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WORKS

Peru: Beset by Countervailing Winds

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Estudios Económicos – Scotiabank (Peru)

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- Strong Q4 recovery trend
- Metal prices
- Strong macro balances
- Political turbulence
- Second COVID-19 wave
- Elections

Macro Growth & Balances	2020	2021
GDP Growth	-11.1	8.7
Domestic Demand	-9.8	7.8
Private Consumption	-8.7	6.8
Private Investment	-17.2	15.1
Public Investment	-17.7	13.8
Unemployment (% GDP)	13.8	10.0
Inflation	2.0	2.6
Reference rate	0.25	0.25
Fiscal Balance (% GDP)	-8.9	-5.4
Trade Balance	7,750	12,523
NIR (USD mn)	74,707	77,000

2021 GDP growth, y/y

- Consensus 9.5%
- Market range 6%–12%

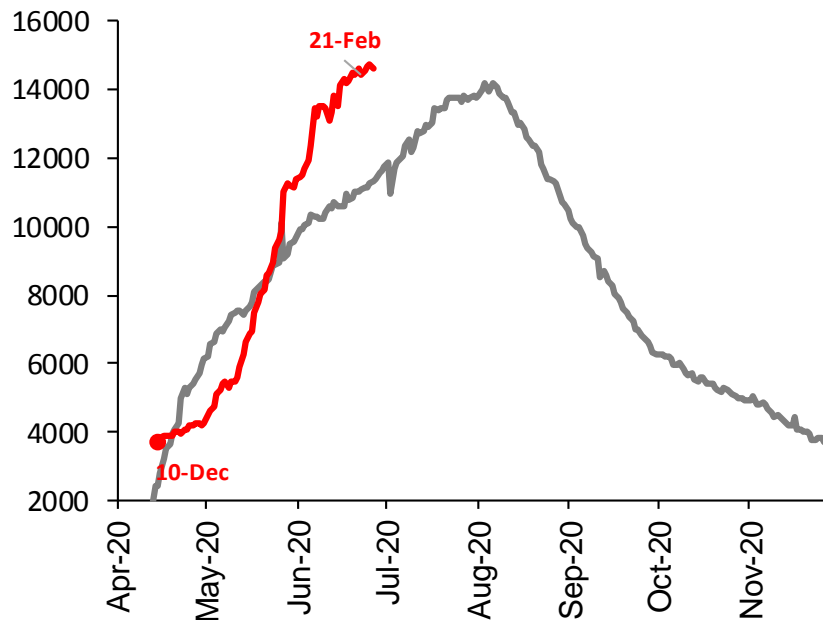
Source: BCRP; Prepared by Scotiabank Peru

- Mortality per million: 1,200 (the world average is 280 per million).
- Timing of second-wave restrictions much later than in first wave.

Status of vaccines

- Procurement of 85 mn doses.
- 1 mn have arrived, 2 mn in March, 10 mn by June.
- Government goal: 15 mn vaccinated by July.
- 160,000 health professionals have been vaccinated (0.5% of the population).

COVID-19 Hospital Patients



Inoculation Phases

1. Health professionals, domestic security 1.7mn
2. People over 60 or with health issues, indigenous communities 6.0mn
3. Ages 18 to 59 16.8mn

New measures restrict mobility, not production

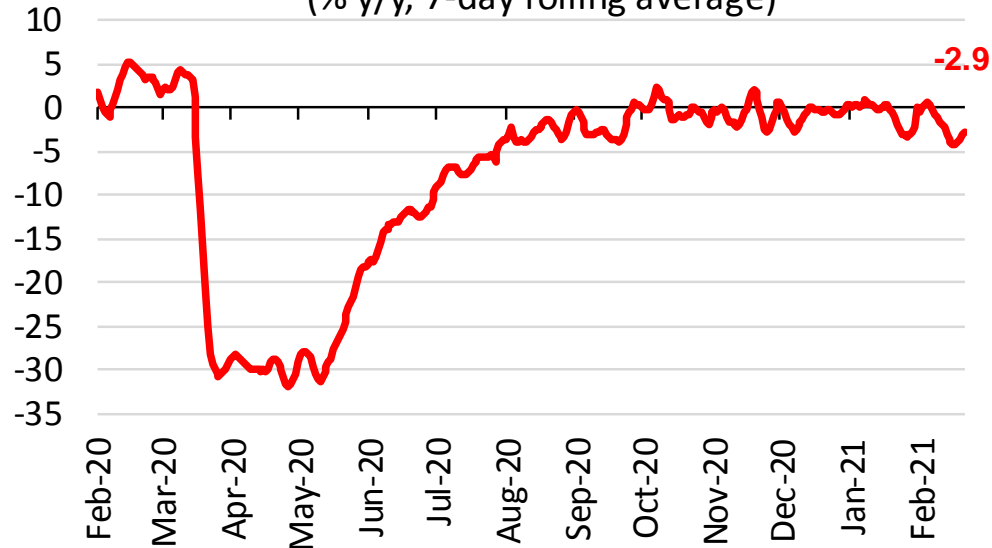
- 95% of the economy allowed to operate, versus 44% at height of 2020 lockdown.
- Our GDP growth forecast of 8.7% y/y for 2021 in line with 6.8 weeks of restrictions.
- New support measures represent 2.5% of GDP in resources for households.
- Difference between electricity demand and mobility trends: government restrictions have affected mobility, but not production.

Support measures:

- PEN 600 transfer to over four million families.
- One-month postponement on the payment of income, sales, and other taxes.
- PEN 2 bn small-business support program (similar to Reactiva), and a PEN 0.2 bn tourism support program.

Electricity Demand Growth

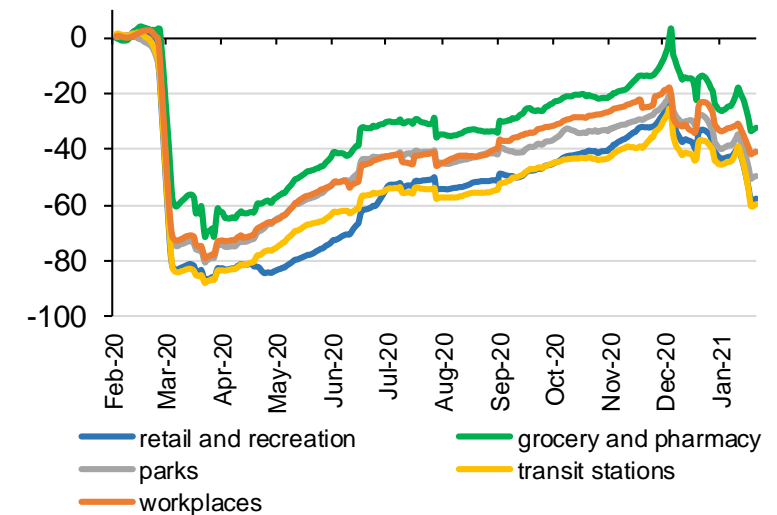
(% y/y, 7-day rolling average)



