % CHANGE COMPARED TO THE SAME PERIOD PRE-PANDEMIC[2/])



1: Information from payments into the accounts of selected companies used.
2: The figures for 2021 are compared with those of the same period in 2019 and those for January 2022 with the same period in 2020.
Source: BBVA Research, with information from BBVA.

In the domestic financial markets, the returns of sovereign bonds continue rising within a context in which the Fed appears hawkish

SOVEREIGN BOND YIELD CURVE (%)



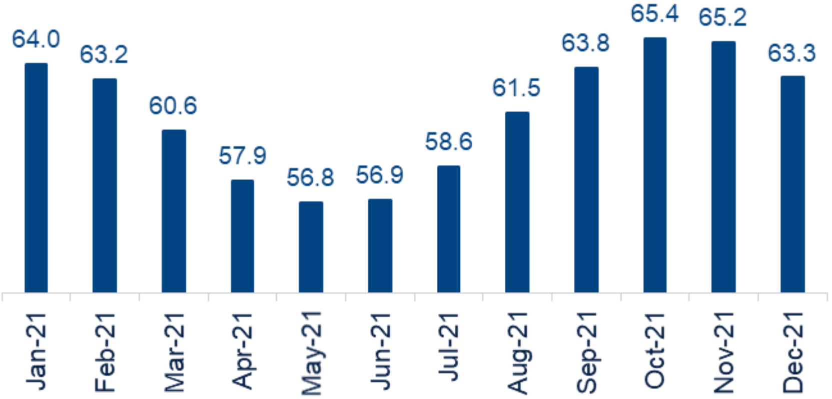
SOVEREIGN BOND YIELD CURVE (%)

	2023	2024	2026	2028	2029	2031	2037	2042	2055
31.12.2020	0.72	0.90	1.49	2.42	2.52	3.51	4.82	5.04	5.10
31.12.2021	3.62	4.25	4.71	5.36	5.49	5.90	6.67	6.79	6.81
Current (21/01/2022)	3.81	4.45	4.95	5.60	5.71	6.13	6.81	6.89	6.93
(differences in bp)									
31/12/21 vs 31/12/20	290	336	321	294	297	239	185	175	171
21/01/2022 vs 31/12/21	19	20	25	24	23	22	14	10	13

Source: BBVA Research, information from Bloomberg.

In the domestic financial markets, the returns of sovereign bonds continue rising within a context in which the Fed appears hawkish

TREND IN SOVEREIGN BONDS FOR NON-RESIDENTS
(BILLIONS OF PEN)



AS A % OF THE TOTAL BALANCE OF SOVEREIGN BONDS

52	50	48	46	44	45	46	48	50	51	51	49

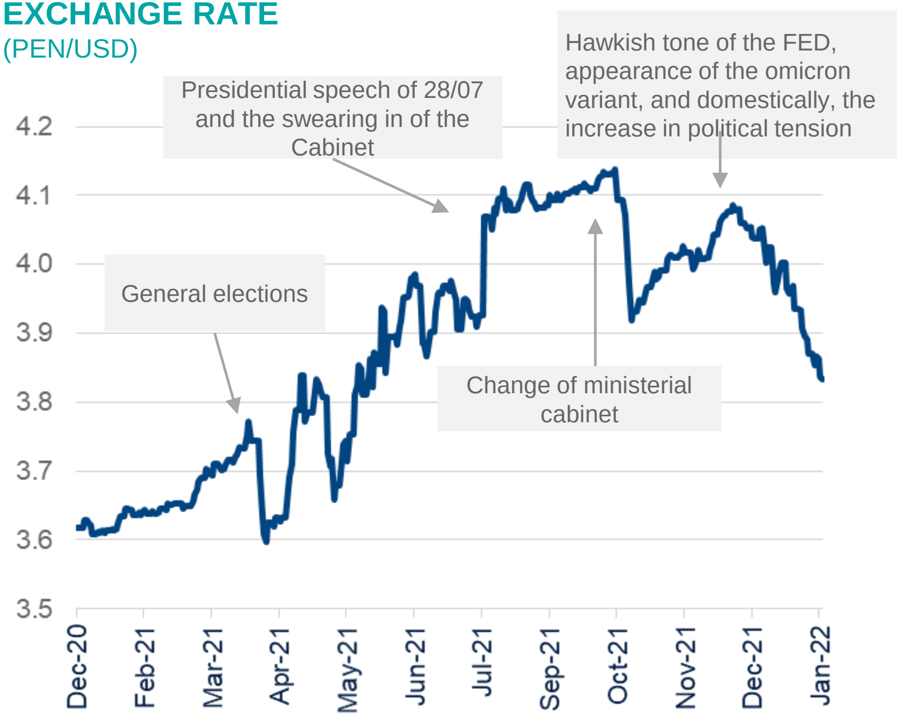
Source: BBVA Research, information from MEF.

The sovereign bond yield curve increased in 2021, mainly due to

1. the domestic electoral and political environment,
2. the release of pension funds,
3. the monetary adjustment of the Central Bank (which also had an influence on flattening the curve), and the
4. tapering of the FED, which at the last minute is combined with the anticipation that the FED will adjust its monetary positions sooner rather than later within an environment of strong inflationary pressures.

The domestic currency, after facing depreciation pressures throughout a good part of 2021, rallied in the last few weeks

EXCHANGE RATE
(PEN/USD)

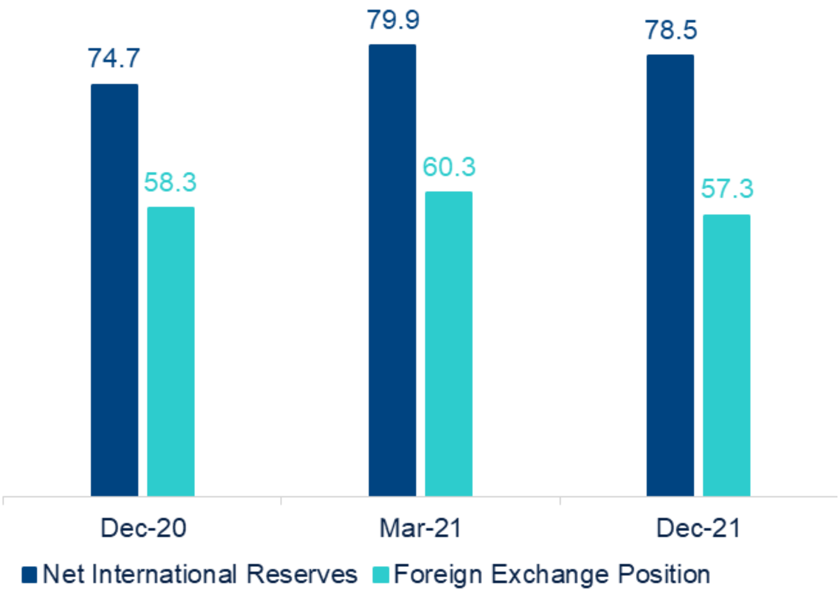


Source: BBVA Research, information from Bloomberg.

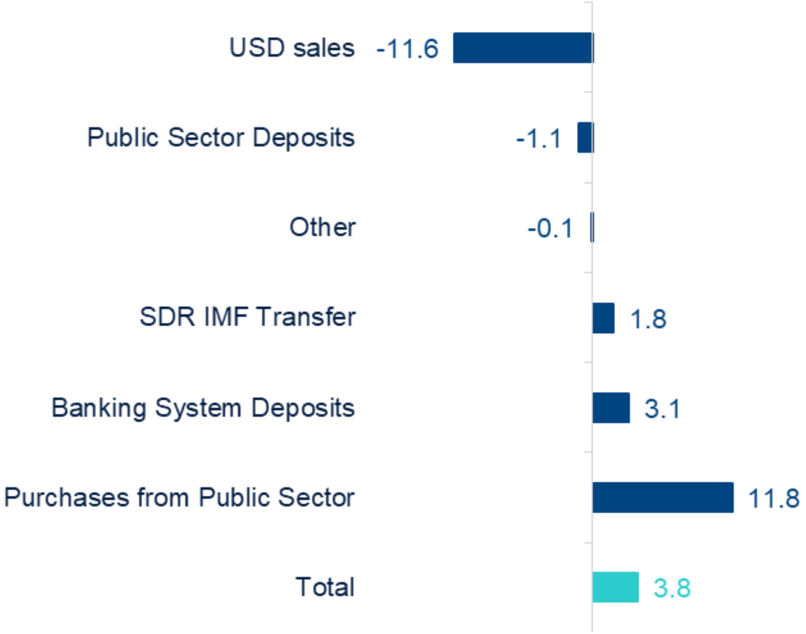
- The behavior of the exchange rate was affected by the domestic high electoral and political uncertainty for a good part of 2021, which led to a sharp fall in relative demand for assets in domestic currency (dollarization of portfolios, outflow of capital) by households, companies and foreign investors, thus weakening the PEN.
- The Central Bank (BCRP) intervened in the forex market to moderate the depreciation of the PEN by offering US$17.5 billion in 2021 (US$11.6 billion at the market spot rate).
- In recent weeks, and in spite of the FED being more hawkish, the PEN has rallied within an environment in which (i) the concerns about the global economic impact of omicron have lowered; (ii) the internal realization that an extreme (radical) political/economic scenario is less likely (Constituent Assembly); (iii) the fiscal deficit has decreased sharply; (iv) the BCRP continues to increase its policy rate and (v) the trade surplus continues to be significant.

Despite the strong intervention by the BCRP on the FX market over the last twelve months, international reserves remain at a high level…

BCRP: INTERNATIONAL RESERVES AND EXCHANGE RATE POSITION (MILLIONS OF USD)



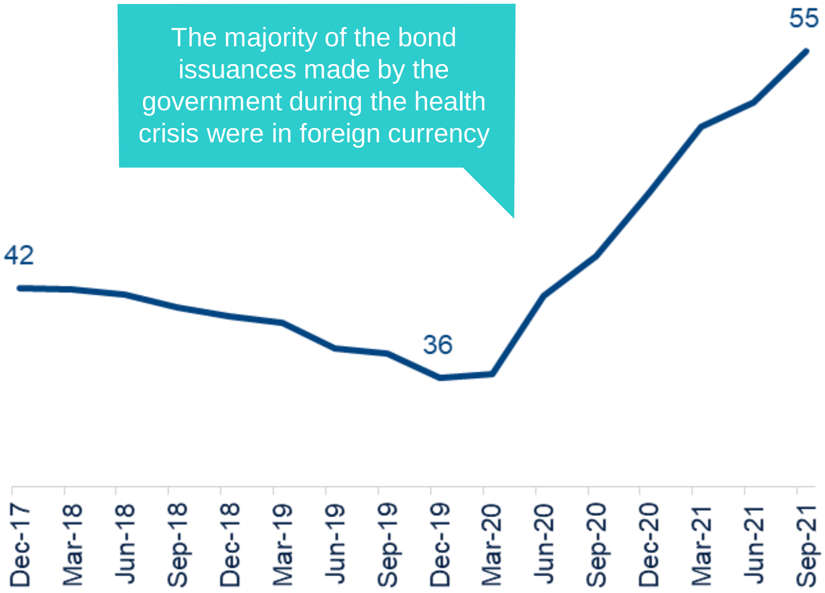
CHANGE IN NET INTERNATIONAL RESERVES (DEC-21 VS DEC-20, IN BILLIONS OF USD)



Source: BBVA Research, information from BCRP.

