



# BTMU Focus Latin America

## Peru: macroeconomic performance

(2015 GDP and Current Monthly Indicators)



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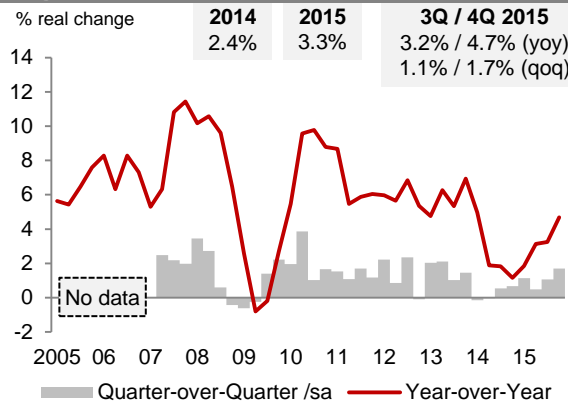
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# I) Peru: Growth Momentum (1)

■ An unexpected comeback: the Peruvian economy expanded by 3.3% in 2015, one of the highest in the region.

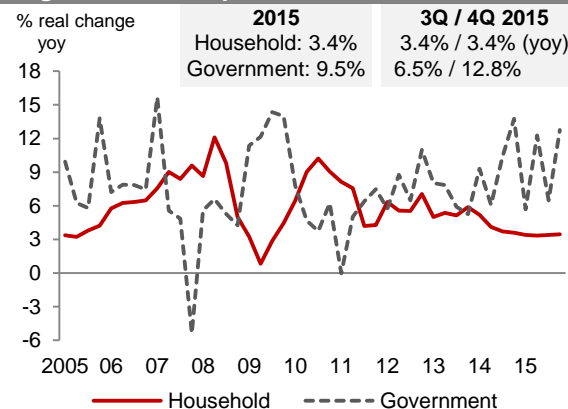
It was an unexpected but pleasant surprise: Peru's economy, which has been stuck in a subpar-growth mode since 1Q 2014, largely due to lower prices for metals, made a strong comeback in 2H 2015 and ended the year with an annual growth rate of 3.3%, the highest among members of the Pacific Alliance bloc. The boost to growth mostly stemmed from the mining sector, which grew by over 20% in 2H 2015, as new mines and expansion projects came into operation. In fact, the country saw its copper output balloon by 25.8% last year, which in turn paved the way for a rebound in exports. Yet not all is rosy. Household consumption, though remained growth-supportive throughout 2015, grew at the slowest pace since 2009. And gross fixed capital formation (GFCF), a proxy for overall investments, shrank for two years in a row as export-orientated firms (e.g., mining companies) cut capital spending to adapt to the adverse external environment. The message is clear: domestic demand was the soft spot last year and could remain so in 2016. This, naturally, casts doubts whether the recovery is on solid ground.

Figure 1: GDP Growth



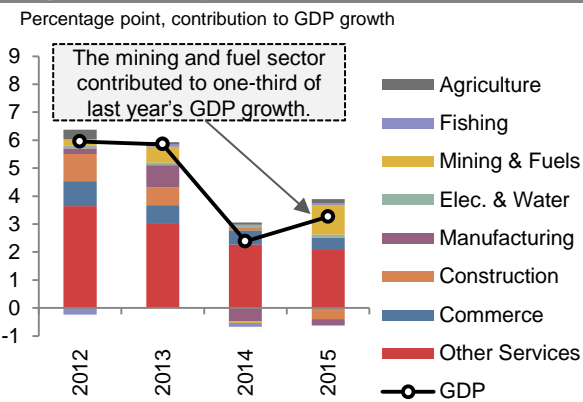
Source: Instituto Nacional de Estadística e Informática (INEI); Central Reserve Bank of Peru; BTMU