Source: COES Prepared by: EstudiosEconómicos Scotiabank Perú

Google Mobility Trends

(% change compared to baseline)



Baseline: Dayli Average (Jan 3–Feb 6, 2020)

Source: Google

To Jan 24

Prepared by Scotiabank Research Department



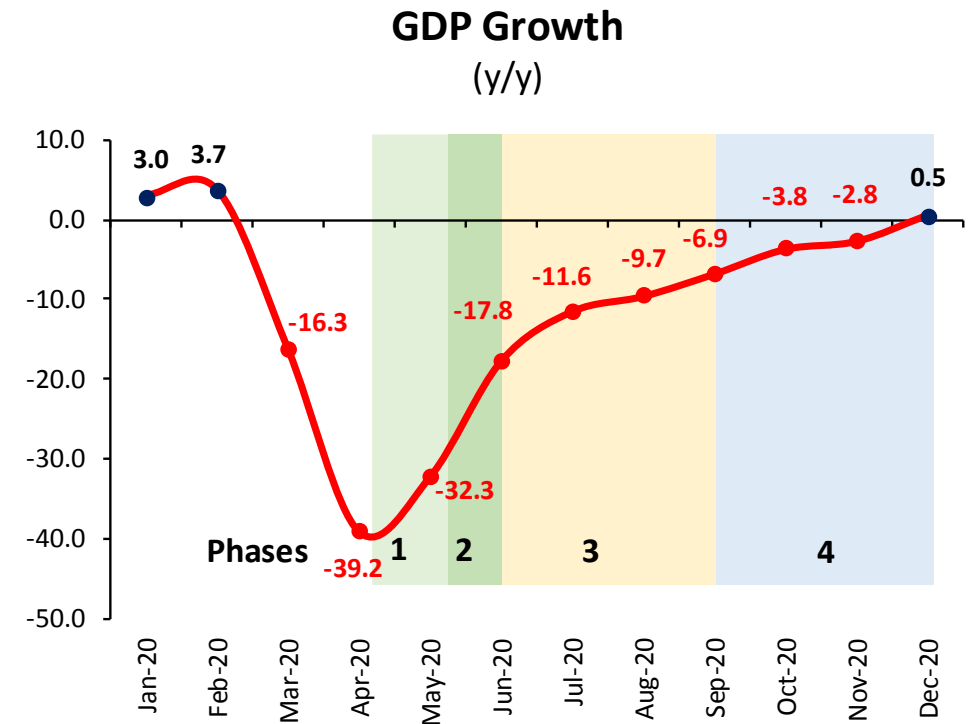
2020: the recovery was better than expected

Q4 especially strong

- Domestic demand did not contract.
- Surprisingly strong private investment turnaround.
- December: positive growth ahead of expectations.
 - 6 of 12 major sectors rose (fishing, construction, resource processing, government services, telecom, and financial services).

GDP Demand Growth	2020	
	Q4	FY
GDP	-1.7	-11.1
Domestic Demand	0.0	-9.8
Private Consumption	-1.5	-8.7
Govt Current Spending	21.7	7.5
Private Investment	9.4	-17.2
Public Investment	8.6	-17.7
Exports Volume	-11.2	-20.0
Imports Volume	-5.6	-15.6

Source: BCRP; Prepared by Scotiabank Peru

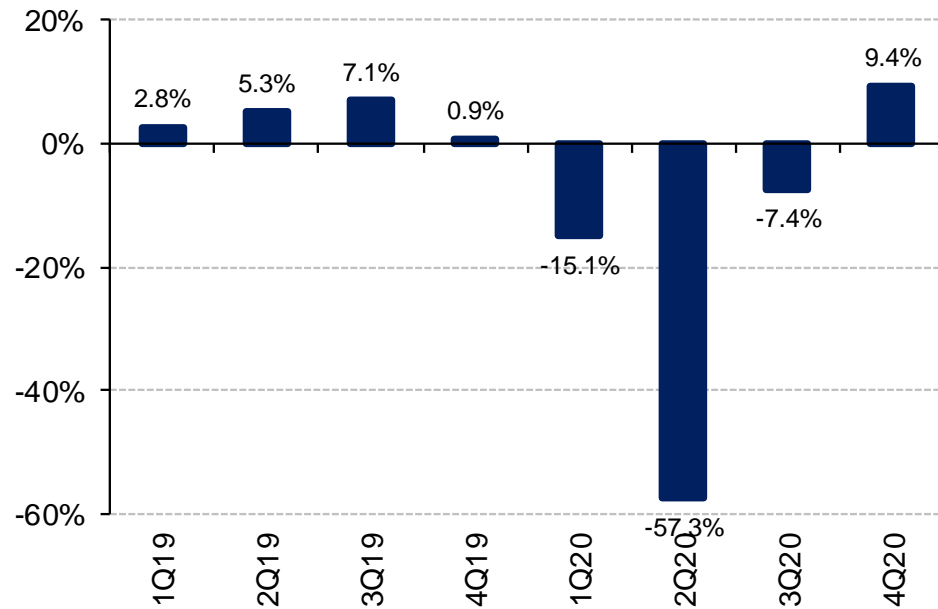


Sources: BCRP; Prepared by Scotiabank Peru.

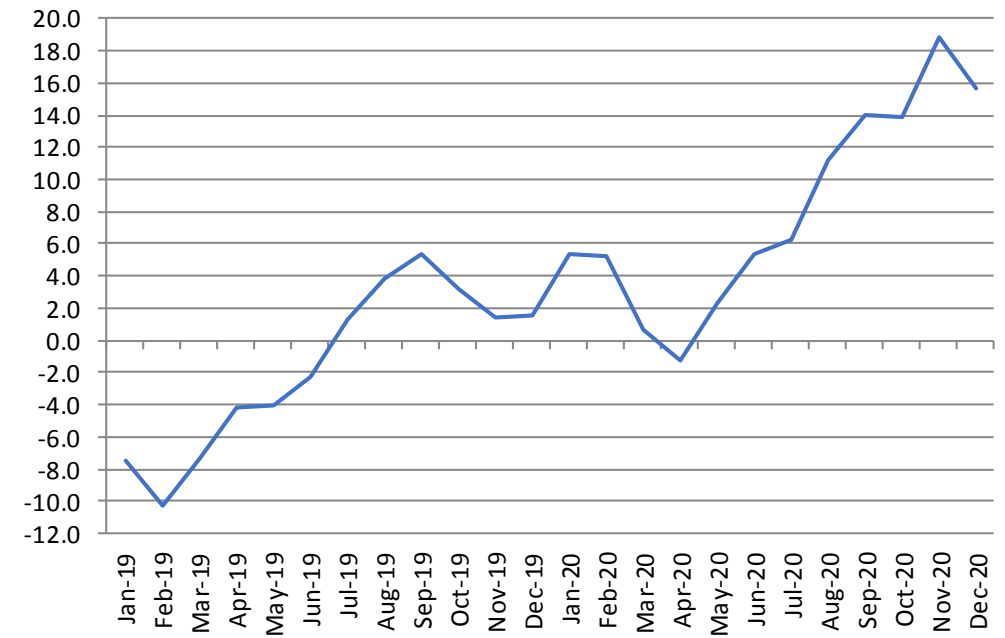
An encouraging improvement in private demand—investment

- Technological transformations.
- Booming real estate.
- Companies adapting to new consumption patterns.
- Terms of trade (high metal prices) have traditionally given strong support to macro accounts and business confidence.

