

Central Bank Operations and their Current Challenges in Peru

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CEMLA**



BANCO CENTRAL DE RESERVA DEL PERÚ

Central Bank Policy Response

01

Reduction of policy rate to historical minimum

Reduction of the policy rate between March and April 2020, from 2.25% to 0.25%, its historical minimum.

Forward guidance: The BCRP Board of Directors emphasized that it considers appropriate to maintain an expansionary monetary stance as long as the negative effects of the pandemic on inflation and its determinants persist.

02

Easing of reserve requirements

Reduction of the reserve requirement in soles from 5% to 4% and of reserve requirement on FX external liabilities with terms below two years from 50% to 9%.

Reduction of banks' minimum current account requirement in soles with the BCRP from 1.0% to 0.75%.

Suspension of the additional reserve requirement associated with dollar loans.

03

Financial system liquidity

Repos up to 3 years (securities and FX).

Easing of portfolio repos (new scheme includes factoring, entities rated up to B +, reduction of minimum guarantee).

Discount window (elimination of limit on operations).

New liquidity facilities: (i) Repos under Government Loan Guarantee Program; (ii) Repos conditional on rescheduling of loan portfolios; and (iii) liquidity facility under Government Loan Portfolio Guarantee.

04

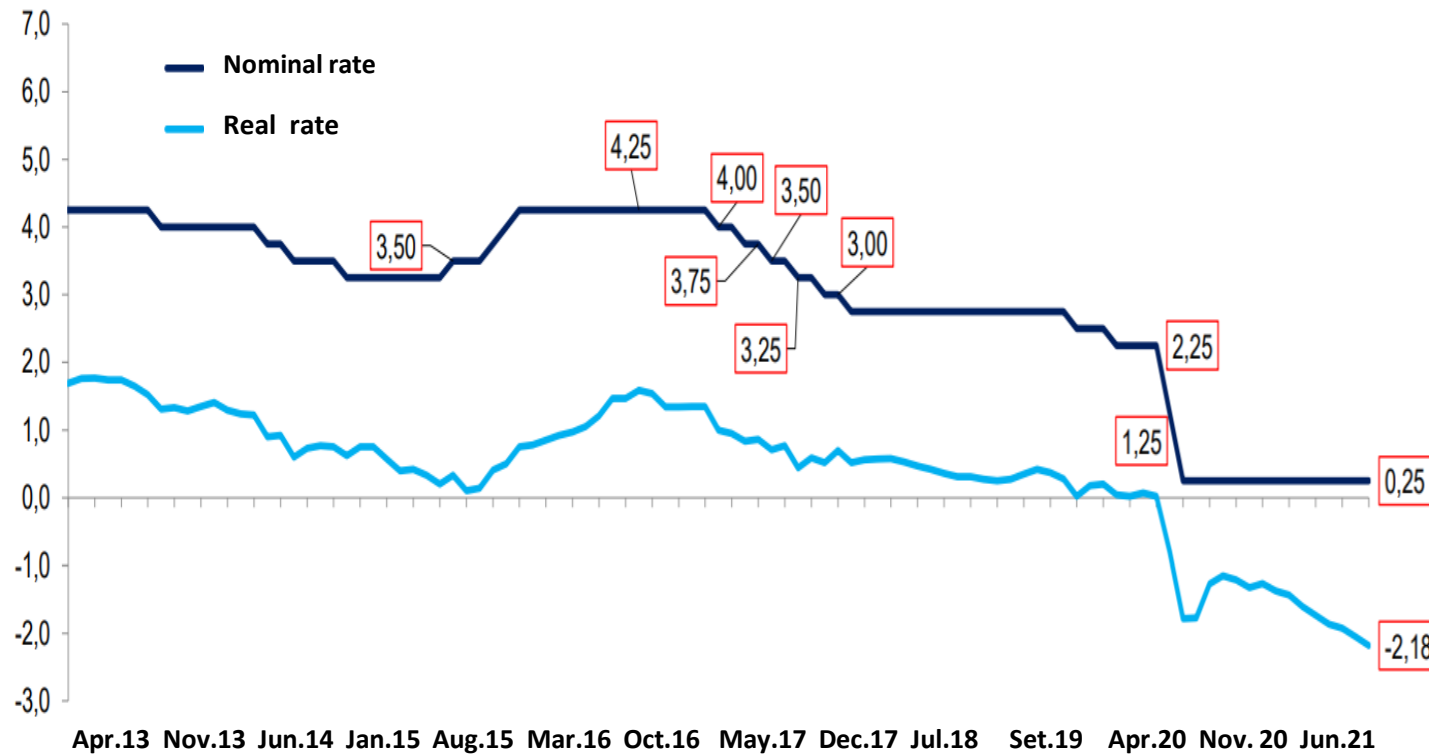
Reduced volatility in long-term interest rates and the exchange rate

FX intervention through spot and derivatives operations.