… offsetting the sales of dollars on the spot market with purchases of foreign currency from the Treasury

PUBLIC DEBT IN FOREIGN CURRENCY
(% OF TOTAL BALANCE)



Source: BBVA Research, information from BCRP and MEF.

- The Central Bank offset the sale of dollars on the spot market (to alleviate the depreciation pressures on the PEN) with the purchase of foreign currency from the Treasury, thus becoming indebted abroad in foreign currency (issues of global bonds) but would still require sols domestically to pay its expenses.
- In this context, the public debt continued to become dollarized in 2021, reversing the tendency to 'solarize' up until that time during the period of the health crisis.

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03

Macroeconomic outlook

3.1. GDP and economic activity

Main external considerations

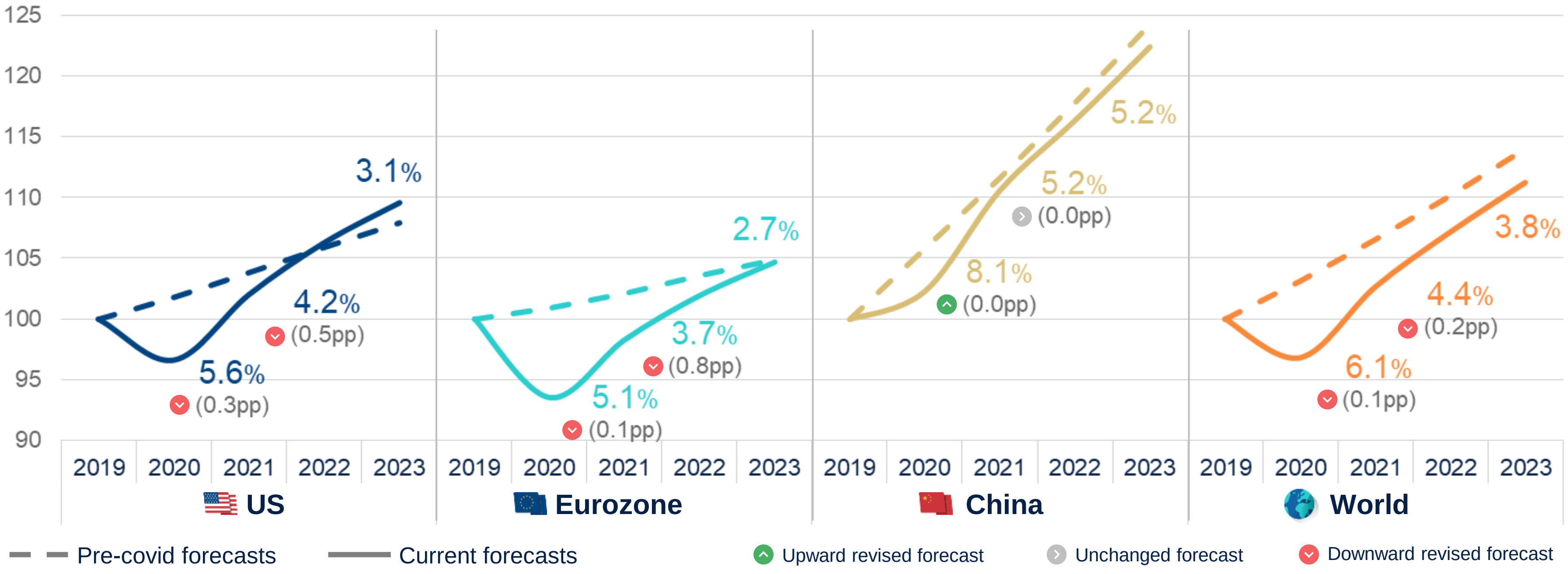
BASELINE SCENARIO

Pandemic	New waves of infections, with decreasing impacts on healthcare tension and on the economy (vaccination and better treatments)
Bottlenecks	These are maintained during the first half of 2022 and then return to normal due to the moderation in demand and the reaction of supply
Global growth	Gradual slowdown in growth, remaining relatively robust
Inflation	High -mainly short term and in the US- but gradually falling and under control
Economic policy	Early withdrawal of stimulus to control inflation; limited financial volatility

Global growth is estimated to be relatively robust in the next two years, although it will be weaker than previously anticipated

REAL GDP

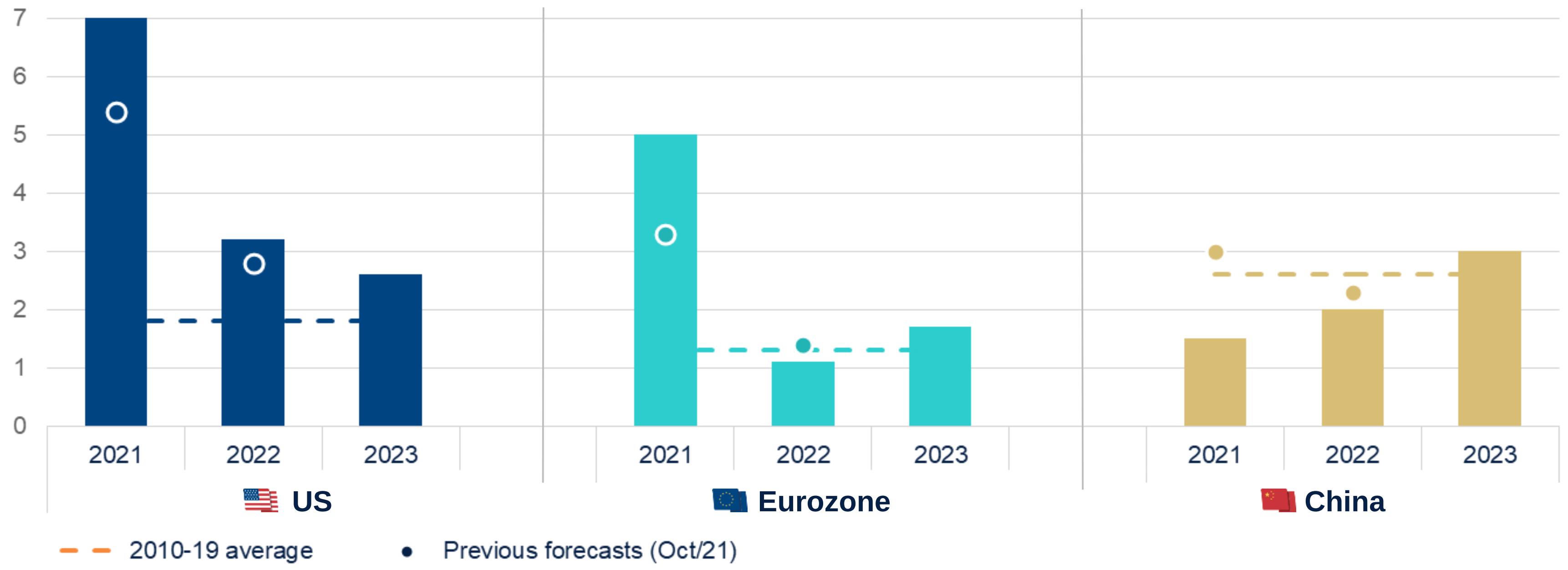
(LINES: GDP LEVEL 2019=100, FIGURES: FORECASTS AND CHANGES WITH RESPECT TO THE PREVIOUS ONES)



Source: BBVA Research.

Inflation will remain high, mainly in the short term and in the US; risks are to the upside, it is key to avoid significant second-round effects

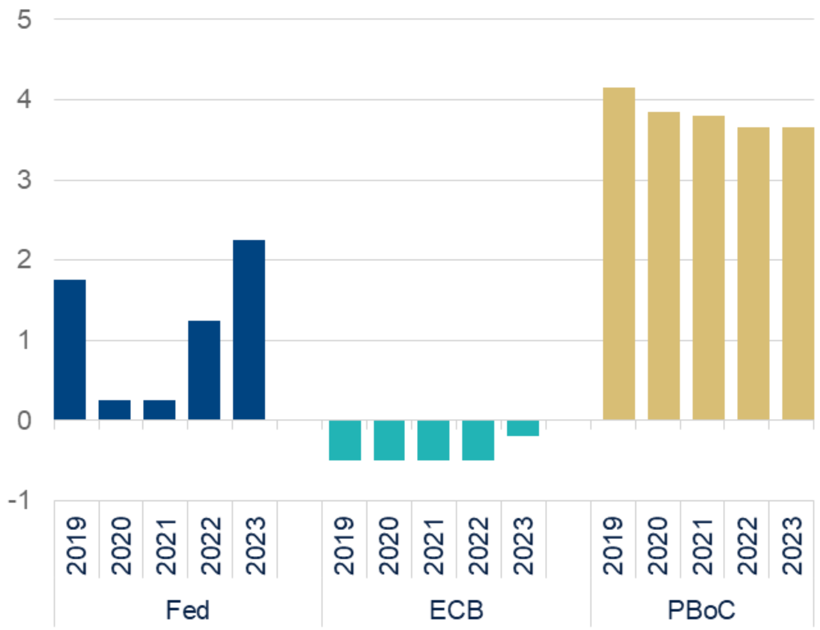
INFLATION: CPI
(Y/Y %, END OF PERIOD)



Source: BBVA Research.

The Fed will react to inflation with a quick tapering and interest rate hikes; the ECB will be more patient and the PBoC will remain focused on growth

POLICY INTEREST RATES*
(%, END OF PERIOD)



*: In the case of the ECB, deposit facility rates. Forecasts for 2022 and 2023.
Source: BBVA Research

US

- The Fed is focused on controlling inflation.
- We expect i) the tapering to end no later than in Feb/22, ii) four 25bp rate hikes in 2022 and four in 2023, iii) a balance sheet reduction from this year on.