Private Investment Growth
(y/y)



Terms of Trade
(y/y, %)



Source: BCR Elaboration: Research Department-Scotiabank Peru

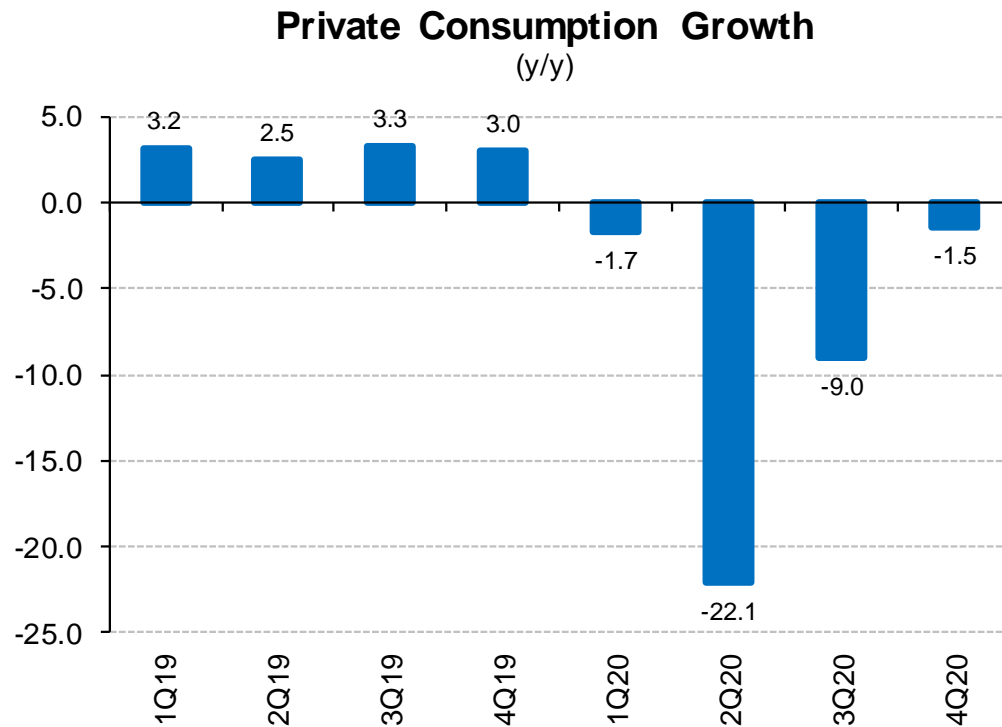
Source: BCRP; Sunat Prepared by: Research Department-
Scotiabank Peru

Infrastructure investments are slow, but progressing

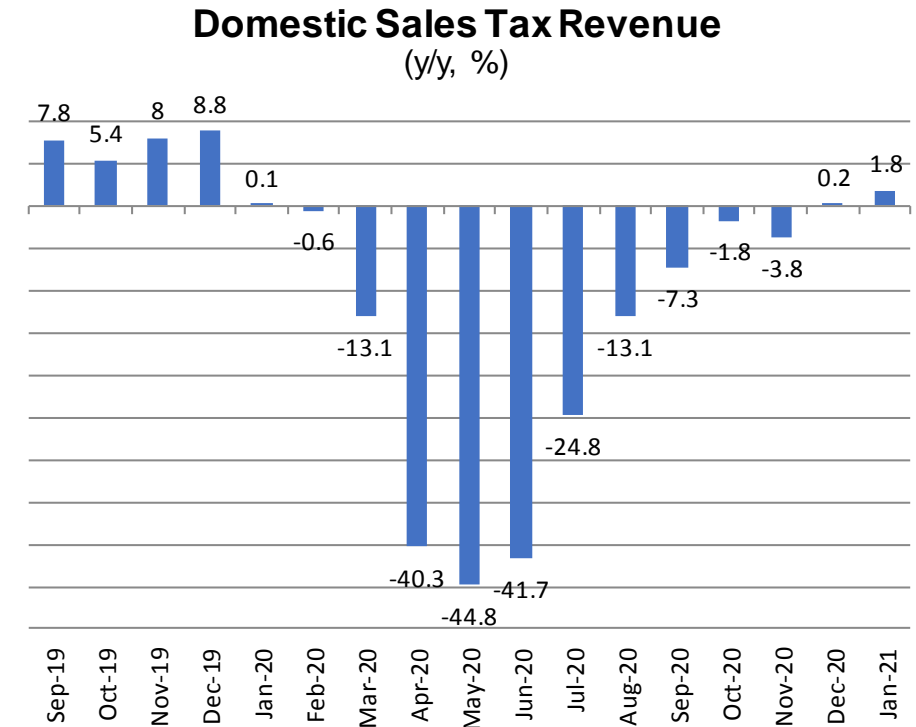
- Ancón Industrial Park: USD 750 mn – tender pending.
- Chancay Port – phase 1: USD 1.2 mn – beginning construction.
- Lima Metro Line 2: USD 5.3 bn – under construction.
- Lima airport: USD 1.2 bn – under construction.
- 9 Ports: USD 420 mn – (Salaverry, San Martin, others).
- Reconstruction North: PEN 22.7 bn (USD 6.2 bn) – G2G UK.
- Hospitals: PEN 1 bn (USD 280 mn) – G2G France.
- Projects on agenda for tender in 2021: PEN 4.3 bn (USD 1.2 bn).

An encouraging improvement in private demand—consumption

- Government measures (5.5% of GDP).
- Rebound in employment.
- New (virtual) sources of service income.
- Sales tax revenue above pre-COVID-19 levels reflects robust sales, but also new activities and the formalization of informal sales through digitalization.



Source: BCRP; Prepared by: Research Department-Scotiabank Peru



Source: BCRP; Sunat Prepared by: Research Department-Scotiabank Peru

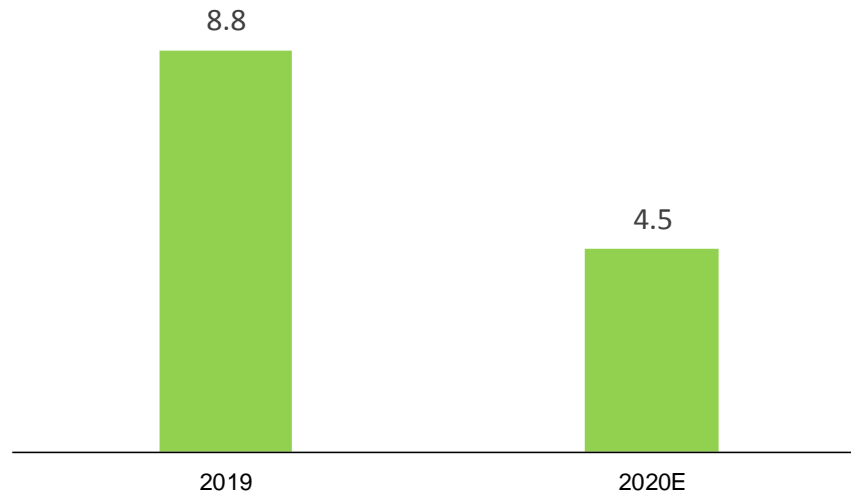
Resources available to boost domestic demand

In 2020, government transfers and access to savings helped sustain consumption.