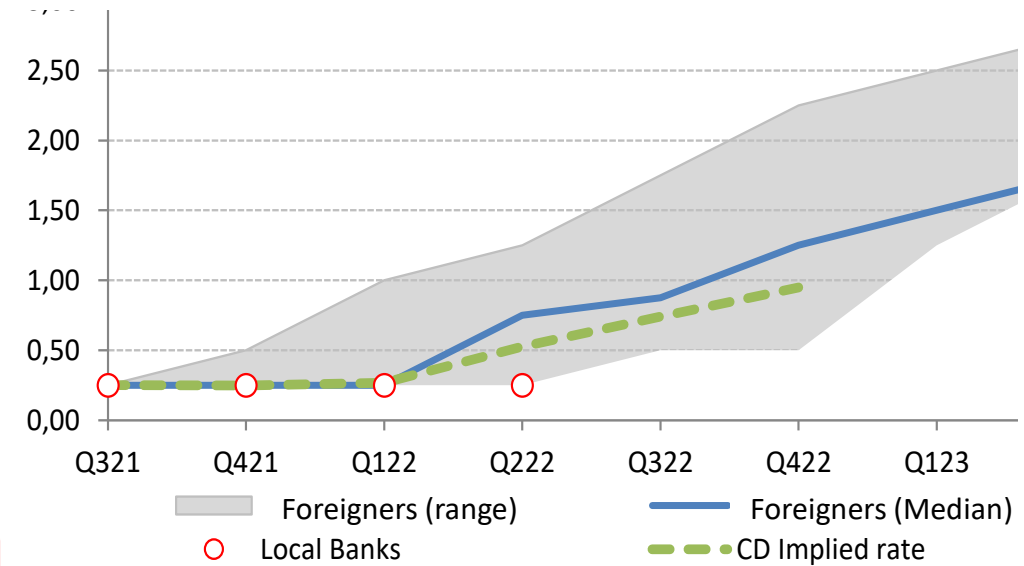
The current stance of Monetary Policy

i) Low real interest rates

Monetary Policy rates
(In percentages)

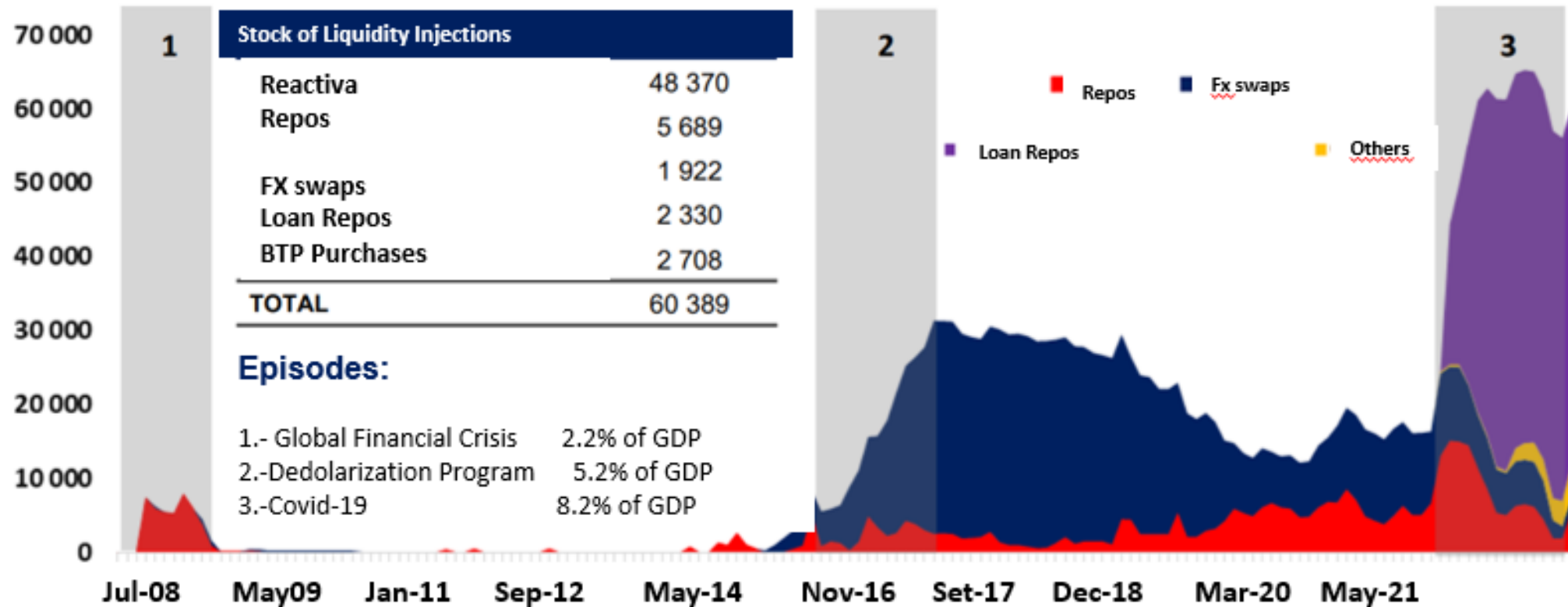


Market expectations for the Monetary policy rate
(In percentages)



