



Summary

Macroeconomic policy has remained prudent and Peru's economy is likely to grow by 5.5%-6% a year in 2012 and 2013. The current account deficit is likely to grow to roughly 2.5% of GDP this year, but this deficit is more than covered by large inflows of FDI. Inflation has returned within the central bank's target range, after it increased above this range in 2011. Social tensions surrounding mining activity remain high, and resulted in the death of 5 people this year. It also resulted in the second reshuffle of the Humala government. However, after the second reshuffle president Humala's popularity has continued to fall.

Author: **Herwin Loman**
Country Risk Research
Economic Research Department
Rabobank Nederland

Contact details: P.O.Box 17100, 3500 HG Utrecht, The Netherlands
+31-(0)30-21-31105
H.Loman@rn.rabobank.nl

Peru			
National facts		Social and governance indicators	
Type of government	constitutional republic	Human Development Index (rank)	rank / total 80 / 187
Capital	Lima	Ease of doing business (rank)	43 / 185
Surface area (thousand sq km)	1,285	Economic freedom index (rank)	42 / 179
Population (millions)	30.0	Corruption perceptions index (rank)	80 / 183
Main religions	Roman Catholic (81.3%) Evangelical (12.5%)	Press freedom index (rank)	115 / 178
Main ethnic groups	Amerindian (45%) Mestizo (37%) White (15%)	Gini index (income distribution)	48.14
Head of State (president)	Ollanta Humala Tasso	Population below \$1.25 per day (PPP)	4.9%
Head of Government	Ollanta Humala Tasso	Foreign trade	
Monetary unit	nuevo sol (PEN)	2011	
Economy		2011	
Economic size		Main export partners (%)	
	<i>bn USD</i>	<i>% world total</i>	<i>Main import partners (%)</i>
Nominal GDP	177	0.26	China 15
Nominal GDP at PPP	302	0.38	US 25
Export value of goods and services	51	0.23	US 13
IMF quotient (in mln SDR)	638	0.29	Canada 10
Economic structure		Main export products (%)	
	<i>2011</i>	<i>5-year av.</i>	
Real GDP growth	6.9	7.2	Copper 23
Agriculture (% of GDP)	8	7	Gold 22
Industry (% of GDP)	34	36	Fishmeal 5
Services (% of GDP)	58	56	Zinc 3
Standards of living		Main import products (%)	
	<i>USD</i>	<i>% world av.</i>	
Nominal GDP per head	5819	54	Intermediate goods 49
Nominal GDP per head at PPP	9947	80	Capital goods 32
Real GDP per head	3953	48	Consumer goods 18
		Openness of the economy	
		Export value of G&S (% of GDP) 29	
		Import value of G&S (% of GDP) 25	
		Inward FDI (% of GDP) 4.6	

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank.

Introduction and update

After growing by 8.8% in 2011 and 6.9% in 2011, Peru's economic growth rate is likely to slow somewhat. Nevertheless, the economy is likely to grow by a still decent 5.5%-6% a year in 2012 and 2013. Investment growth, which recovered in 2010, has remained strong. Meanwhile, employment growth has remained vigorous as well, which is very important, as 28% of the population remains below Peru's poverty line, even as the poverty rate has fallen rapidly in recent years. Partially on the back of capital imports related to investment, the current account deficit is likely to widen to 2.5% of GDP this year, but this deficit is more than covered by FDI inflows equal to 5% of GDP. Most FDI continues to go to the mining and oil and gas sectors, but FDI in other sectors has increased. Peru's economy remains partially dollarized. Meanwhile, foreign exchange reserves are expected to grow to USD 59.5bn in 2012, and will thus cover 15 months of imports and surpass Peru's USD 39bn foreign debt. This greatly reduces balance of payments risk. The central bank has maintained its main policy rate at 4.25% since May 2011. Inflation increased above its 1-3% target range in 2011, but has fallen within the range afterwards and is now expected to stay within this range in the near future. Peru's President Ollanta Humala has followed a centrist and pragmatic course. Peru is likely to post a fiscal surplus this year and is likely to continue to do so in the coming years. Meanwhile, the already low public debt ratio is expected to fall. The share of debt issued in local currency has continued to grow and stands at 45% now.