Figure 3: Consumption



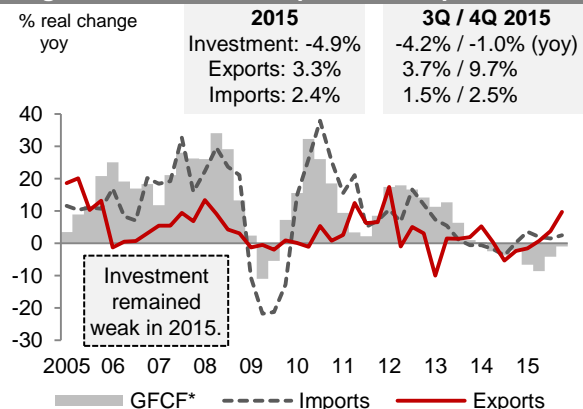
Source: Central Reserve Bank of Peru; BTMU

Figure 2: GDP by Sector



Source: INEI; BTMU

Figure 4: Investment, Exports and Imports



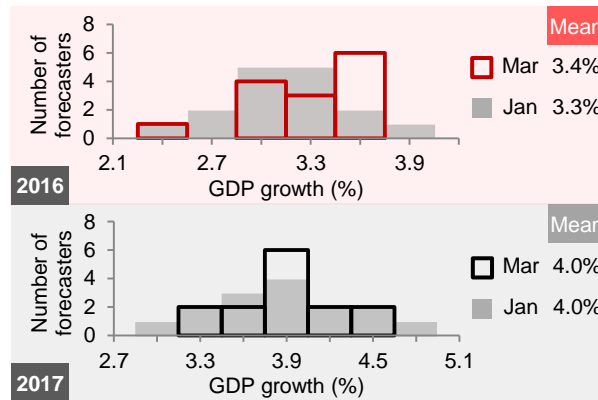
\*Gross Fixed Capital Formation  
Source: Central Reserve Bank of Peru; BTMU

# I) Peru: Growth Momentum (2)

■ Getting back some of its shine: Peru is expected to grow faster than most major Latin American economies.

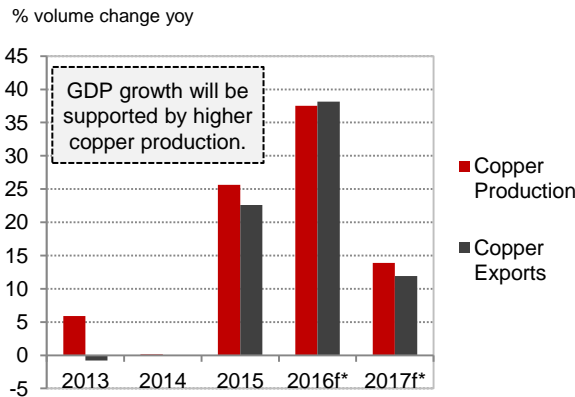
Peru's economic prospects look brighter than that of other major economies of the region, despite its high reliance on commodity revenues. GDP growth is expected to be above 3% in 2016, cemented by solid government consumption, an upturn in public investment as more infrastructure projects begin construction, and another sharp increase in copper production that will probably wind up stimulating exports. Better yet, should household consumption, and in particular private investment, start to gain speed during the second half of 2016, next year's rate of growth could potentially reach 4%. Thus, it seems the Andean economy will get some of its shine back. Still, caution is required because there are important downside risks to this outlook. First, the presidential election set for April 10 has become more and more messy, especially after the recent controversial disqualification of Julio Guzmán, who was polling in second place with 18% support, right behind the frontrunner, Keiko Fujimori, and followed by Pedro Pablo Kuczynski (continued on next slide).