ii) Large volumes of liquidity in the financial system

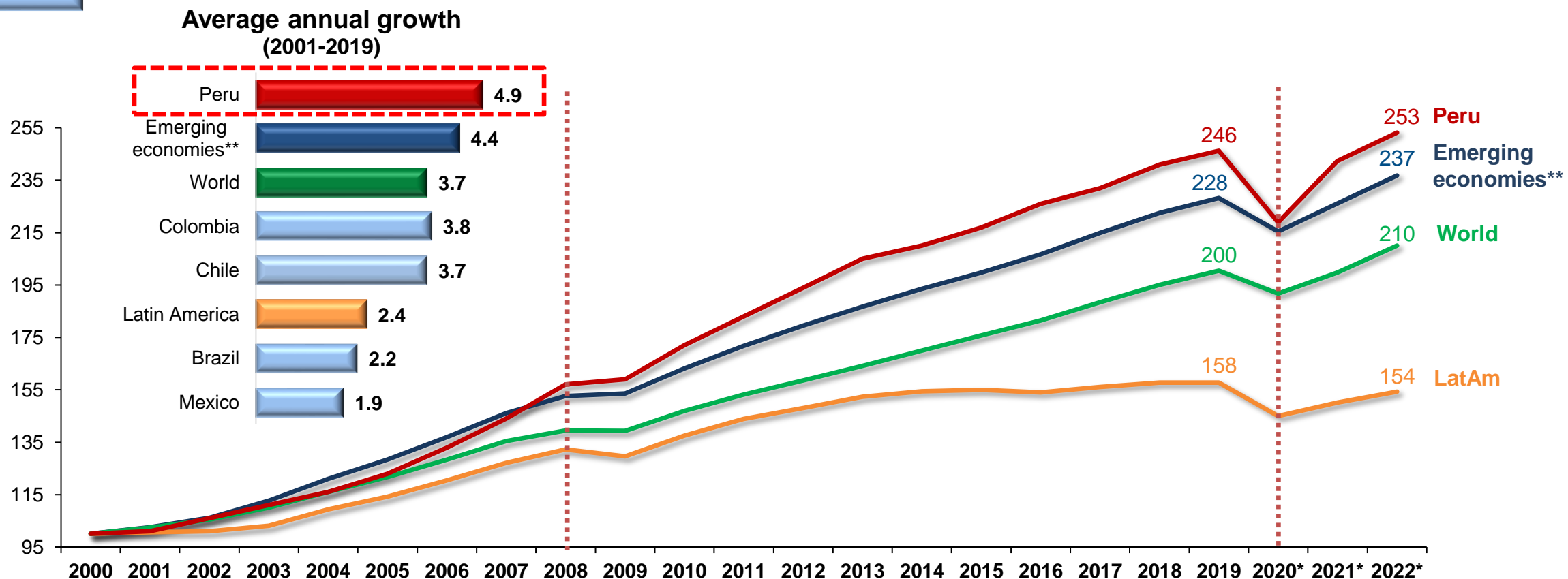
Monetary Operations For Liquidity Injection (In million of PEN)



Peru's GDP is expected to recover to pre-crisis levels by 2022, with a good performance among EMEs.

GDP Growth

Real GDP
(Index 2000 = 100)

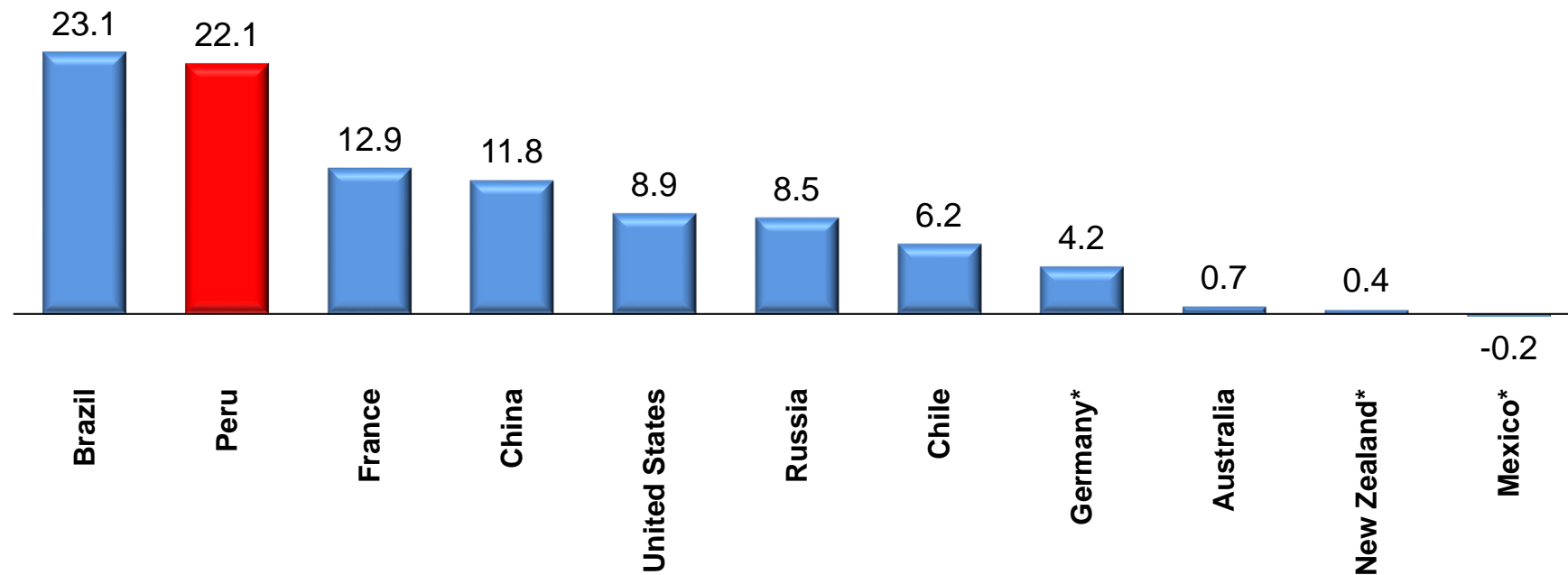


**Excludes China.

Source: IMF (World Economic Outlook Database, October 2020) and BCRP (Peru).