Europe

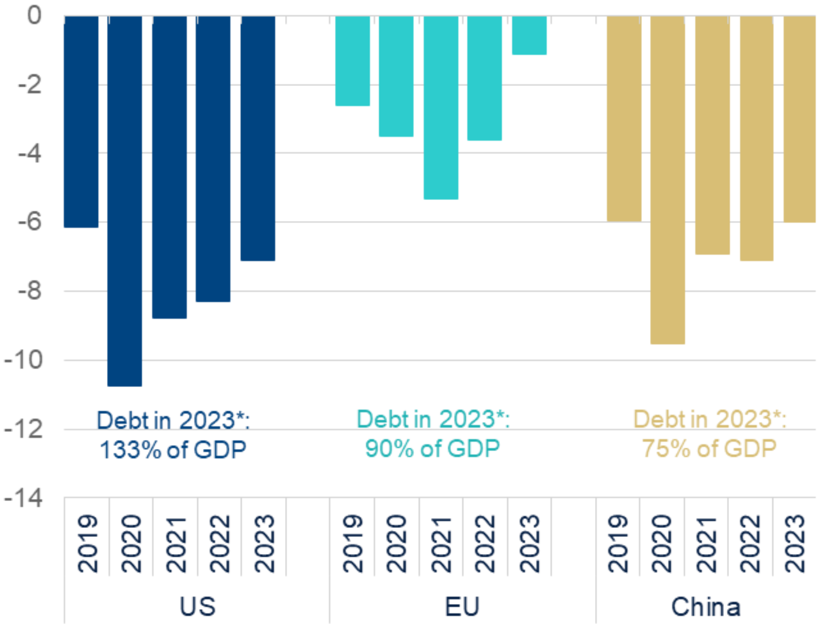
- End of the PEPP on Mar/22, and bond purchases via APP will be reduced until mid-2023.
- Interest rates will remain unchanged until the second half of 2023; ECB to exhibit an increasingly hawkish tone.

China

- Monetary stimulus is resumed: further cuts in interest rates and bank reserve requirements, among other measures, in 2022 to avoid a sudden slowdown in the economy.

Fiscal policy will still be expansionary in the coming years, but the stimuli will not be as notable as in 2020-2021

STRUCTURAL FISCAL RESULT
(% OF POTENTIAL GDP)



*: General government gross debt estimated by the IMF.
Source: BBVA Research based on data by the IMF and the European Commission.

US

- New stimuli, more focused on supporting supply (with less impact on inflation).
- After the approval of the infrastructure plan (less significant than expected), the social investment plan is now being debated.

Europe

- Increasing use of NGEU resources will support growth in 2022-23.
- Increasing debate on fiscal rules from 2023 on.

China

- Additional stimulus measures to counteract the impact of regulatory activism, real estate market adjustments, “zero tolerance” on COVID and energy transition policies.

Main domestic considerations

COVID-19

The third wave of infections at the beginning of 2022 will have a limited and transitory impact on activity (confinement measures will not be as tough) due to the progress of the vaccination program. Beyond this, the maximum allowed capacity will once again become normal.

Political context

The likelihood of an extreme (radical) political/economic scenario is decreasing. The most radical proposals have not achieved any significant progress. The risk remains, but less so. For example, the approval of a law and a pronouncement of the Electoral Board have reinforced that any constitutional reform must be approved by Congress before going to a potential referendum (this reduces the likelihood of a Constituent Assembly being formed). Support for the Executive has decreased. Subsequently, uncertainty and caution with regard to spending remains on the horizon for the foreseeable time, but gradually beginning to ease.

Mining production

Construction of Quellaveco will be finished. This and another two medium-sized copper mines enter the production phase. However, the negative impact in production is sensitive to social conflicts.

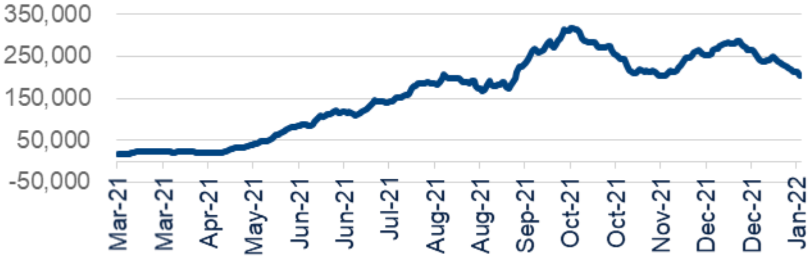
Economic policies

The monetary stimulus is withdrawn. On the fiscal side, it is assumed that no more liquid funds will be released for families (AFP, CTS); the award of transfers to families is more restricted and focused; the costs of the healthcare emergency are beginning to stabilize. Slowdown in public investment in 2023, then subnational elections (towards the end of 2022).

Regarding the sanitary front, the third wave of infections at the beginning of 2022 will have a limited and transitory impact on activity due to the progress of the vaccination program

DAILY DOSES
(30-DAY MOVING AVERAGE)

The vaccination program advances…



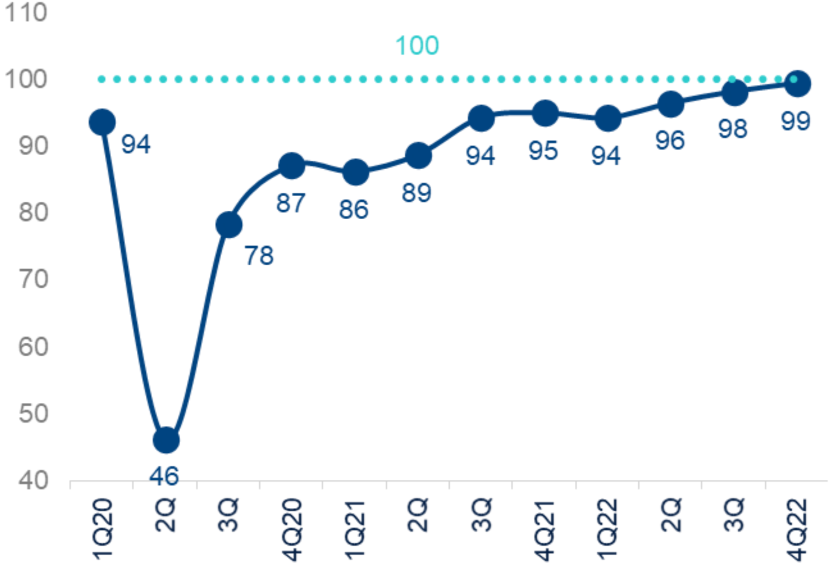
NUMBER OF VACCINE DOSES PER SUPPLIER
(MILLIONS OF DOSES)

Laboratory	2021	2022	Total
Sinopharm	26.5	0	26.5
Pfizer[1]	33.2	35.7	68.9
AstraZeneca	5.3	8.5	13.8
Covax Facility	2.9	12.3	15.2
Gamaleya	-	20.0	20.0
Moderna	-	20.0	20.0
Total	**67.8**	**96.6**	**164.4**

… and in 2022 there will be vaccines available…

1: Including 2 million doses donated by the US
Source: BBVA Research, information from News reports and MINSA.

INDEX OF ACTIVITY OF ALL SECTORS MOST AFFECTED BY THE CONFINEMENT MEASURES
(LEVEL AS A % OF THE SAME PERIOD FOR 2019)

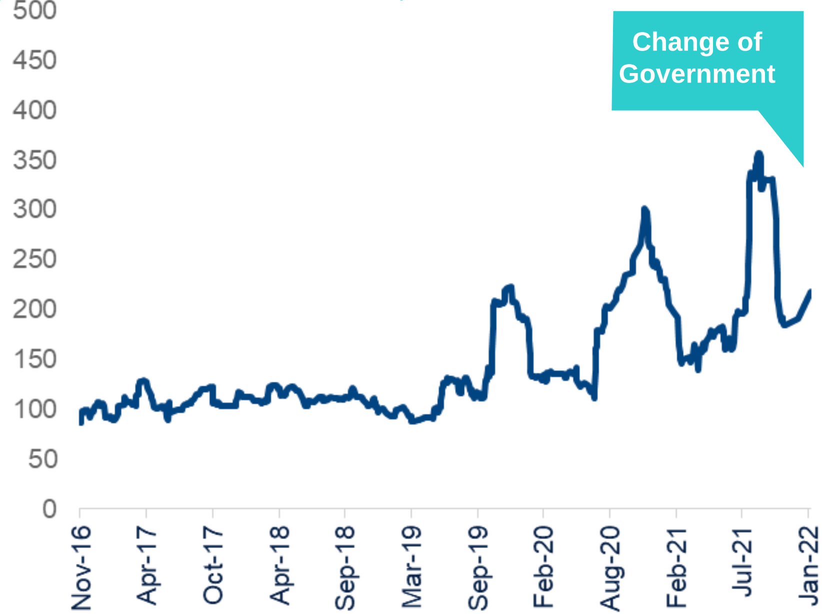


… the activity of the sectors most affected by the confinement measures will gradually return to normal

In politics, it is considered that the likelihood of an extreme (radical) scenario is decreasing and with it the uncertainty and caution in spending

CONSTITUENT ASSEMBLY[1/]: MENTIONED IN THE MEDIA

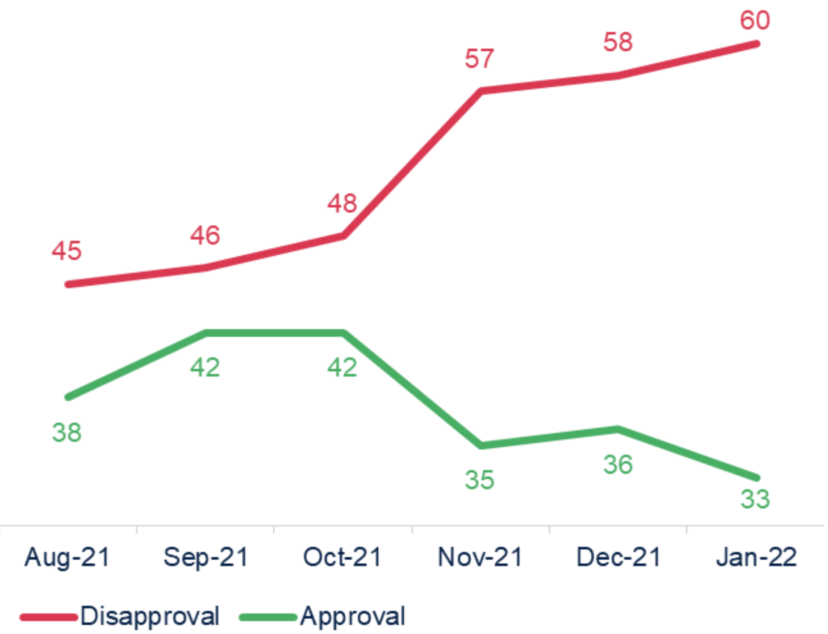
(INDEX, AVERAGE DEC.19 = 100)



1: Also considers mentions of constitutional changes
Source: BBVA Research, information from GDELT.