Resources that will be available in 2021: +5% of GDP.

- Household deposits at banks up by PEN 30 bn (15%) between March and December 2020.
 - lower spending on restricted activities + resources from AFP withdrawals + Reactiva.
- Nearly PEN 19 bn in pension withdrawals, government transfers.

Peru: Spending in restaurants
(in US\$ billions)



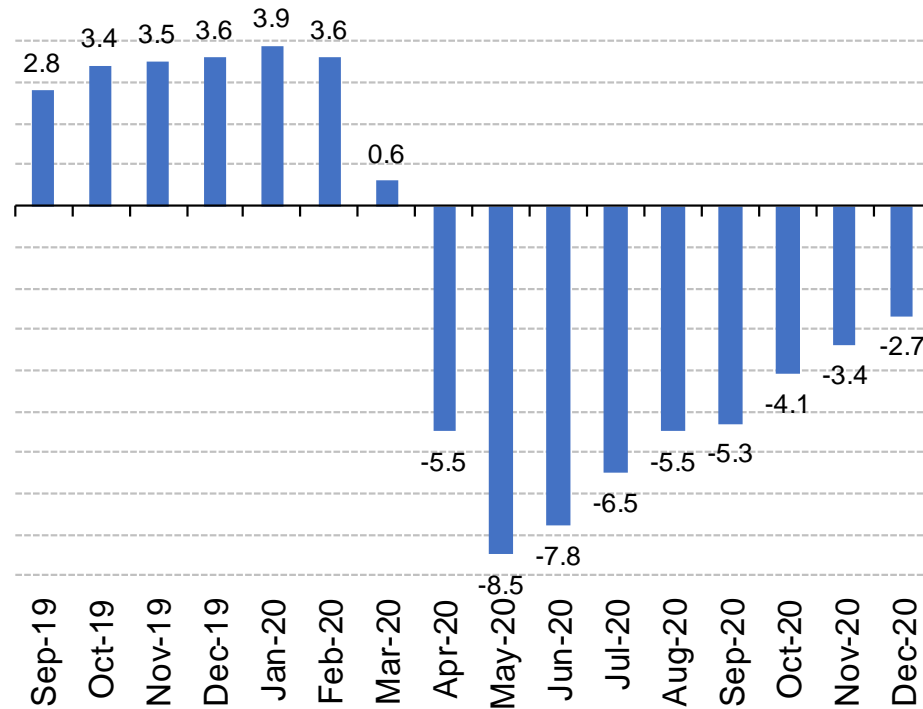
Source: BCRP, Research Department-Scotiabank Peru

Resources Available for Households

• AFP withdrawals in 2020:	S/ 24.3bn
• CTS withdrawals in 2020:	S/ 4.5 bn
• Household Support funds 2020:	S/ 13 bn
Total 2020:	S/ 41.8 bn (5.5% of GDP)
• AFP withdrawals 2021:	S/ 15.9 bn
• ONP Support funds:	S/ 0.5 bn
• Household Support funds 2021	S/ 2.4 bn
Total 2021:	S/ 18.8bn (2.5% of GDP)

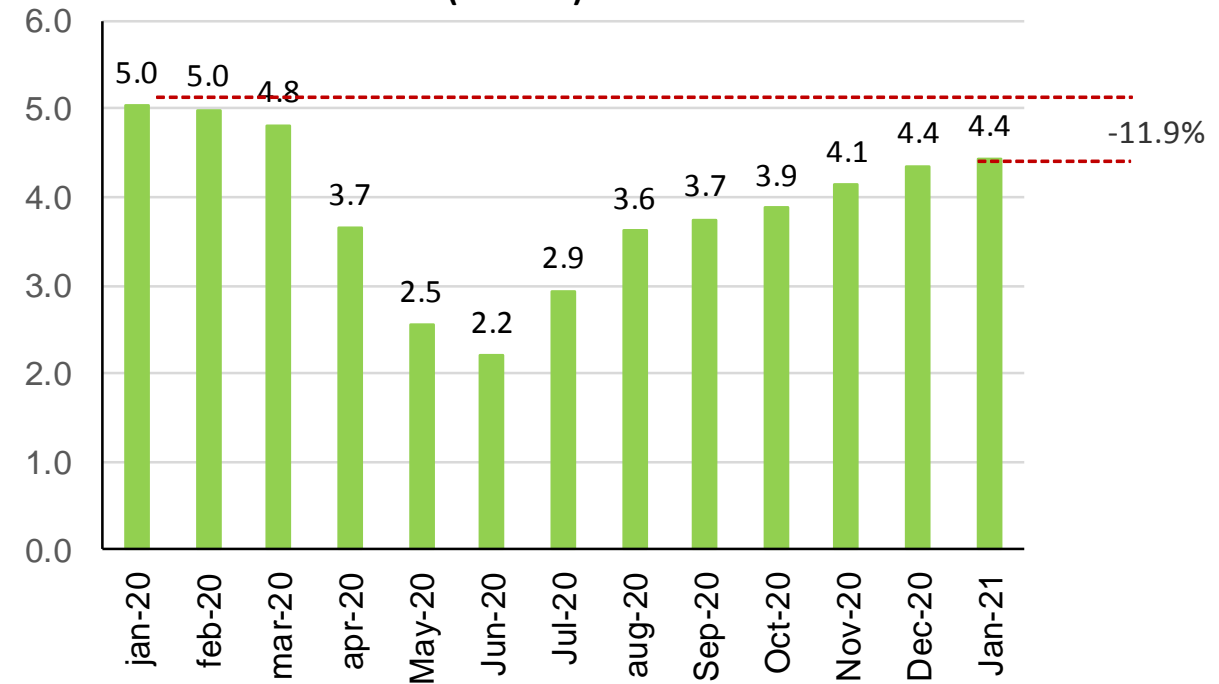
Employment is also recovering, albeit still under past levels

Formal Jobs Growth- Sunat Digital Payroll
(y/y, %)



Source: BCRP, Sunat Prepared by: Research Department-Scotiabank Peru

Employment in Lima
(millions)