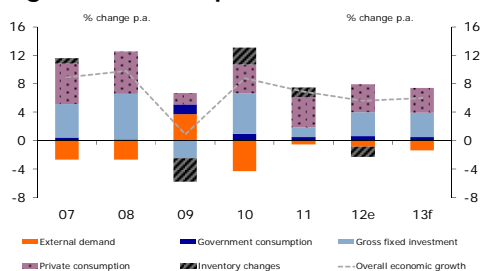
Large mining projects remain controversial

Peru continues to be affected by social tensions related to large scale mining projects. The most important controversial project is the Minas Conga project. Since October 2011, there have been large scale protests against this USD 5bn project, which faced a lot of criticism as local communities fear that the project will destroy their water supplies. These protests escalated in July 2012 and resulted in the death of 5 people. In early September, the state of emergency that was in place since July 2012 expired, but tensions remain high. Newmont, one of the two shareholders in the project, has stated that it wants to proceed with the project, but it is unclear to what extent the work on the project can be finished. However, there are many other large mining projects that do not face protests. Although the recent protests are likely to slow new investment in the mining sector, overall investment is likely to remain high.

The biggest constraint to reducing social tensions is institutional. Although local governments receive large transfers from the central government, they are often unable to spend this money on infrastructure and social projects, as they lack the capacity to manage such projects. This does not only limit the ability of the government to reduce social tensions, it also constrains Peru's long term development, as lack of infrastructure and educated workers are already important factors that constrain economic growth.

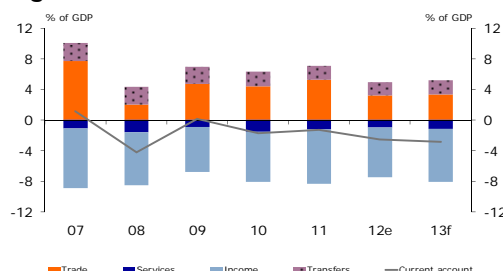
The large scale resistance has had political repercussions. In July 2012 president Humala implemented the second reshuffle of his government. He fired his prime minister, Oscar Valdés, as he had become controversial due to the hardline approach he took against the mining protests. His successor is Juan Jiménez, a human rights lawyer and former minister of justice. However, Humala's hopes that this reshuffle would help to boost his popularity do not seem to materialize. His popularity has continued to decrease gradually and now stands at a low 40%. It seems that growing concerns about security related to recent outbreaks of violence by the Maoist Shining Path guerrilla group is also hurting Humala's popularity. The Shining Path staged an insurgency during the 1980s, but the movement right now does not resemble its former self and it is not a national threat. However, remnants of the group still fight against security forces in some parts of the countryside.