PRESIDENTIAL APPROVAL

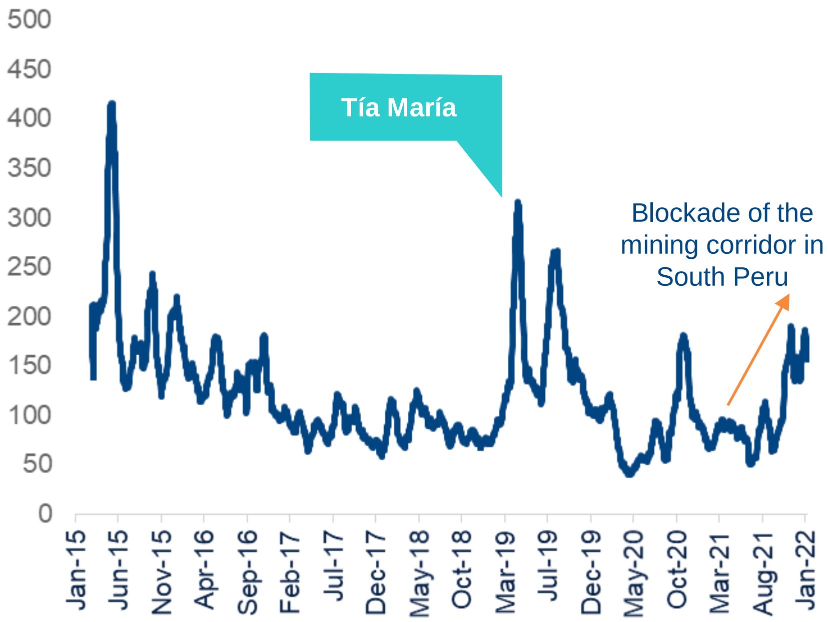
(%)



Source: BBVA Research, information from Ipsos Peru.

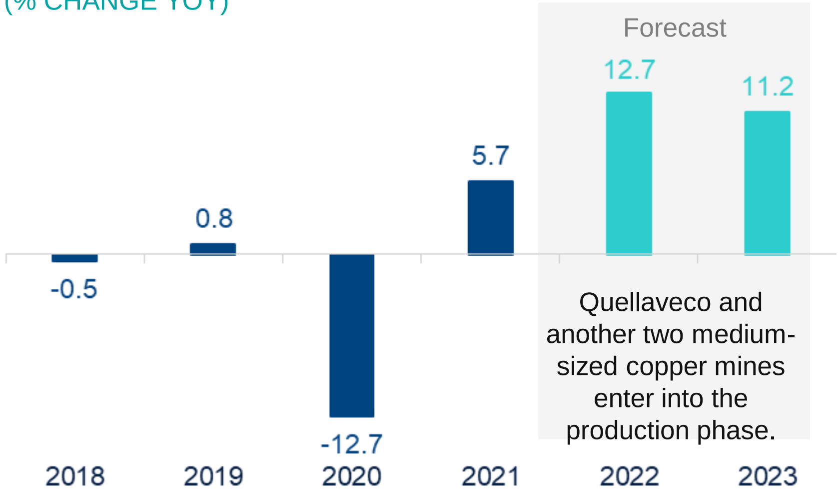
And in the mining sector, Quellaveco enters its production phase in 2022… although the impact of the social conflicts will also be significant

MINERS SOCIAL CONFLICTS: MENTIONS IN THE MEDIA (INDEX, AVERAGE DEC.19 = 100)



Source: BBVA Research, information from GDELT.

COPPER PRODUCTION (% CHANGE YOY)



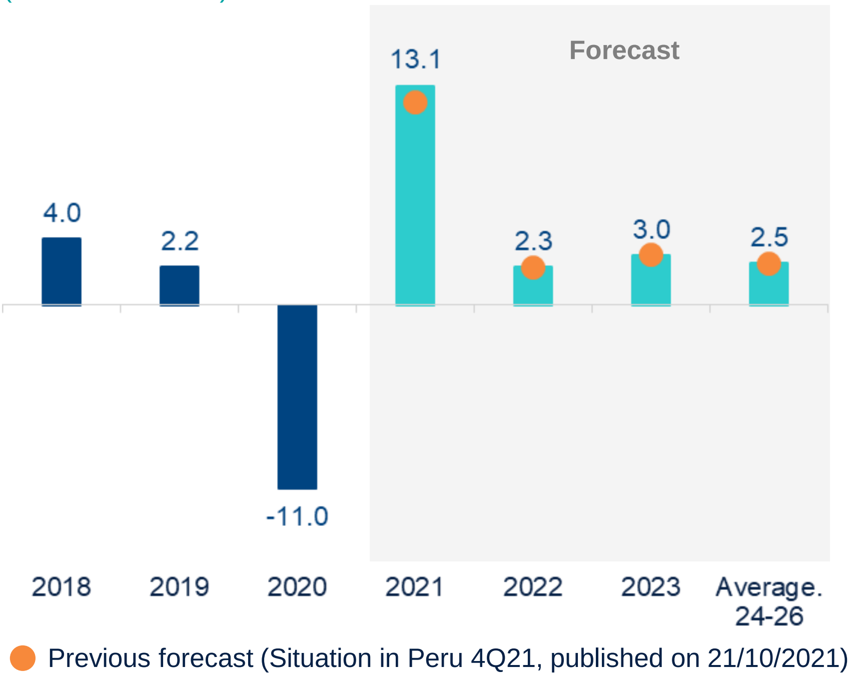
COPPER PRODUCTION (MILLIONS OF MT)

2019	2020	2021	2022	2023
2.2	2.0	2.1	2.3	2.6

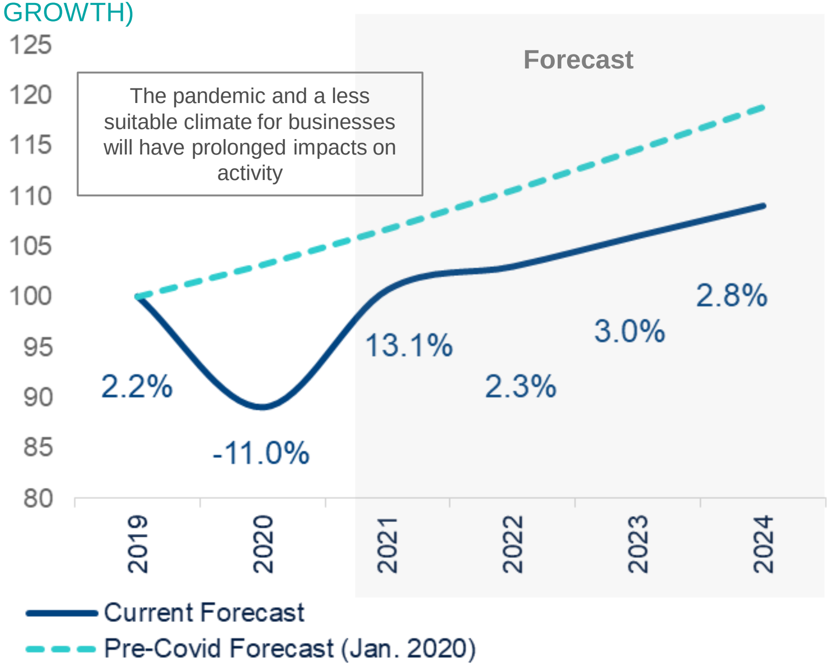
The figures for 2021 are estimated.
Source: BBVA Research, information from BCRP.

In this scenario, we forecast that the GDP will increase by 2.3% this year and 3.0% the next

GDP
(% CHANGE YOY)



GDP
(LINES: INDEX, LEVEL 2019 = 100; FIGURES: FORECAST GROWTH)

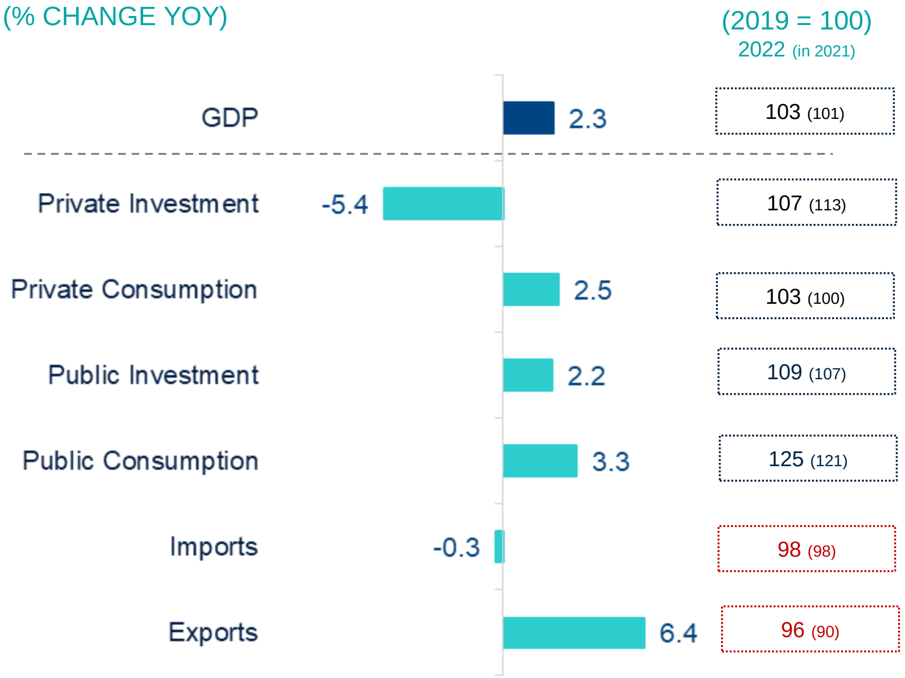


Source: BBVA Research, with information from BCRP. Forecast: BBVA Research.

Uncertainty and higher interest rates slow down private investment; increased mining production will favor exports

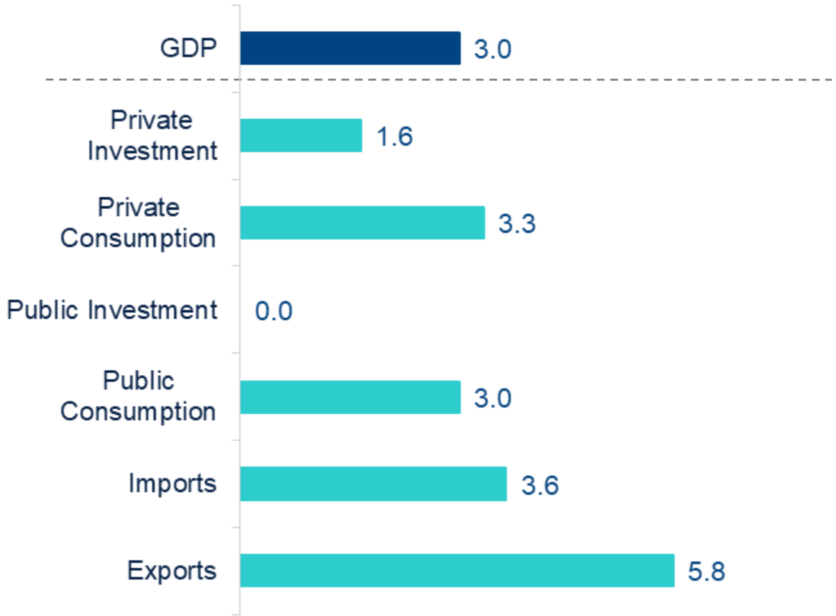
GDP ON EXPENDITURE SIDE IN 2022

(% CHANGE YOY)