Countercyclical expansion of credit to the private sector

Credit to non-financial firms: as of January 2020
(Annual growth rate)



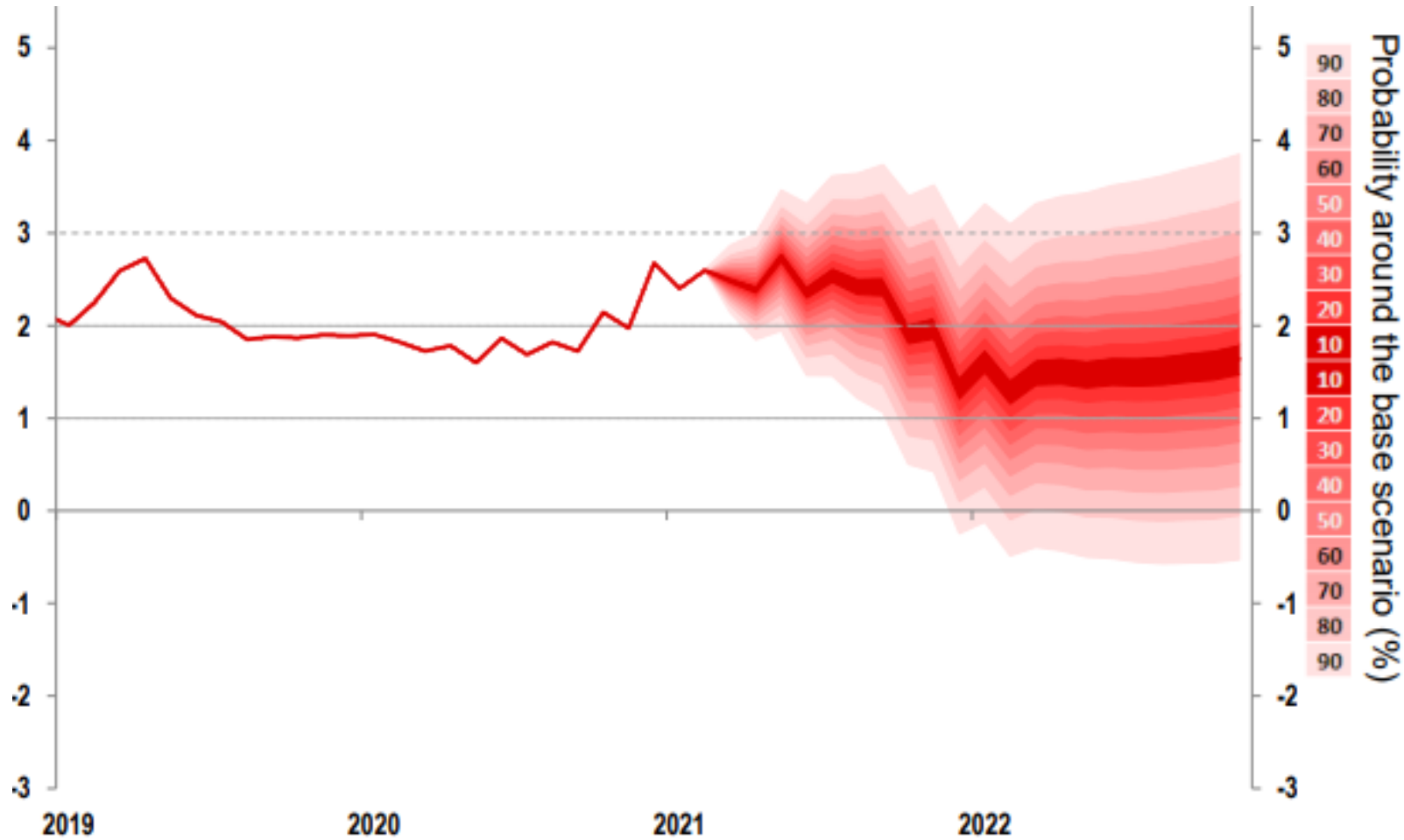
Note: for China, includes credit to the public and private sector.

* As of December 2020.

Source: Central banks

Inflation subdued and within the Central Bank target range

Inflation Forecast: 2021-2022
(Last 12-month % change)



New challenges for BCRP Monetary Operations

- **Mitigate Volatility in financial markets.**
 - Fears of sooner than anticipated FED's monetary policy reversal are generating volatility in capital flows.
 - The uncertainty about the direction of macroeconomic policies under a new government in Peru has triggered an increase in the demand for foreign assets.
 - Congress has passed a new Pension Fund withdrawal, which also is generating volatility in long-term interest rates
- **Contain pressures in foreign currency liquidity.**
 - Demand for deposits in foreign currency has increased recently in response to higher uncertainty.

Targeted Liquidity Provision

Repos to inject FX

To reduce pressure on FX liquidity



Repos with bank loans guarantee by the National Government

To provide liquidity to small financial institution.