Figure 5: GDP Growth (Private Forecasts)



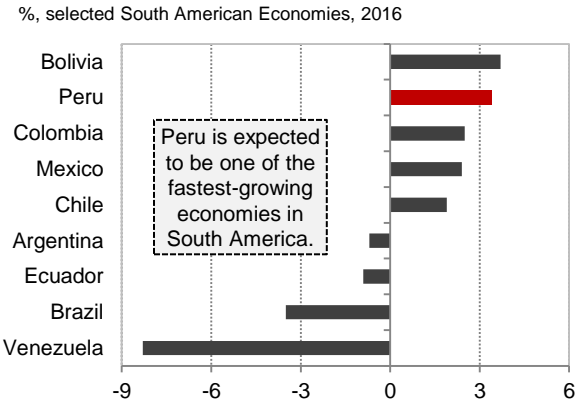
Source: Consensus Economics; BTMU

Figure 7: Copper Production and Exports



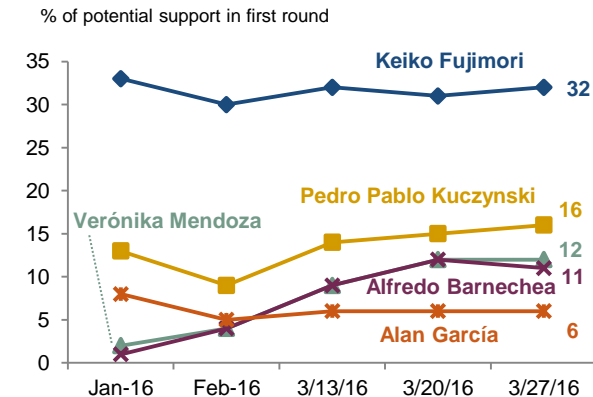
\*Forecasted by the Central Reserve Bank of Peru  
Source: Central Reserve Bank of Peru; BTMU

Figure 6: GDP Growth Ranking (Private Forecast)



Source: Consensus Economics; BTMU

Figure 8: 2016 Presidential Election Polls\*



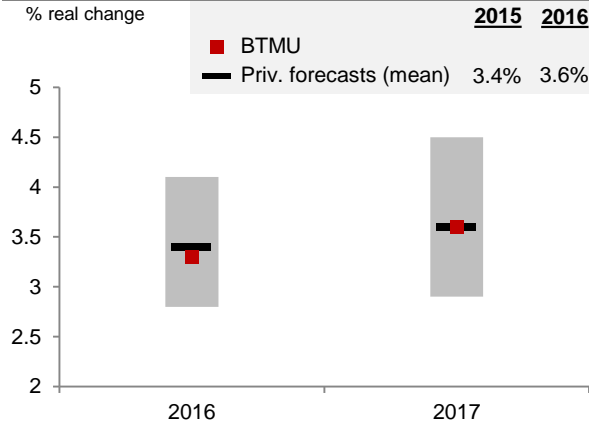
\*Margin of error +/-2.3 percentage points  
Source: Ipsos Perú; BTMU

# I) Peru: Growth Momentum (3)

Political uncertainty and external headwinds could intensify and weigh on an already feeble domestic demand.

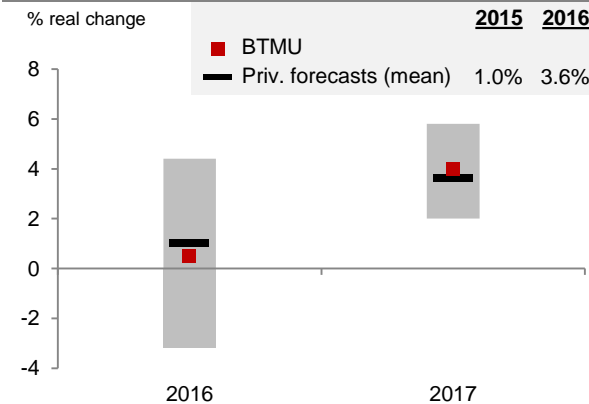
The latter candidates, with 48% combined support according to Ipsos, also face risk of disqualification amid vote-buying allegations. There is no doubt the country's political environment has become more uncertain and unstable. Worse yet, It could linger beyond the heated presidential election (the second round run-off should take place in early June), and prompt households and firms to further delay their decision to consume or invest, limiting the recovery in domestic demand. Second, headwinds coming from the external front (e.g., low commodity prices and tight financial conditions) could intensify and further weigh on exports and a domestic demand that is already expected to remain feeble this year. Household consumption, for instance, is unlikely to grow at a faster pace than in 2015 given the limiting factors: modest credit growth, less auspicious labor market conditions, and a weakening currency that will likely keep inhibiting imports of consumer goods for some time yet. True, public investment is expected to pick up this year, but given the current backdrop, private investment will likely sag again.