GDP ON EXPENDITURE SIDE IN 2023

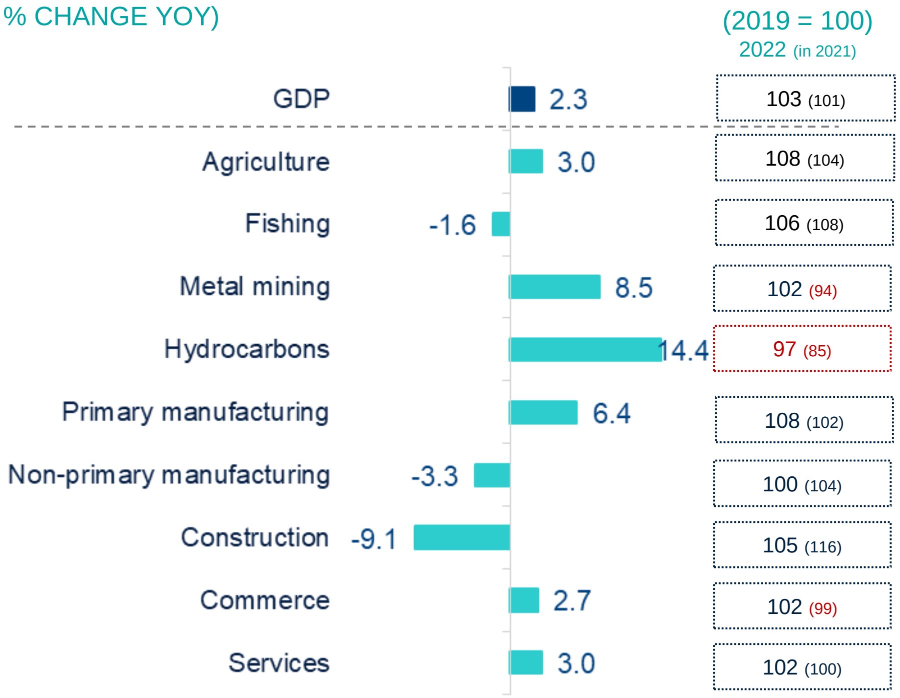
(% CHANGE YOY)



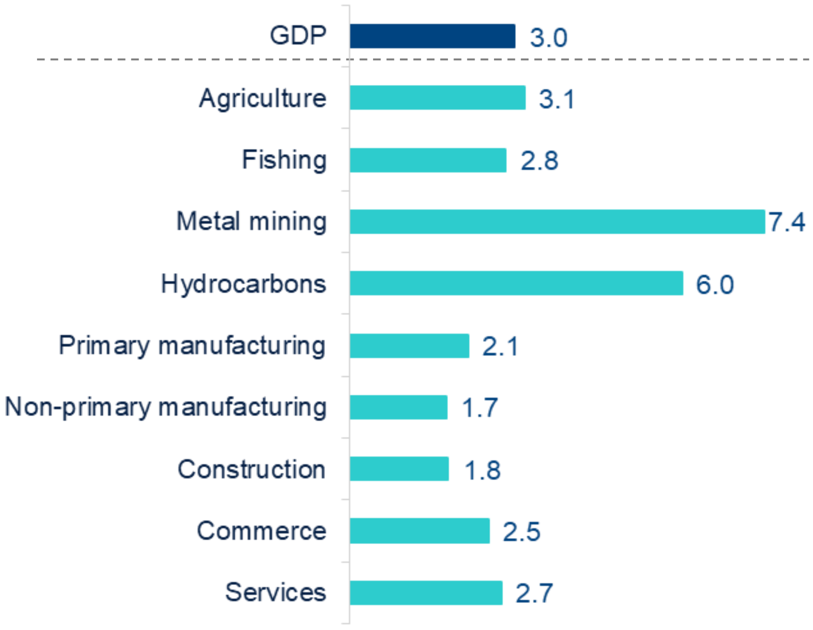
Source: BBVA Research.

The reversal of private investment in 2022 will be reflected in the construction and non-primary manufacturing sectors

GDP BY SECTOR IN 2022
% CHANGE YOY)



GDP BY SECTOR IN 2023
% CHANGE YOY)



Source: BBVA Research.

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03

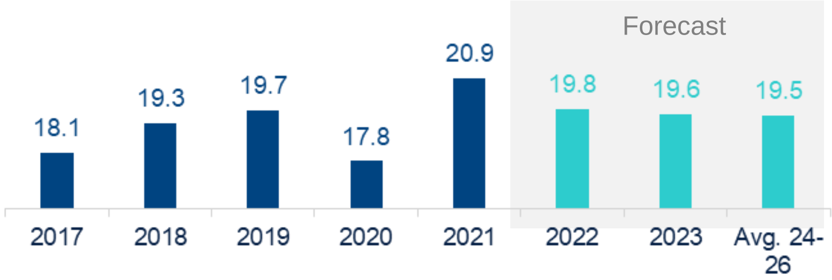
Macroeconomic outlook

3.2. Fiscal balance and public debt

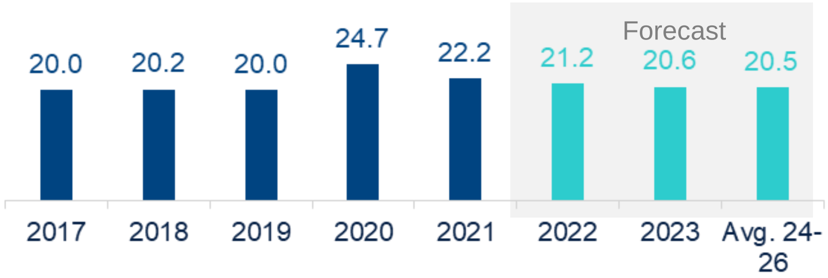
Metal prices, a recovery in activity, and more moderate expenditure explain the sharp decrease in the fiscal deficit in 2021

FISCAL BALANCE
(NON-FINANCIAL PUBLIC SECTOR, % OF GDP)

GENERAL GOVERNMENT REVENUE
(% OF GDP)



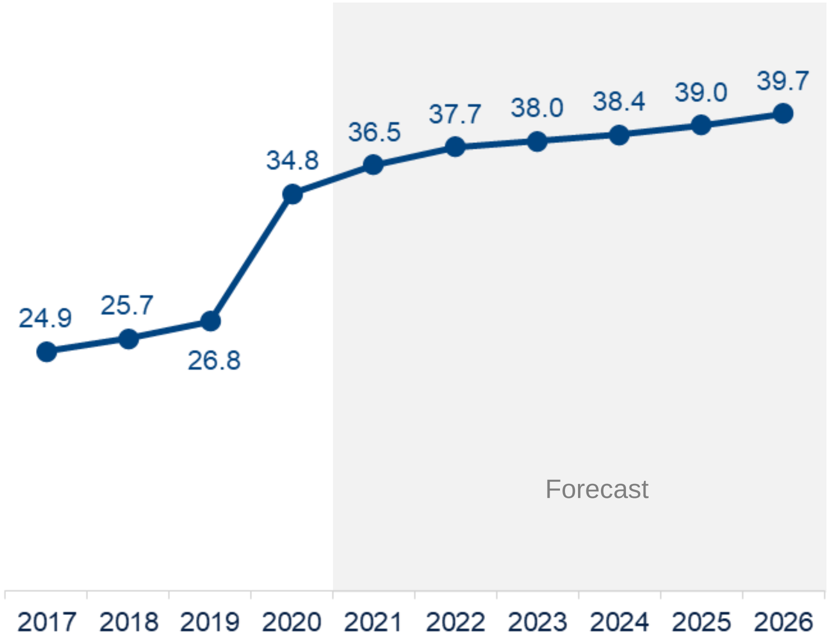
GENERAL GOVERNMENT EXPENDITURE (% OF GDP)



Source: BBVA Research, information from BCRP. Forecast: BBVA Research

Gross public debt will continue escalating; measures to increase fiscal revenue and contain expenditure will be required to stabilize it

GROSS PUBLIC DEBT (% OF GDP)



Source: BBVA Research, information from BCRP. Forecast: BBVA Research.

STRUCTURAL FISCAL BALANCE

(NON-FINANCIAL PUBLIC SECTOR, % OF POTENTIAL GDP)

	2020	2021	2022	2023
Primary structural balance	-3.1	-1.4	-1.3	-1.0
Economic structural balance	-4.5	-2.9	-2.9	-2.7
Fiscal drive	3.1	-1.7	-0.1	-0.3

- According to our estimates, stabilizing the gross public debt at a level equal to 40% of GDP would require a primary fiscal deficit of between 0.5% to 0.6% of GDP.

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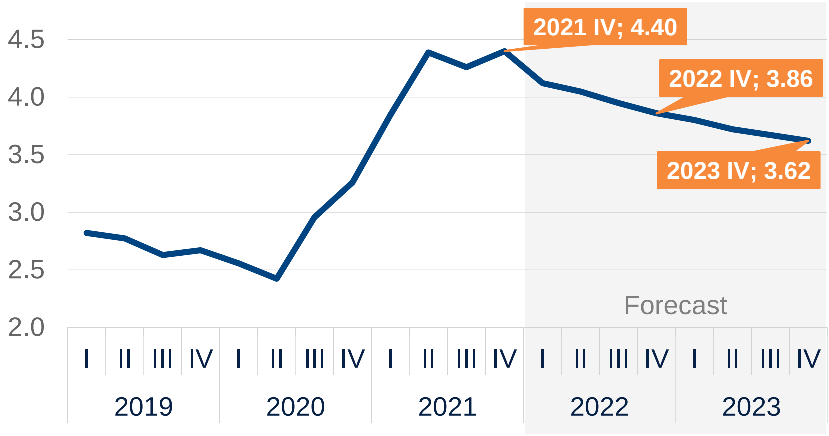
03

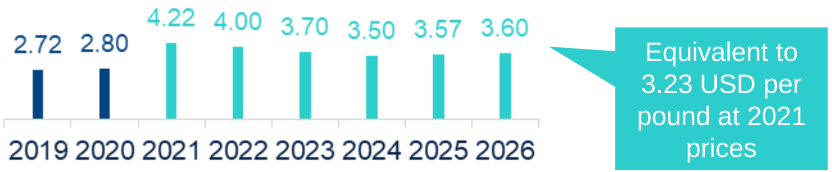
Macroeconomic outlook

3.3. External sector and exchange rate

Copper price will fall in 2022-2023 but the new levels will continue to be attractive for mining investment

PRICE OF COPPER
(AVERAGE FOR THE PERIOD USD/POUND)





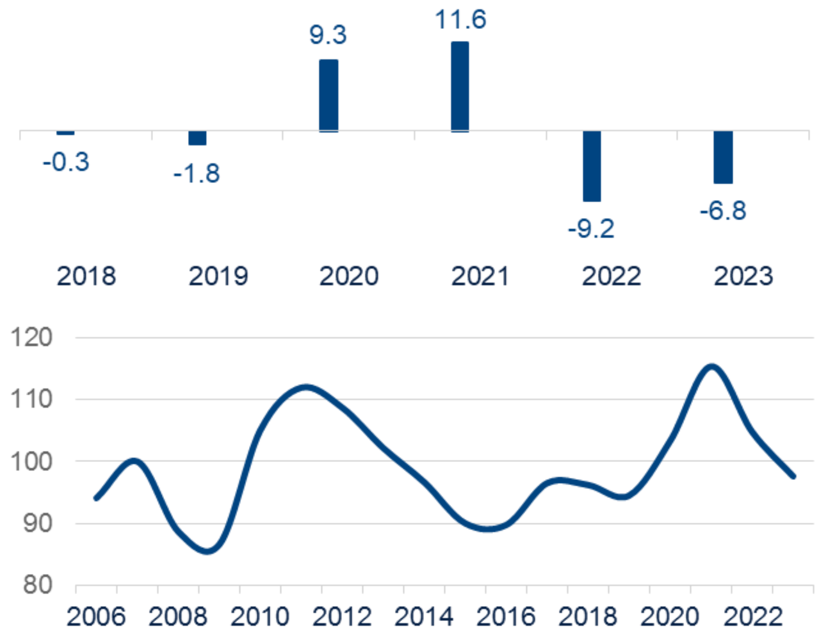
- We forecast that in 2022 the global copper deficit will decrease, firstly due to the entry into production of some mines (such as Quellaveco), and secondly the slowdown of global growth.
- Production problems due to social conflicts (in Peru, for example) will take some time to dissipate.
- In the medium term, the price of copper will find support in the larger investments in green infrastructures and in vehicle reconversion, areas that are gradually acquiring greater significance.