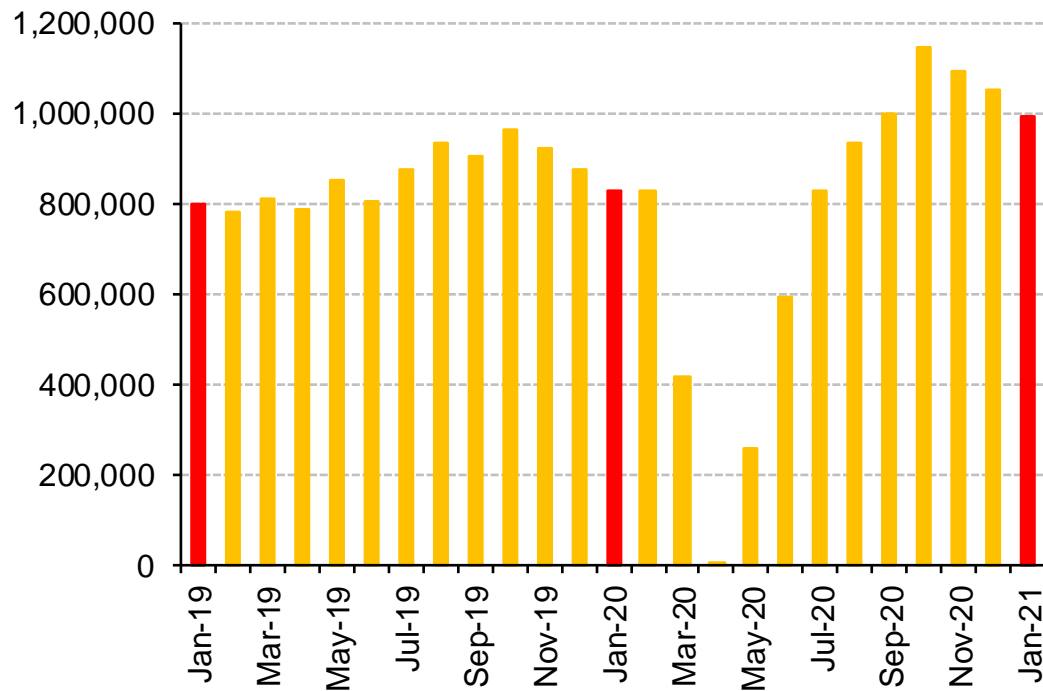


Source: INEI Elaboration: Research Department -Scotiabank Perú

Construction is booming

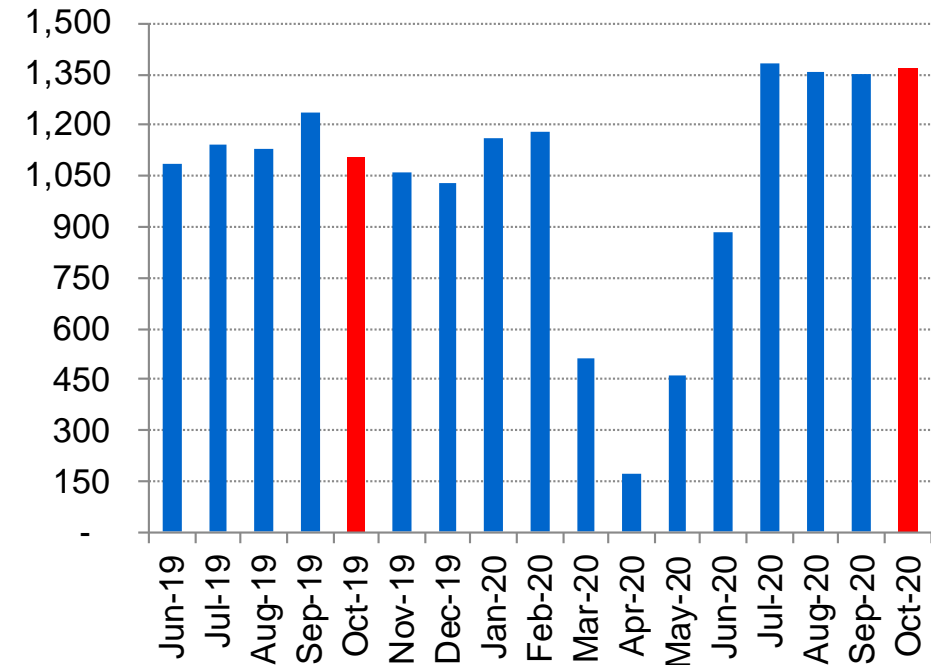
- Cement sales have risen 19%–20% y/y each month from October 2020 to January 2021.
- Construction GDP is currently significantly above pre-COVID-19 levels.
- Part of construction growth is government spending, but most involves a booming real estate market.

Cement sales
(metric tons)



Sources: Asocem Prepared by: Scotiabank Peru.

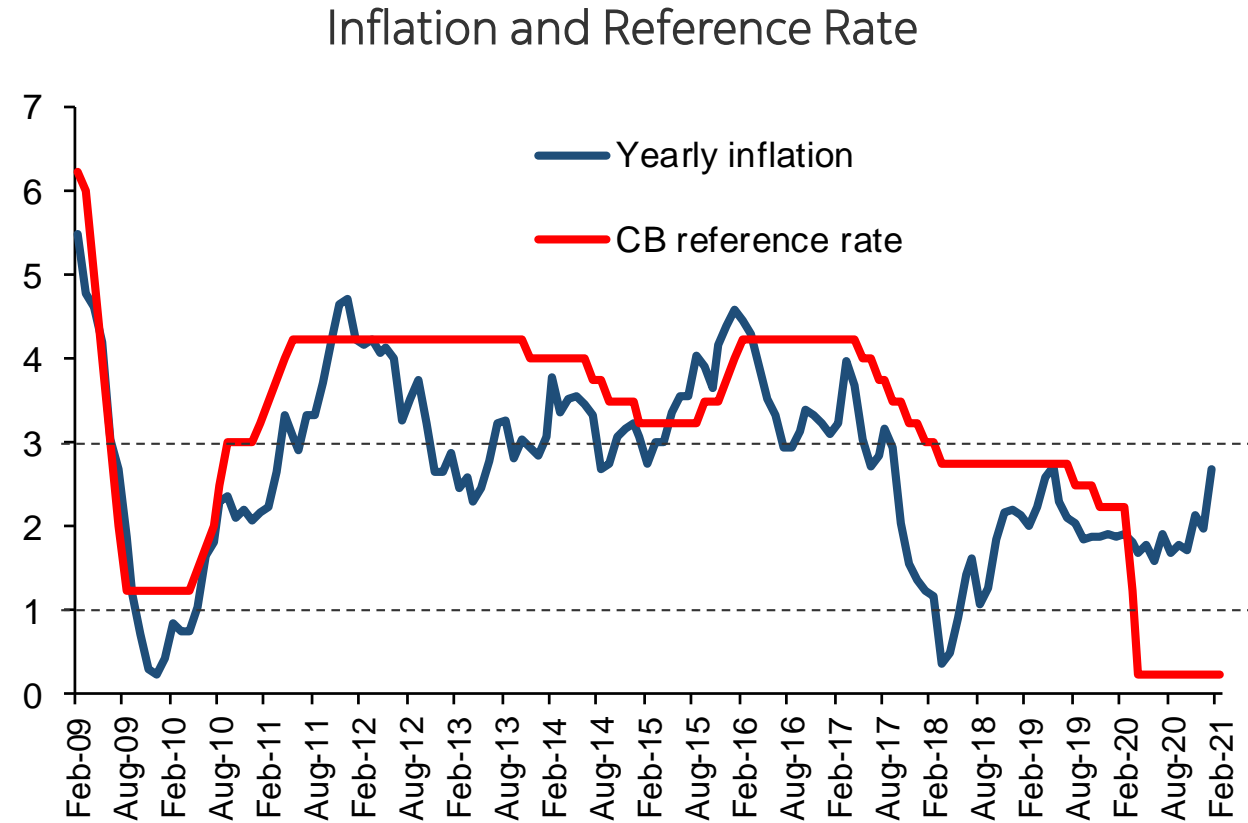
Lima new home sales
(units)