Figure 9: Private Consumption (Forecasts)



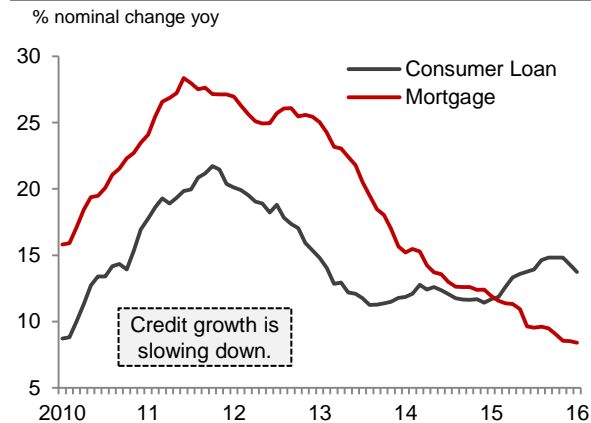
Source: Consensus Economics; BTMU

Figure 11: Gross Fixed Investment (Forecasts)



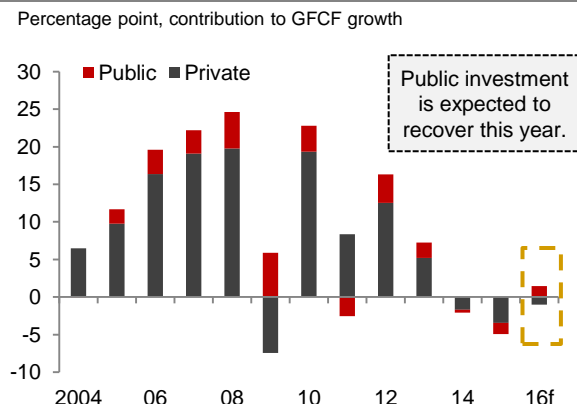
Source: Consensus Economics; BTMU

Figure 10: Outstanding Credit



Source: Central Reserve Bank of Peru; BTMU

Figure 12: Private and Public Investment\*



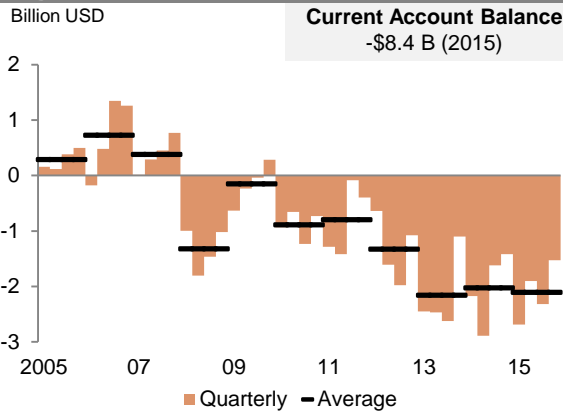
\*Using central bank's forecast for public investment  
Source: Central Reserve Bank of Peru; BTMU

## II) Peru: External Sector

■ **Current account deficit in 2015 remained large but stable: lower profit remittances offset larger trade deficit.**