Repos to provide liquidity to Pension Funds:

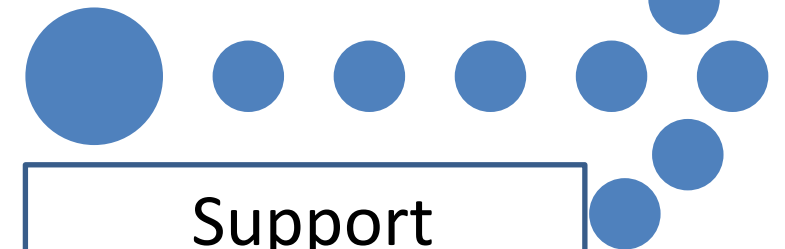
-To reduce volatility in long-term interest rates

Fx Intervention



Targeted
liquidity
provision

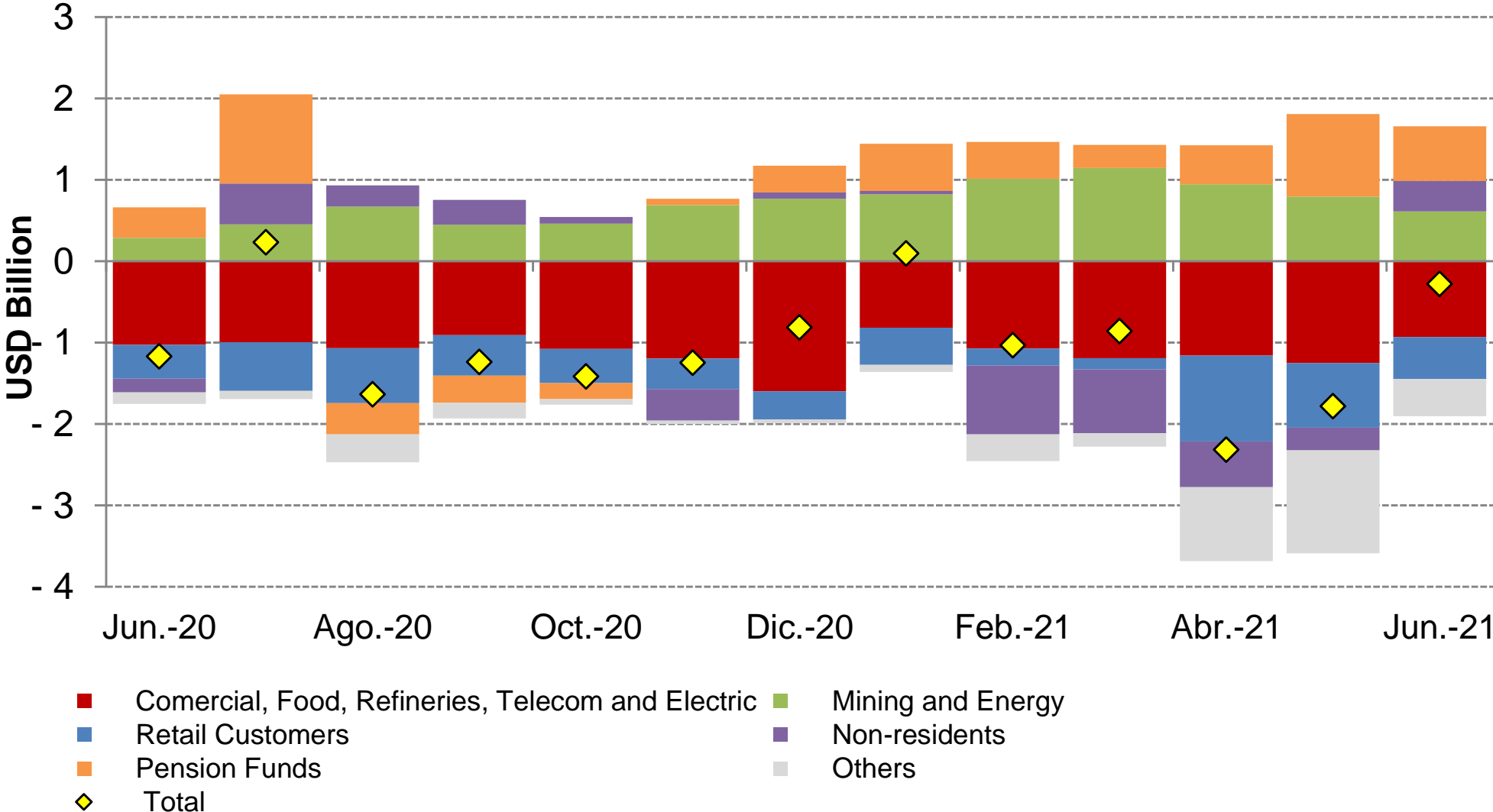
Stabilize Financial
Markets



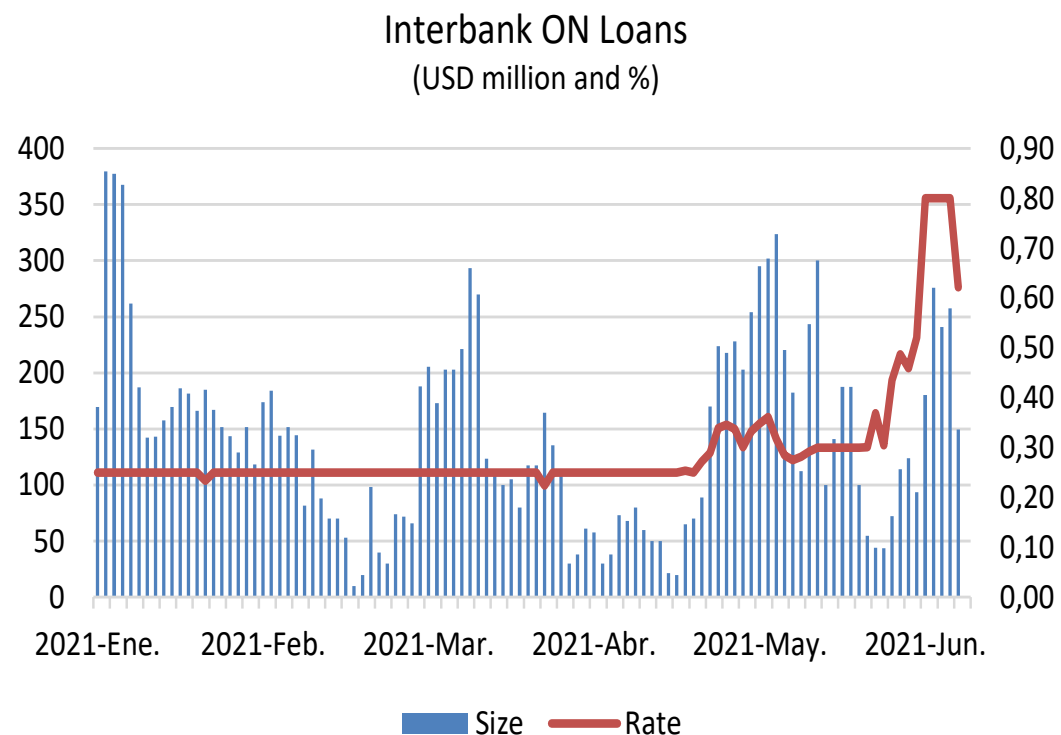
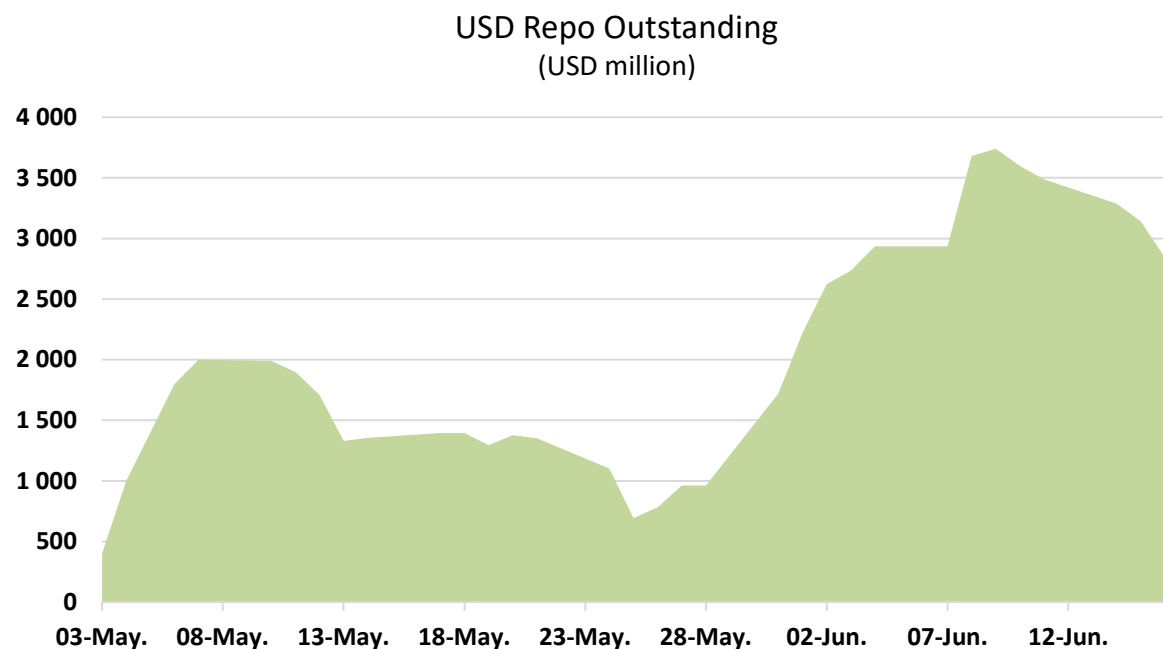
Support
monetary policy
transmission