Figure 1: Growth performance



Source: EIU

Figure 2: Current account



Source: EIU

Peru							
Selection of economic indicators	2007	2008	2009	2010	2011	2012e	2013f
<i>Key country risk indicators</i>							
GDP (% real change pa)	8.9	9.8	0.9	8.8	6.9	5.6	6.0
Consumer prices (average % change pa)	1.8	5.8	2.9	1.5	3.4	3.6	3.1
Current account balance (% of GDP)	1.1	-4.2	0.2	-1.7	-1.3	-2.5	-2.9
Total foreign exchange reserves (m USD)	26857	30272	32013	42648	47206	59550	64850
<i>Economic growth</i>							
GDP (% real change pa)	8.9	9.8	0.9	8.8	6.9	5.6	6.0
Gross fixed investment (% real change pa)	22.6	27.1	-9.2	23.2	5.1	12.5	11.8
Private consumption (real % change pa)	8.3	8.7	2.4	6.0	6.4	5.9	5.3
Government consumption (% real change pa)	4.5	2.1	16.5	10.0	4.8	6.2	5.8
Exports of G&S (% real change pa)	6.9	8.2	-3.2	1.3	8.8	5.3	5.3
Imports of G&S (% real change pa)	21.4	20.1	-18.6	24.0	9.8	8.4	10.6
<i>Economic policy</i>							
Budget balance (% of GDP)	3.2	2.4	-1.8	-0.4	1.9	0.9	1.5
Public debt (% of GDP)	27	23	25	22	20	18	16
Money market interest rate (%)	5.8	7.3	2.1	3.8	5.1	5.1	5.4
M2 growth (% change pa)	24	23	3	22	10	11	13
Consumer prices (average % change pa)	1.8	5.8	2.9	1.5	3.4	3.6	3.1
Exchange rate LCU to USD (average)	3.1	2.9	3.0	2.8	2.8	2.7	2.6
Recorded unemployment (%)	7.0	8.1	8.9	6.6	7.9	7.7	7.8
<i>Balance of payments (m USD)</i>							
Current account balance	1220	-5318	211	-2625	-2267	-4860	-6190
Trade balance	8287	2569	5951	6750	9302	6230	7250
Export value of goods	27882	31018	26962	35565	46268	47380	51810
Import value of goods	19595	28449	21011	28815	36967	41150	44570
Services balance	-1187	-2056	-1144	-2345	-2132	-1850	-2540
Income balance	-8374	-8774	-7484	-10055	-12636	-12660	-14950
Transfer balance	2494	2943	2887	3026	3200	3430	4050
Net direct investment flows	5424	6188	5178	7973	8006	9520	10470
Net portfolio investment flows	2637	1947	-5165	292	3665	1590	2340
Net debt flows	4205	1454	1862	5975	733	1670	1380
Other capital flows (negative is flight)	-3141	-802	-110	-632	-5422	4440	-2800
Change in international reserves	10345	3470	1976	10983	4716	12370	5210
<i>External position (m USD)</i>							
Total foreign debt	32073	34559	36393	36271	37393	38910	40150
Short-term debt	5334	5420	4731	6055	5119	5660	6200
Total debt service due, incl. short-term debt	10613	10625	9813	11103	11468	9880	9310
Total foreign exchange reserves	26857	30272	32013	42648	47206	59550	64850
International investment position	-31164	-30245	n.a.	n.a.	n.a.	n.a.	n.a.
Total assets	47615	48253	n.a.	n.a.	n.a.	n.a.	n.a.
Total liabilities	78779	78498	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Key ratios for balance of payments, external solvency and external liquidity</i>							
Trade balance (% of GDP)	7.7	2.0	4.7	4.4	5.3	3.2	3.3
Current account balance (% of GDP)	1.1	-4.2	0.2	-1.7	-1.3	-2.5	-2.9
Inward FDI (% of GDP)	5.1	5.5	4.4	5.3	4.6	5.0	4.9
Foreign debt (% of GDP)	30	27	29	24	21	20	19
Foreign debt (% of XGSIT)	91	88	104	83	68	68	64
International investment position (% of GDP)	-29.1	-23.8	n.a.	n.a.	n.a.	n.a.	n.a.
Debt service ratio (% of XGSIT)	30	27	28	26	21	17	15
Interest service ratio incl. arrears (% of XGSIT)	7	5	6	6	1	1	1
FX-reserves import cover (months)	13.5	10.6	14.9	14.7	13.0	14.9	14.9
FX-reserves debt service cover (%)	253	285	326	384	412	603	697
Liquidity ratio	150	135	164	163	154	168	169

Source: EIU

Disclaimer

This document is issued by Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A. incorporated in the Netherlands, trading as Rabobank Nederland, and regulated by the FSA. The information and opinions contained herein have been compiled or arrived at from sources believed to be reliable, but no representation or warranty, express or implied, is made as to their accuracy or completeness. It is for information purposes only and should not be construed as an offer for sale or subscription of, or solicitation of an offer to buy or subscribe for any securities or derivatives. The information contained herein is not to be relied upon as authoritative or taken in substitution for the exercise of judgement by any recipient. All opinions expressed herein are subject to change without notice. Neither Rabobank Nederland, nor other legal entities in the group to which it belongs accept any liability whatsoever for any direct or consequential loss howsoever arising from any use of this document or its contents or otherwise arising in connection therewith, and their directors, officers and/or employees may have had a long or short position and may have traded or acted as principal in the securities described within this report, or related securities. Further it may have or have had a relationship with or may provide or have provided corporate finance or other services to companies whose securities are described in this report, or any related investment. This document is for distribution in or from the Netherlands and the United Kingdom, and is directed only at authorised or exempted persons within the meaning of the Financial Services and Markets Act 2000 or to persons described in Part IV Article 19 of the Financial Services and Markets Act 2000 (Financial Promotions) Order 2001, or to persons categorised as a "market counterparty or intermediate customer" in accordance with COBS 3.2.5. The document is not intended to be distributed, or passed on, directly or indirectly, to those who may not have professional experience in matters relating to investments, nor should it be relied upon by such persons. The distribution of this document in other jurisdictions may be restricted by law and recipients into whose possession this document comes from should inform themselves about, and observe any such restrictions. Neither this document nor any copy of it may be taken or transmitted, or distributed directly or indirectly into the United States, Canada, and Japan or to any US-person. This document may not be reproduced, distributed or published, in whole or in part, for any purpose, except with the prior written consent of Rabobank Nederland. By accepting this document you agree to be bound by the foregoing restrictions.