Source: BBVA Research, information from Bloomberg. Forecast: BBVA Research.

Against this backdrop, the trade surplus in 2021 was the highest on record and will remain with a positive outlook for the next two years

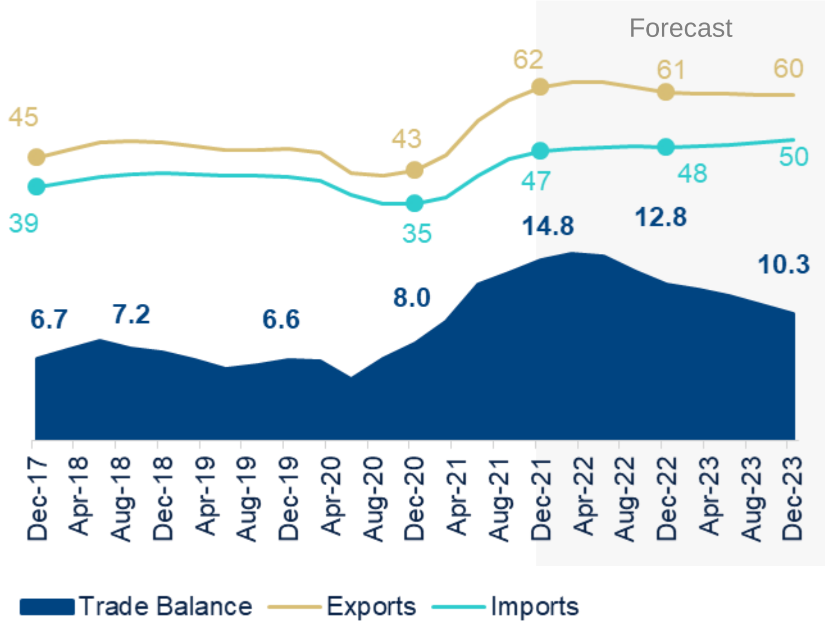
TERMS OF TRADE

% CHANGE YOY; INDEX, 2007 = 100)



TRADE BALANCE

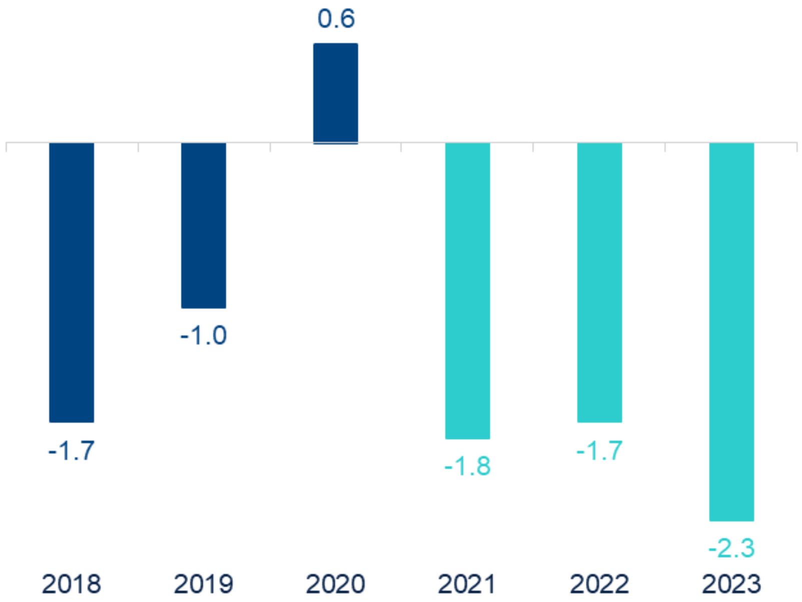
(IN BILLIONS OF USD, ACCUMULATED FOR THE LAST FOUR QUARTERS)



Estimates for 2021. Forecast for 2022 and 2023.
Source: BBVA Research, information from BCRP. Forecast: BBVA Research.

The trade surplus forecast for the next two years is consistent with low external financing requirements (low current account deficits)

BALANCE OF PAYMENTS CURRENT ACCOUNT
(% OF GDP)

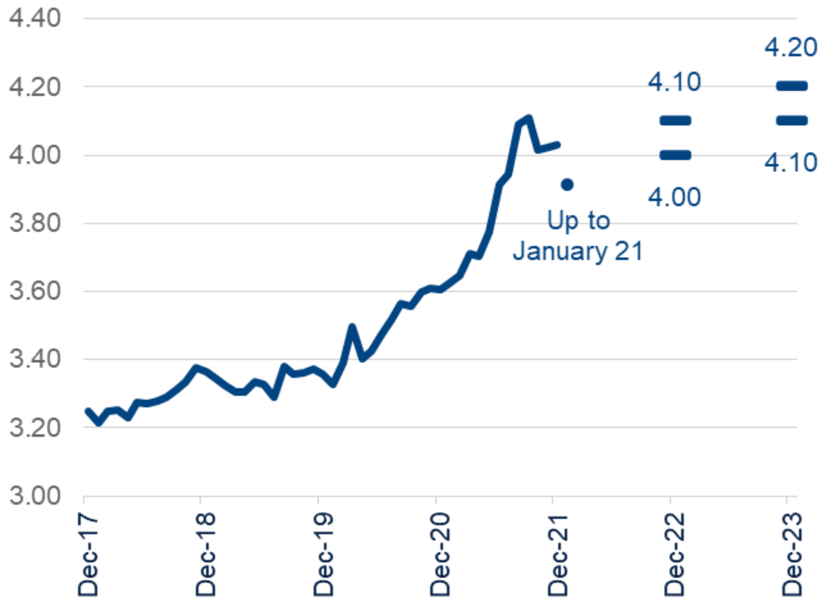


Estimates for 2021. Forecast for 2022 and 2023.
Source: BBVA Research, information from BCRP. Forecast: BBVA Research.

- The decrease in metal prices will be offset by the greater production of copper, a gradual improvement in tourism, and a slowdown in the prices of imported consumables (oil, food).
- As a result, the annual deficit of the current account balance of payments will stand at around 2% of GDP for the next two years (USD 4.5 billion), on average.
- One of the main sources of financing of the deficit of the current account balance of payments will be the external debt taking of the public sector.
- The baseline scenario for the balance of payments does not assume short-term outflows of capital like those observed in 2021 (due to the decreased likelihood of an extreme, or radical, political/economic scenario).

We forecast a limited depreciation of the PEN in 2022: The Fed removes the monetary stimulus, but domestic political uncertainty decreases

EXCHANGE RATE
(PEN/USD, MONTHLY DAILY AVERAGE)



Source: BBVA Research, information from Bloomberg. Forecast: BBVA Research

- The main reason why the PEN weakened in 2021 was the domestic electoral/political factor, with a high risk of the implementation of radical measures (such as the Constituent Assembly).
- The baseline scenario for 2022 incorporates a decreased likelihood of such a situation, although the risk does not fully disappear. The depreciation pressures on the PEN will be lower because of this.
- In 2022, it will be the FED, with the withdrawal of the monetary stimulus (quick tapering, interest rate hikes, balance sheet reduction), which will be the source of the upward pressures on the USDPEN.
- The monetary adjustment of the BCRP and the high trade surplus will ease these pressures.
- In this environment, we estimate that the domestic price of the dollar will close 2022 (daily average for December) at between 4.00 and 4.10 PEN/USD, whereas in 2023, it will be between 4.10 and 4.20 PEN/USD.

BBVA Research

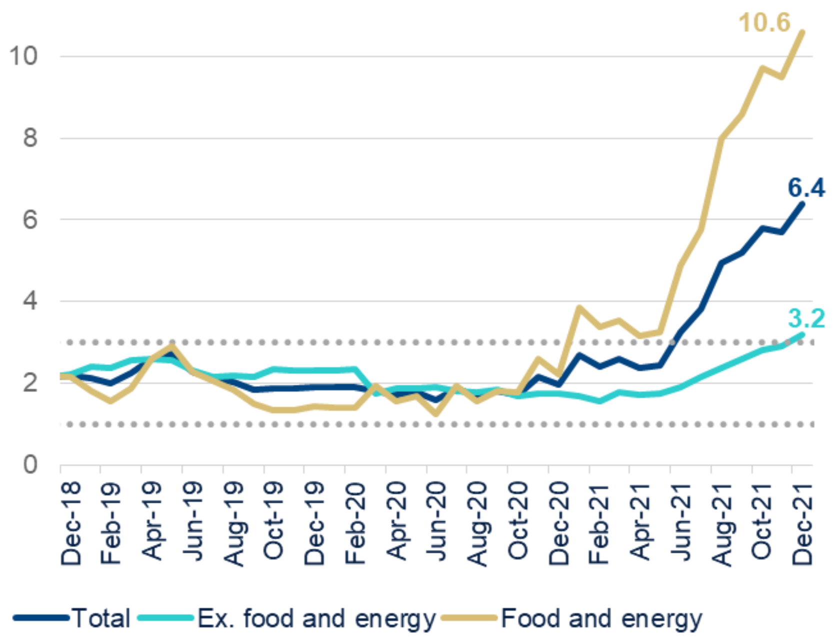
03

Macroeconomic outlook

3.4. Inflation and monetary policy

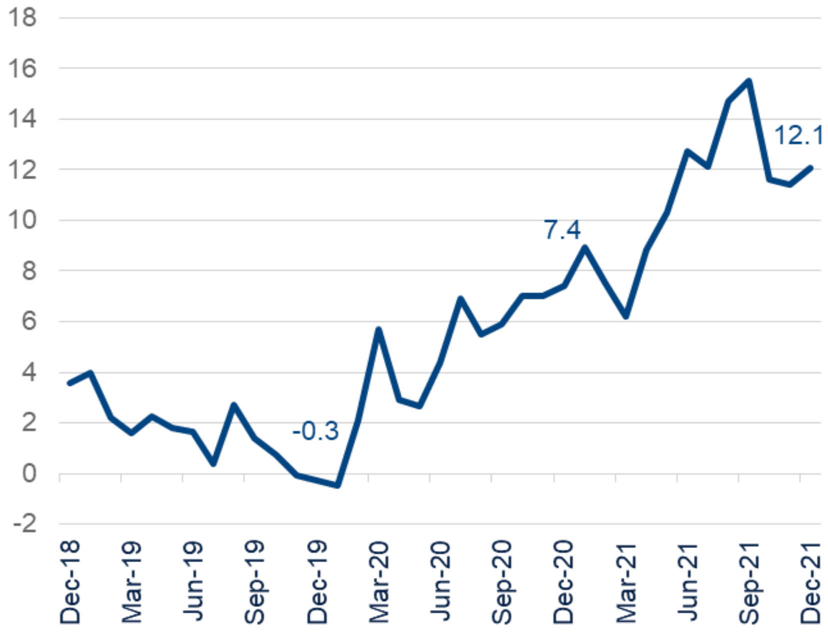
Inflation rose significantly in 2021 due to the sharp increase in the exchange rate…

INFLATION
(% CHANGE YOY OF THE LIMA CPI)



Source: BBVA Research, information from INEI.