Source: Asociación de Empresas Inmobiliarias
Prepared by Scotiabank Research Department

Low interest rates is probably the most likely source

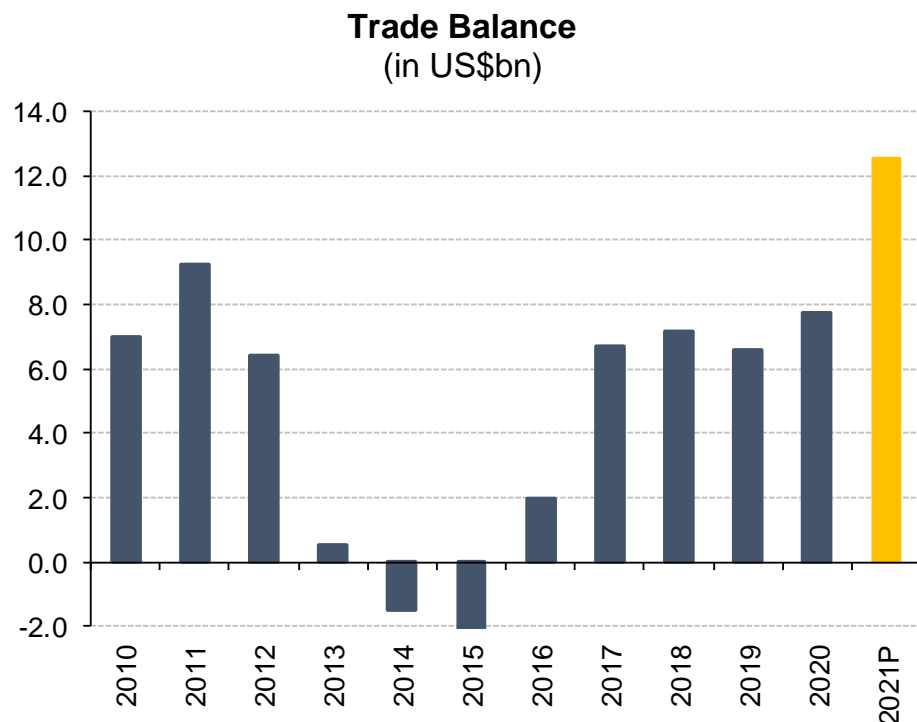
The reference rate will remain low well into 2022, although rising inflation merits monitoring.



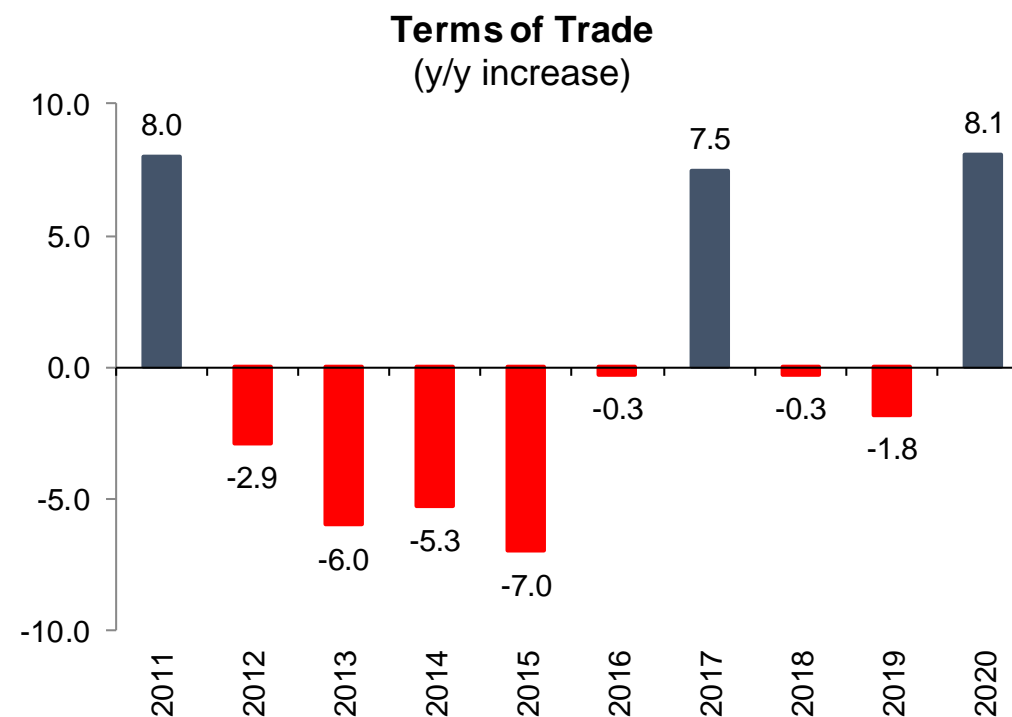
Source: BCRP. Scotiabank Peru

Metal prices are changing external outlook

- External accounts are very, very strong, and are set to get even stronger in 2021 as metal prices move higher.
- 2020 Current Account: 0.5% of GDP.
- Net international reserves: USD 74.7 bn, or 25 months of imports.
- Every one cent increase raises exports by USD 50 mn.
- A copper price of USD 4.00/lb would increase exports by over USD 3 bn.



