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Latam Daily: Peru's External Accounts

- **Peru: The best may be over for Peru's robust external accounts**

PERU: THE BEST MAY BE OVER FOR PERU'S ROBUST EXTERNAL ACCOUNTS

Alarms went off when the BCRP published the second quarter 2022 balance of payments results, which showed the current account deficit remaining at a very high 4.6% of GDP, signalling that the 6.3% of GDP in Q1 was not an outlier. Both figures were higher than the 2.3% of GDP deficit for 2021.

However, if one takes a deeper look at the accounts, one can breathe a little bit easier. It was all the fault (yes, fault) of high metal prices and strong earnings by foreign companies operating in Peru.

BoP accounting treats total earnings of foreign companies as a current account outflow, regardless of whether an actual outflow occurs or not. Retained/reinvested earnings—earnings that do not actually leave the country—are then treated as a financial account inflow. This, of course, includes the mining companies themselves.

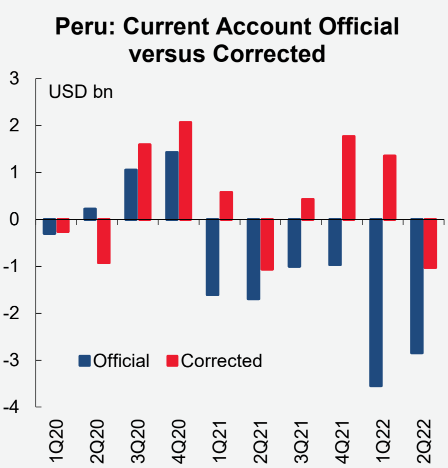
In Peru, mining and oil & gas accounted for 64% of total earnings registered in the current accounts. Thus, there is a direct correlation between foreign earnings and commodity prices. As a result, it is not unusual for Peru's current account to worsen, counterintuitively, worsen when metal prices rise, and improve when they prices fall.

Most of these earnings are retained and never actually leave the country. In Q2, retained earnings amounted to USD 1.8 bn (2.9% of GDP). If these retained earnings are excluded, the current account deficit for the quarter would be USD 1.0 bn (1.7%) of GDP rather than USD 2.8 bn (4.6%) (chart 1).

Even so, a 1.7% corrected current account deficit is still a deficit, and does denote a certain deterioration from the past. The net overall result of the BoP tells a similar story, declining by USD 1.3 bn in Q2 (table 1). This came after an even greater decline of USD 2.5 bn decline in Q1.

A large factor behind this, rather modest, deterioration in external accounts was the sharp decline in the trade surplus, from USD 4.2 bn in Q1, to USD 1.5 bn in Q2. At the same time, the capital account saw a net inflow of USD 2.3 bn, which was not quite enough to compensate for the current account deficit. The main positive in the details was that the strong hemorrhage of short-term capital of the previous quarters was stemmed. In 2021, capital outflows had left the country at a net pace of over USD 4 bn per quarter.

Chart 1



Sources: Scotiabank Economics, BCRP.

Table 1: Peru—Balance of Payments

USD mn	H1-2021	H2-2021	2021 full-year	Q1-2022	Q2-2022	H1-2022
Current account balance	-3,303	-1,970	-5,273	-3,551	-2,849	-6,400
Trade balance	5,356	9,477	14,833	4,198	1,526	5,725
Exports	28,213	34,938	63,151	17,048	16,186	33,233
Imports	-22,857	-25,461	-48,317	-12,849	-14,659	-27,508
Services	-3,173	-4,174	-7,347	-2,168	-1,925	-4,093
Investment income	-8,116	-10,011	-18,127	-6,878	-3,787	-10,664
Remittances	2,629	2,738	5,367	1,296	1,336	2,632
Capital account balance	2,279	13,348	15,627	904	1,586	2,490
Private sector	7,329	9,346	16,675	5,428	2,343	7,772
Public sector	5,037	10,554	15,590	-417	178	-239
Short-term capital	-10,086	-6,552	-16,638	-4,108	-935	-5,043
Financial	859	12	871	-1,741	393	-1,348
Non-financial	-10,945	-6,564	-17,509	-2,366	-1,329	-3,695
Errors and omissions	-1,468	-4,475	-5,944	100	-54	46
Total balance of payments	-2,493	6,903	4,410	-2,547	-1,317	-3,864

Sources: Scotiabank Economics, BCRP.

This was repeated by a similar USD 4.1 bn in Q1 2022. In contrast, the net outflow in Q2 2022 was only USD 0.9 mn. Furthermore, there was very little inflow either to the public or to the private sector.

It is true that the BoP has taken a bit of a turn for the worst, but not to the extent that the headline current account figures might suggest. Although we expect external accounts to continue weakening, or at least not improving very much, in future quarters, this weakening will be off a position of strength.

—Guillermo Arbe