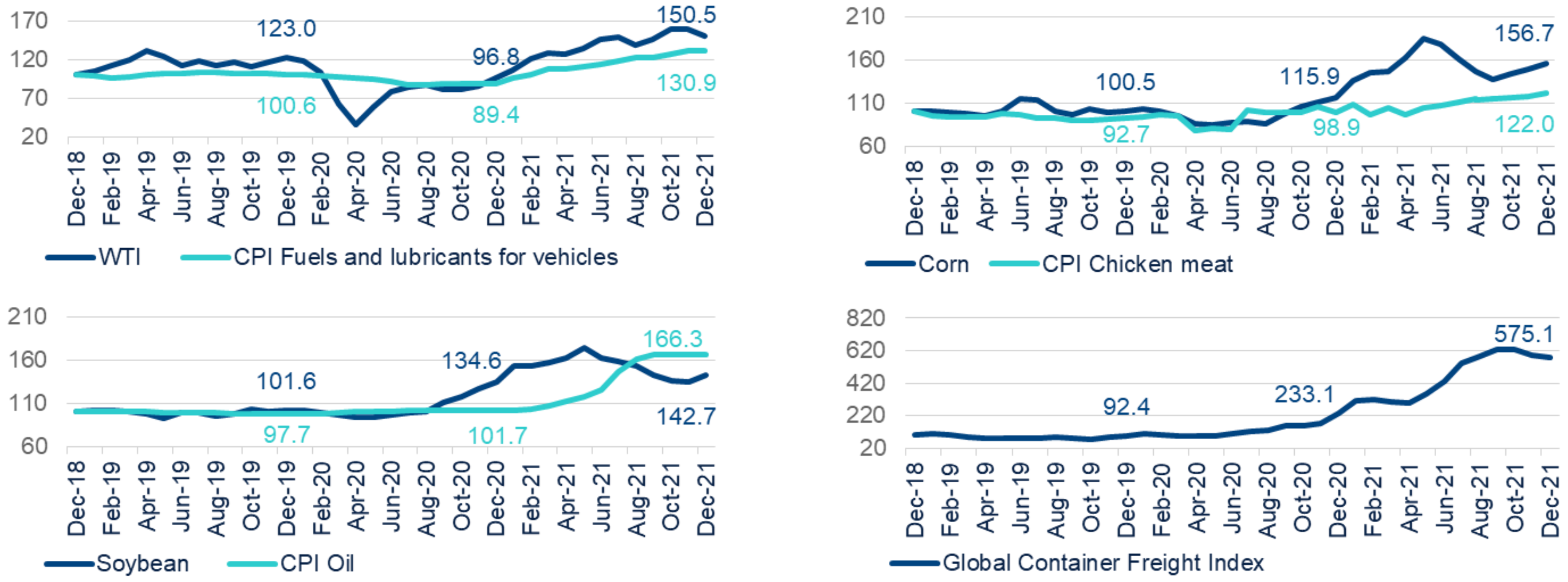
EXCHANGE RATE
(MONTHLY DAILY AVERAGE, % CHANGE YOY)



Source: BBVA Research, information from BCRP.

… international prices in fuels and foods, and global shipping costs

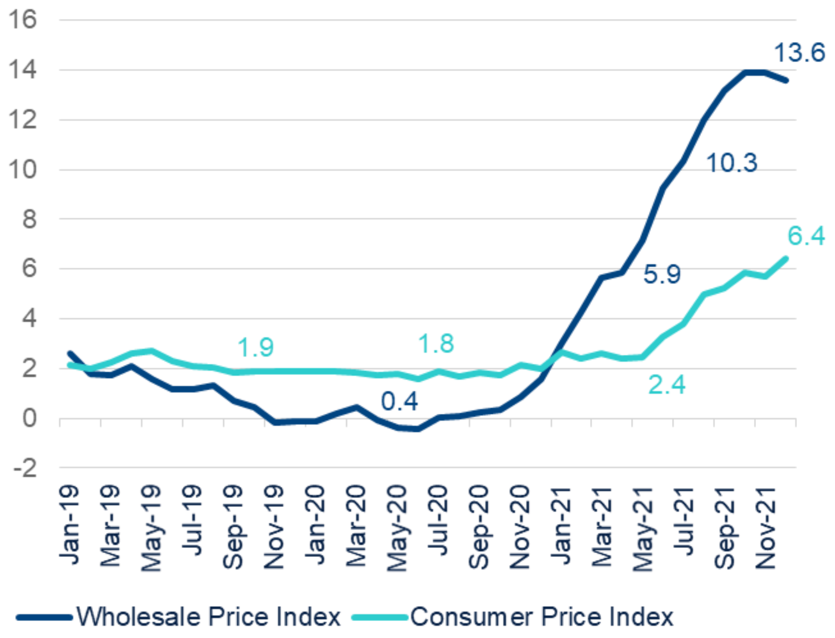
PRICES OF COMMODITIES AND SELECTED COMPONENT OF THE CPI (INDEX, DEC.18 = 100)



Source: BBVA Research via Bloomberg and the INEI.

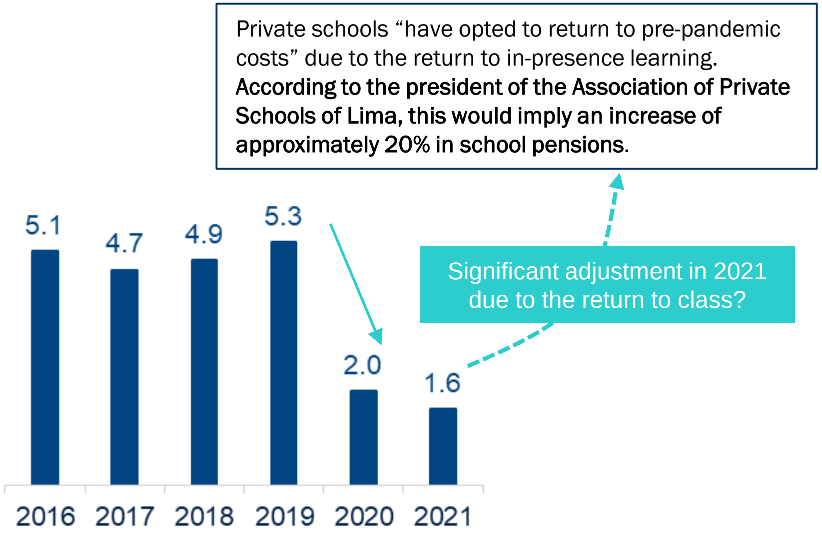
Inflation will be higher over the coming months: (i) additional transmission from wholesale prices, (ii) normalization of prices with the reopening…

WHOLESALE AND RETAIL PRICES
(% CHANGE YOY)



Source: BBVA Research, information from BCRP.

CPI EDUCATION
(INCLUDES ENROLMENT AND TEACHING PENSION, % CHANGE YOY)

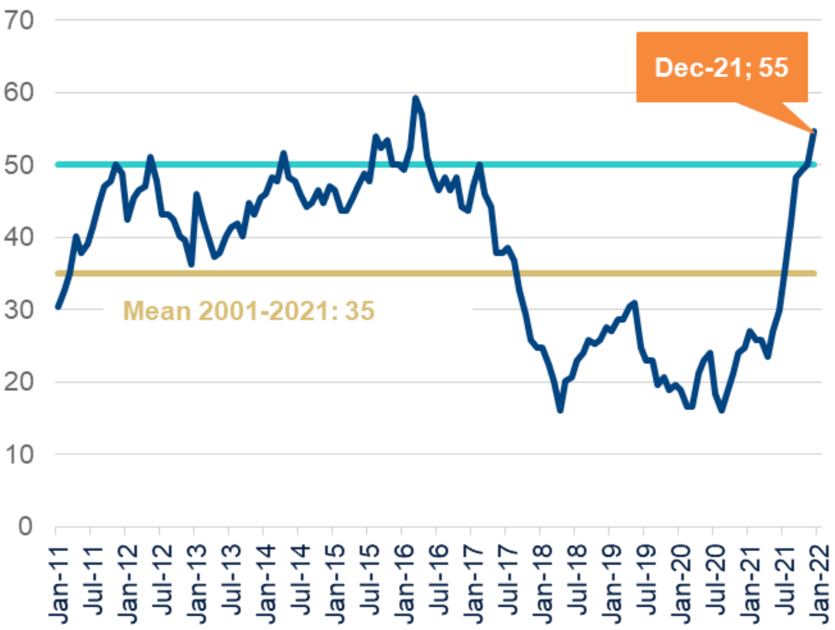


Education has a significant weight in the consumer basket (around 9%)

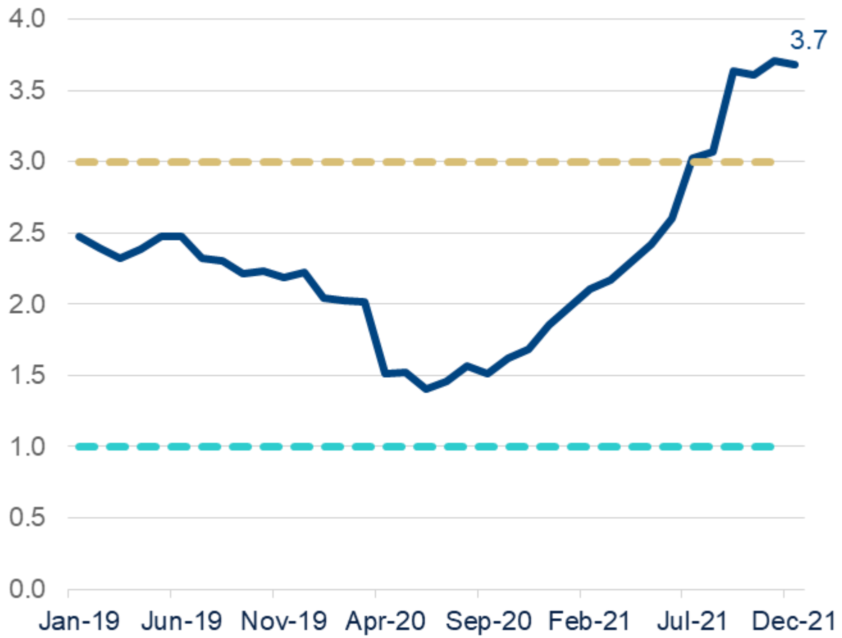
Source: BBVA Research, Information from INEI and local news reports.