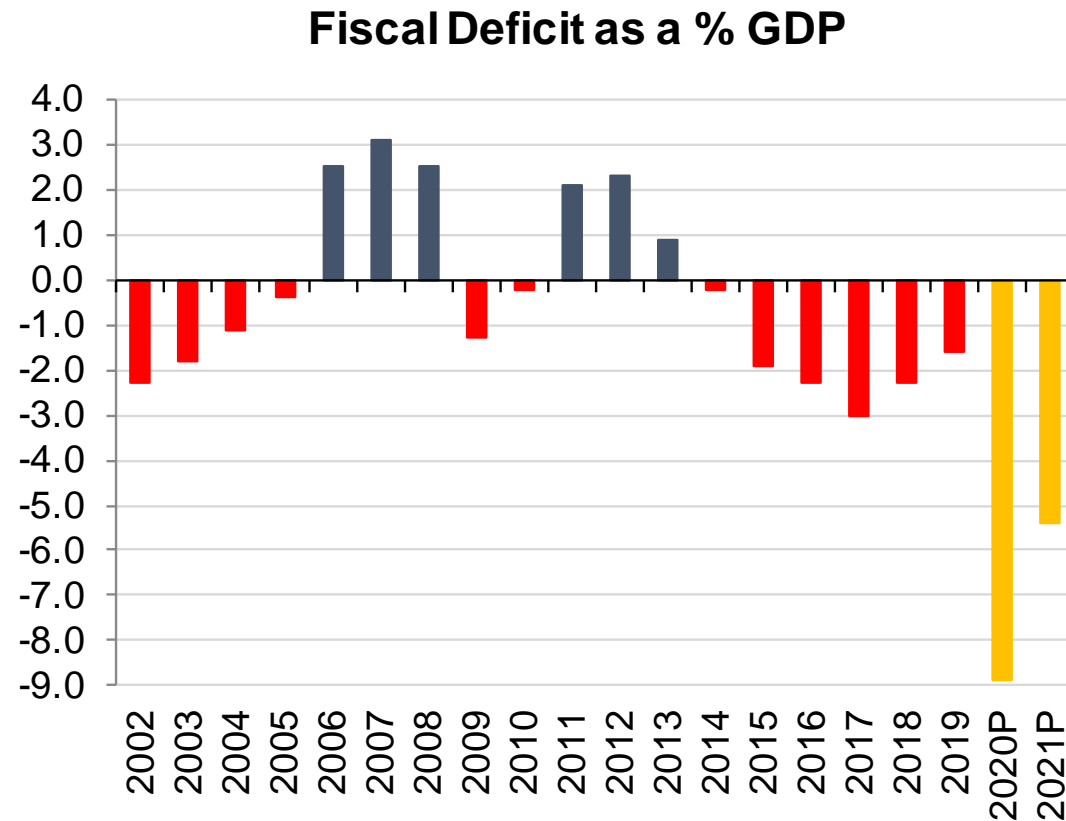
Source: BCRP Projections: Research Department-Scotiabank Peru



Source BCRP: Prepared by: Research Department-Scotiabank Peru

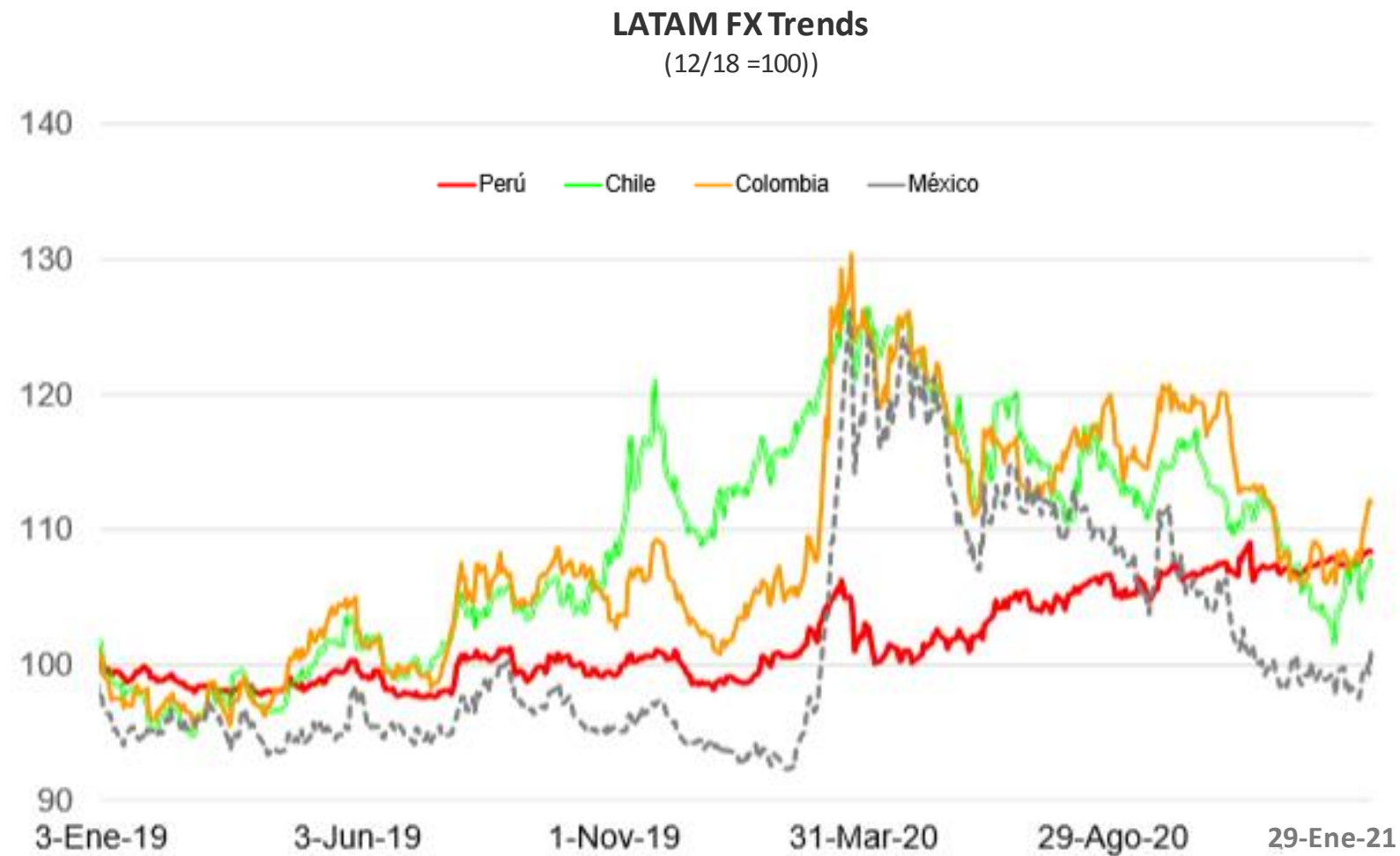
Metal prices could lower 2021 fiscal deficit

- Current 2021 forecast: -5.4% GDP, with avg copper price of USD 3.35/lb.
- Every one cent increase raises income tax revenue by USD 10 mn.
- A copper price of USD 4.00/lb would increase income tax revenue by USD 650 mn to USD 800 mn.
- This would bring down the fiscal deficit by 0.4 ppts to 0.5 ppts.