Banks faced large FX net demand from local clients

Net offer flows in the spot market

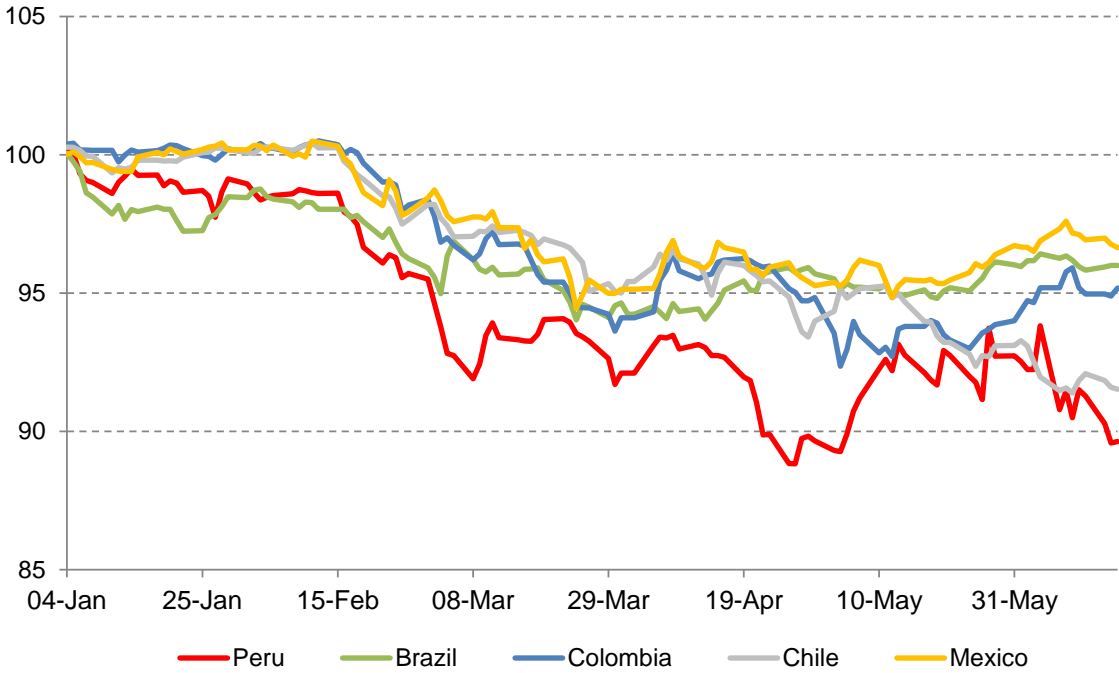


In May-June, local banks lost USD 1.5 billion and USD 572 million in term and demand deposits, respectively, which put pressure on USD liquidity in the local interbank market. As a result, the USD O/N interbank rate increased from 0.25% to 0.80%.



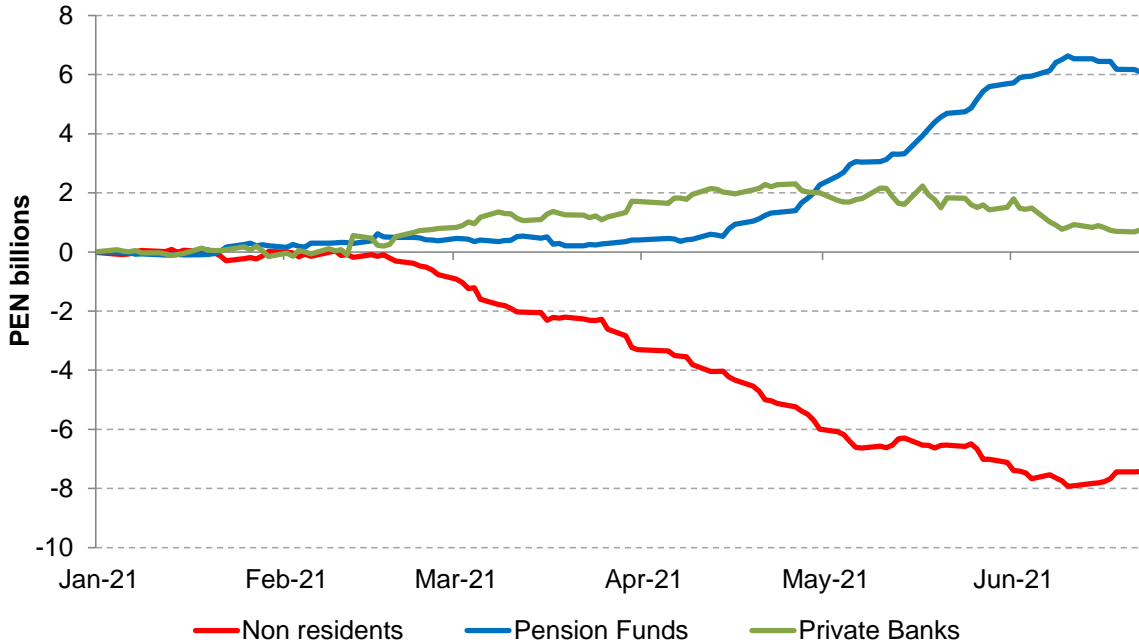
Non-resident investors reduced their BTPs holdings from 52% to 45% during 2021. Pension Fund Managers (AFPs) and the BCRP bought BTPs. BCRP has open a Repo facility to AFP to provide liquidity to this market.