… and (iii) inertia, resulting from the gradual generalization of the increase in prices and higher inflation expectations

PERCENTAGE OF THE HEADINGS OF THE CPI WITH A YOY CHANGE IN PRICES GREATER THAN 3%



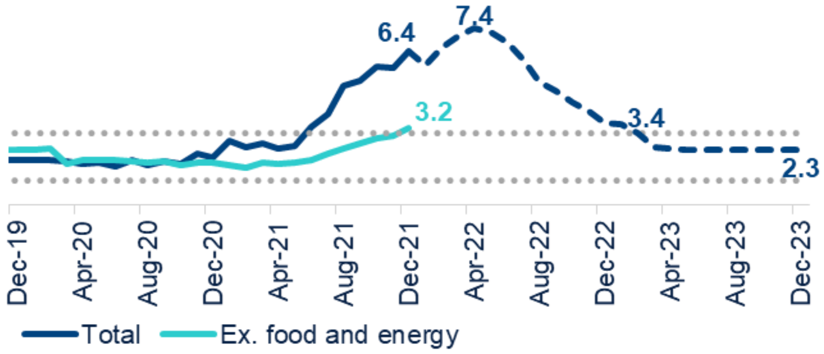
INFLATION EXPECTATIONS FOR THE NEXT YEAR (%)



Source: BBVA Research, information from BCRP.

During the second half of the year, inflation will decrease, but will only return to the BCRP's target range in 2023

INFLATION
(% CHANGE YOY OF THE LIMA CPI)



OUTPUT GAP
(% OF THE POTENTIAL GDP)

INFLATION WILL BEGIN TO EASE DURING THE SECOND HALF OF THE YEAR BECAUSE…

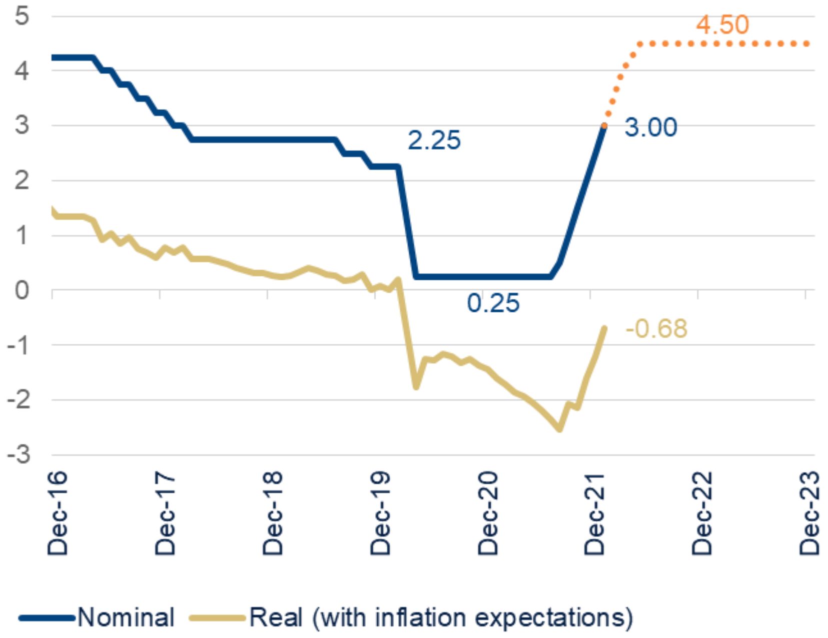
- After depreciating by 12% in 2021, the PEN will show a more limited weakness in 2022 and 2023.
- The international prices of food and energy commodities will begin to at least show some correction.
- Bottlenecks in global supply chains will gradually ease.
- Resistance down? Output gap negative in 2022 but closing, and the impact of the price corrections of some services (education, for example).

Source: BBVA Research, information from BCRP. Forecast: BBVA Research.

Due to the persistence of inflation and the risk of unanchored expectations, the BCRP will rush monetary normalization

REFERENCE RATE

(%)

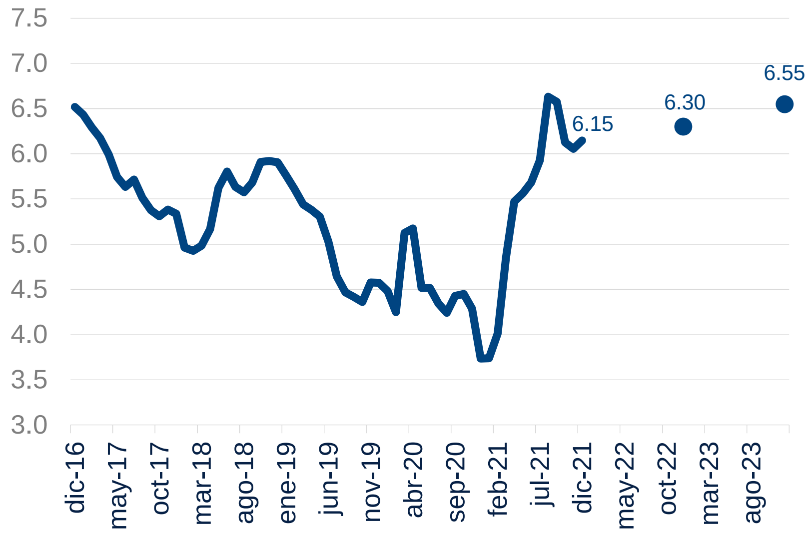


Source: BBVA Research, information from BCRP. Forecast: BBVA Research

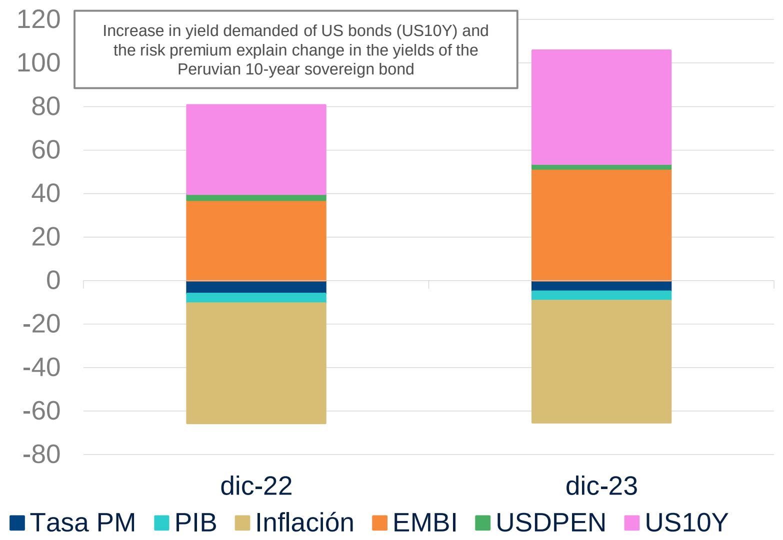
- The BCRP maintained the reference rate at 0.25% until July 2021 in a context of negative output gap and uncertainty regarding the evolution of the pandemic.
- Subsequently, with inflation and its expectations increasing (from 2.6% in June to 3.7% in December), it started a cycle of successive increases in the policy rate: an adjustment of 25 bp in August and then, 50 bp in each of the following five months. Positive surprises in activity provided the necessary space in order to normalize the monetary position.
- Reserve requirements in domestic currency also rose. Additional increases were recently announced for the minimum requirement in soles (+25bp for each of the months between February and May, up to 6.0%).
- We forecast that the policy rate will reach a level of 4.5% in the second quarter of 2022, above what we estimate as neutral, despite the output gap continuing to be negative. The objective is to avoid an even greater persistence of inflation.

Forecast baseline scenario is consistent with an increase in the Peruvian 10-year sovereign bond yield

YIELD ON 10-YEAR SOVEREIGN BOND
(%)



FACTORS THAT EXPLAIN THE CHANGE IN YIELDS OF THE 10-YEAR SOVEREIGN BONDS
(CHANGES COMPARED TO DEC-21, IN BP)



Source: Bloomberg. Forecast: BBVA Research.

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04

Main risks

Main risks of the baseline scenario the forecasts

EXTERNAL

- Fed: faster or more disorderly adjustment of its monetary position.
- More significant slowdown in China.
- More significant and persistent bottlenecks in global supply chains.
- Social and geopolitical tensions.

POLITICAL

- Government implements more radical proposals.
- Presidential vacancy? Dissolution of Congress?

HEALTHCARE

- Progress in vaccination against COVID.
- New coronavirus strains

OTHER

- Greater social conflict.
- Beginning of the Yanacocha Sulfuros mining project (a USD 2,1 billion project).
- Greater use of savings accumulated by households during the pandemic.

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05

Summary of forecasts

Macroeconomic forecasts: summary

	2020	2021 (e)	2022 (p)	2023 (p)
PIB (% %)	**-11.0**	**13.1**	**2.3**	**3.0**
Internal demand (excludes inventory, % %)	**-8.7**	**16.2**	**1.0**	**2.8**
Private spending (% %)	**-10.5**	**16.4**	**0.6**	**2.9**
Private consumption (% %)	-8.7	11.3	2.5	3.3
Private investment (% %)	-16.5	35.6	-5.4	1.6
Public spending (% %)	**1.1**	**15.5**	**3.0**	**2.2**
Public consumption (% %)	7.6	12.2	3.3	3.0
Public investment (% %)	-15.5	26.0	2.2	0.0
Exchange rates (vs USD, EOP)	**3.60**	**4.04**	**4.00 – 4.10**	**4.10 – 4.20**
Inflation (% YoY, EOP)	**2.0**	**6.4**	**3.4**	**2.3**
Monetary policy rate (% EOP)	**0.25**	**2.50**	**4.50**	**4.50**
Fiscal balance (% GDP)	**-8.9**	**-2.6**	**-2.9**	**-2.5**
Balance of payments current account (% of GDP)	**0.6**	**-1.8**	**-1.7**	**-2.3**
Exports (Billions of USD)	42.7	61.7	60.6	60.0
Imports (Billions of USD)	34.7	46.9	47.9	49.7

(e) Estimated. (p) Forecast Year-end of forecasts: 21 January 2022.
Source: BBVA Research.

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Peru economic outlook

1Q22

Updated to: January 21

Creating Opportunities