Source: BCR Projections: Research Department-ScotiabankPeru

PEN is not aligned with regional peers

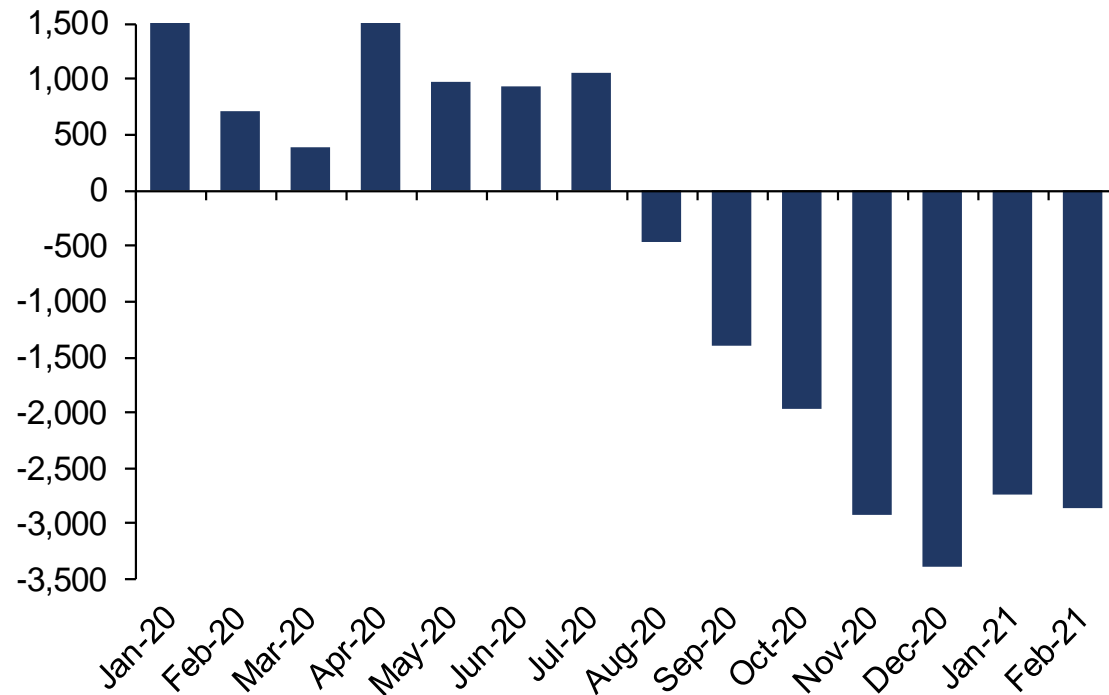


Source: BCPR



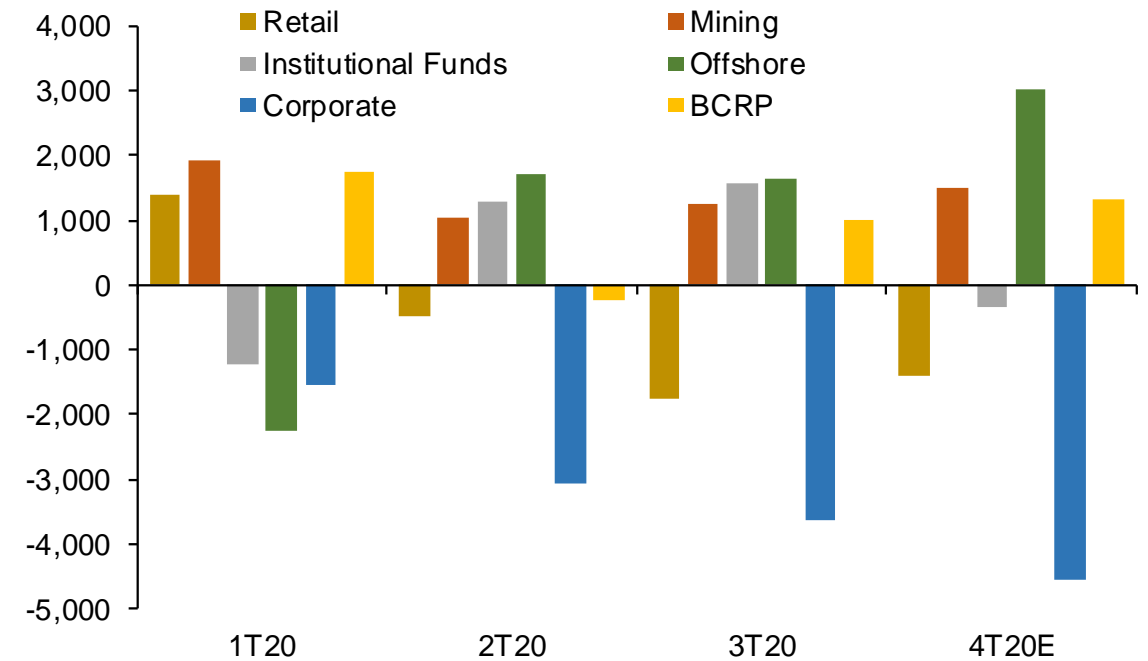
Corporate demand for USD liquidity has shifted from bank loans to FX market

Net USD Assets in Banking System



Source: BCRP. Prepared by: Estudios Económicos Scotiabank Bank Peru

FX Market: Net USD Sales



Source: BCRP, Scotiabank Perú

Elections are in seven weeks

Voter Intention - Peru elections

Candidate	Feb-21	Jan-21	Dec-20	Nov-20
George Forsyth	11	17	18	16
Yonhy Lescano	10	6	4	3
Keiko Fujimori	8	8	7	5
Verónica Mendoza	8	7	7	6
Daniel Urresti	7	6	6	6
Hernando de Soto	4	5	3	na
Julio Guzmán	4	7	8	7
Undecided/None	29	25	28	35

Source: Ipsos

- **Health crisis + credibility crisis + political crisis + economic crisis** may bolster anti-establishment vote.
- A quarter of voters are undecided.
- Votes will shift from lagging to leading candidates as elections near.

Key issues regarding new authorities

- **Forsyth** **no party; city mayor.**
- **Lescano** **no executive experience; Congress.**
- **Fujimori** **political experience; no executive experience.**
- **Mendoza** **no party; no executive experience.**
- **Urresti** **no party; no executive experience.**
- **Guzmán** **new party; no government experience.**

- No candidate has significant governing experience or proven management capacity.
- New cabinet head: will define political priorities and governance.
- New finance minister: will define policy quality and continuity.
- New BCRP Board: will define monetary solvency and confidence.
- The new Congress will include many members with little experience (new law prohibits re-election).

Governability is at issue (again!)

Vacunagate has renewed governability risk—the risk of an empowered Congress

- Exceptional times: health crisis + credibility crisis + economic crisis.

Why is Peru in a state of seemingly perpetual political turbulence?

- The difference between Peru and other countries is the weakness of political institutions and of the rule of law.
- Political parties neither represent voters (no constituencies) nor do they develop future leaders.
- The application of the law is unpredictable.
- State management capabilities have deteriorated.
- Economic institutions are strong, but the above puts them at risk.

Legislative legacy

- **Constitutional Court has struck down:**
 - 1. road tolls elimination;
 - 2. reimbursement of public pension funds; and
 - 3. automatic worker promotion in State institutions.
- Pension fund reform
- Mining law
- Interest rate caps
- **Possible future initiatives:**
 - Wealth tax
 - Education reform

A bright spot

After the Presidential elections are concluded, the economy could soar:

- Electoral uncertainty resolved
- New authorities with the credibility of having been elected
- A vaccinated population in a vaccinated world
- Renewal of correlation between metal prices and private investment
- Pent-up investment and consumption (high level of savings)
- Robust macro accounts
- Infrastructure investment already tendered
- A more digitalized world

Key: adequate governance, continuity in economic policy, no sharp decline in metal prices

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