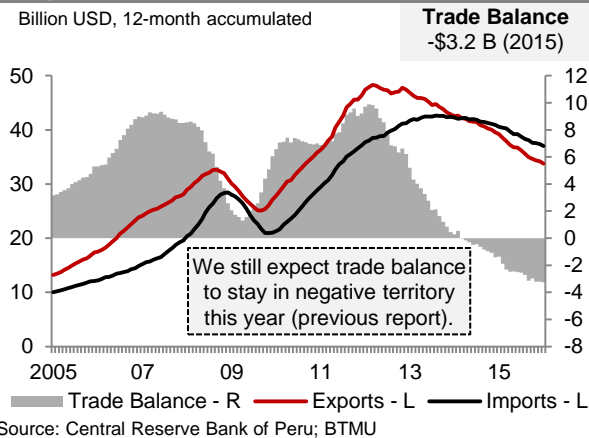
■ Peru posted a current-account deficit of \$8.4bn in 2015, representing around 4.4% of GDP, which is fairly large compared with that of Chile (0.9%) or Mexico (2.6%). The deficit, though, was similar to the previous two years', hinting it has stabilized and maybe bottomed out, despite the country's weak trade performance. In fact, Peru's trade deficit hit \$3.2bn last year, up from \$1.4bn in 2014, as soft commodity prices put a dent in exports earnings. But interestingly, as the windfalls dried up, mining companies also cut their profit remittances, which would up offsetting the rise in trade deficit. More intriguingly perhaps is the fact that Chile, a country that is more dependent on natural resources for their exports, posted a trade surplus of \$4.4bn in 2015. Yet the stark contrast does not imply Peru is in a worse position. Quite the opposite: Peruvian exports fell less than Chile's in nominal terms thanks to higher export volume of copper (expected to climb again this year); and the fall in imports was less severe because private consumption has been relatively more resilient to the external shocks.

**Figure 13: Current Account Balance**



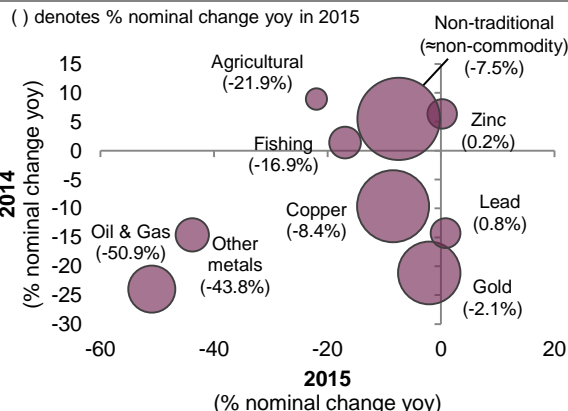
Source: Central Reserve Bank of Peru; BTMU

**Figure 14: Trade Balance, Exports and Imports**



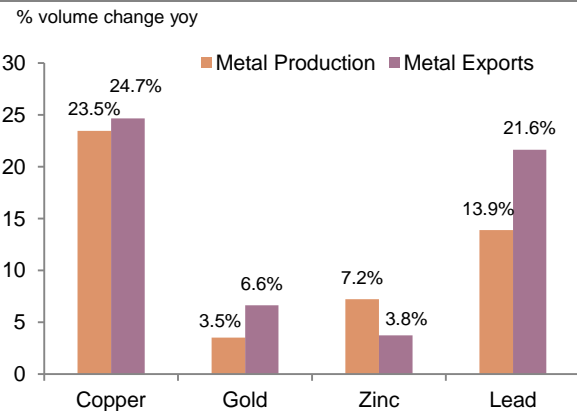
Source: Central Reserve Bank of Peru; BTMU

**Figure 15: Exports\***



\*Size of bubbles indicates share in total Peru's exports  
Source: Central Reserve Bank of Peru; BTMU

**Figure 16: Metal Production and Exports in 2015**



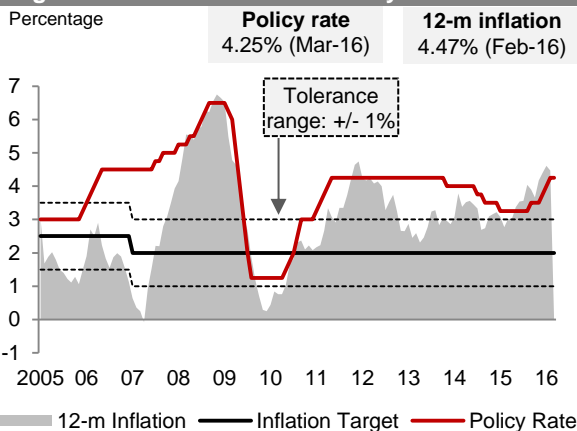
Source: Ministry of Energy and Mines of Peru; BTMU