Latam 5: GBI-EM Index (Local Currency)
31Dec20 = 100



Source: Bloomberg

Cumulative change in BTP nominal holdings by group

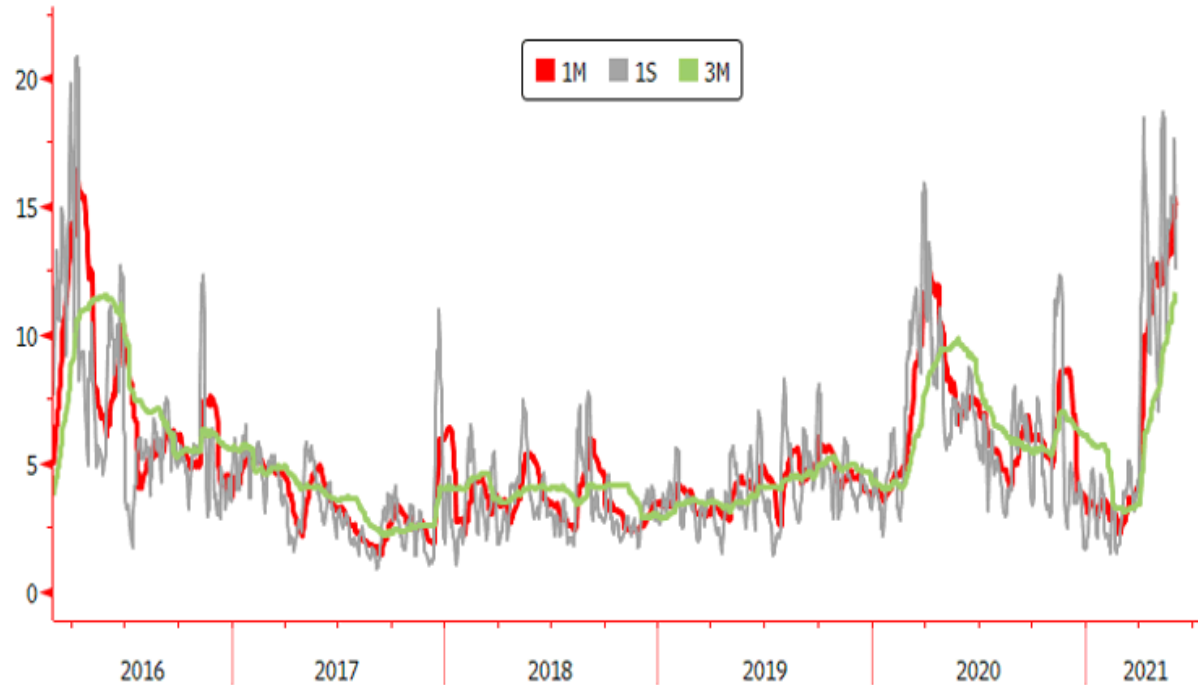


Sources: BCRP based on data from CAVALI and SBS

Non-residents escalated their demand for hedging and residents increased their preference for dollar-denominated deposits. The BCRP has continued to use FX intervention through spot and swap operations to mitigate FX volatility.

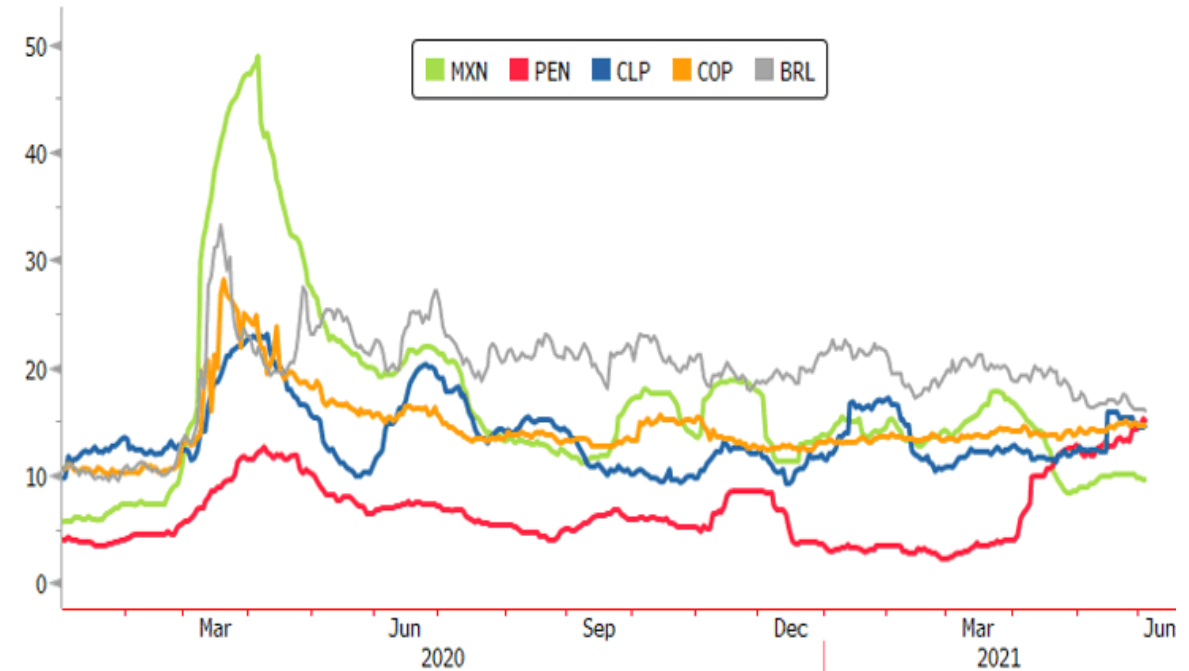
Historical Volatility PEN

Intraday Volatility in pip



Source: Bloomberg

Annualized standard deviations



Source: Bloomberg

Challenges Ahead

- 1. Use effectively monetary policy instruments to smooth volatility in financial markets.**
- 2. Support the stance of monetary policy with the appropriated combination of OMO.**
- 3. Provide timely foreign currency liquidity in order to mitigate the impact of higher volatility on credit and money markets.**
- 4. Targeted strategy to inject liquidity to smaller financial institutions, mutual and pension funds.**