# III) Peru: Prices and Monetary Policy

**Inflation is still entrenched above 4% and could end the year above the target range again.**

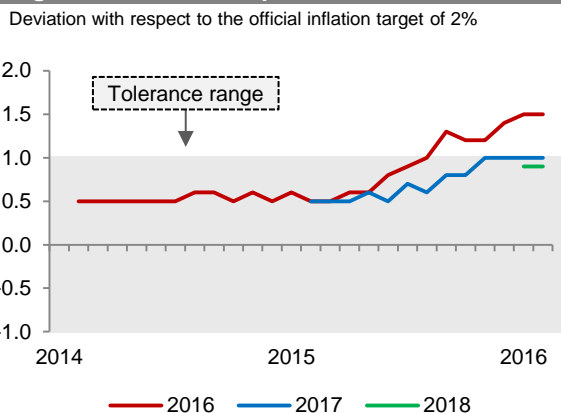
12-m inflation in Lima, a benchmark for the country, ended 2015 at 4.4%, well above the official's target range of 1%-3%. It was the 2<sup>nd</sup> consecutive year in which inflation ended above 3%. The BCRP, Peru's central bank, stressed two major forces behind the rise. First, unusual weather conditions, partly fueled by El Niño, disturbed the supply of some foodstuffs and drove food prices, which have a heavy weight of 37.8% in the consumer-price index, up by 5.4% last year. The other factor pushing inflation up was the depreciation of the Peruvian sol, which not only raised prices of imported products, but also caused electricity rates to shoot up rapidly. The BCRP sees inflation falling back to the target range at the end of 2016. That scenario, though possible, is probably on the optimistic side, as inflation is still entrenched above 4%. Yes, weather conditions are expected to get better this year and the sol might not depreciate much further. But inflation expectations are yet stuck above the target range despite the recent rate increases by the BCRP. Without more rate hikes, maybe inflation will stay above 3% for another year.

**Figure 17: CPI Inflation and Policy Rate**



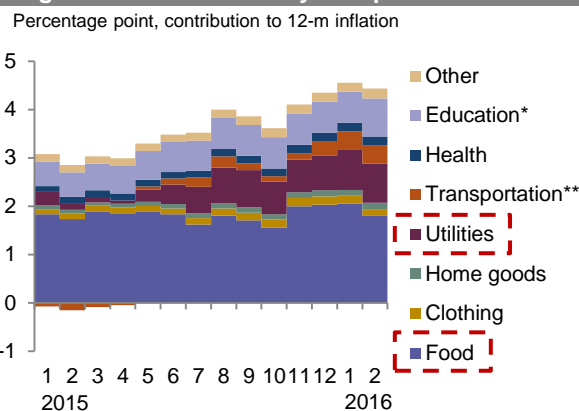
Source: INEI; Central Reserve Bank of Peru; BTMU

**Figure 19: Inflation Expectations**



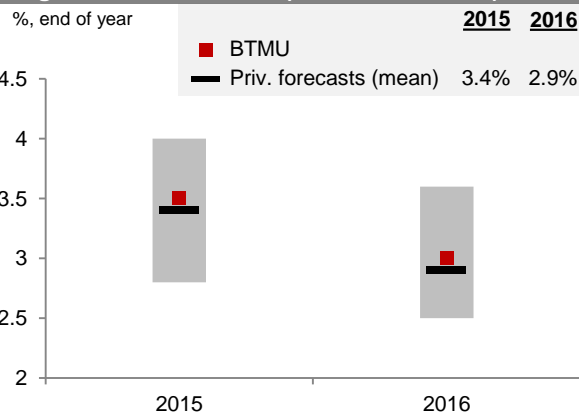
Source: Central Reserve Bank of Peru; BTMU

**Figure 18: CPI Inflation by Components**



\*includes culture; \*\*includes communication  
Source: Central Reserve Bank of Peru, BTMU

**Figure 20: CPI Inflation (Private Forecasts)**



Source: Consensus Economics; BTMU

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