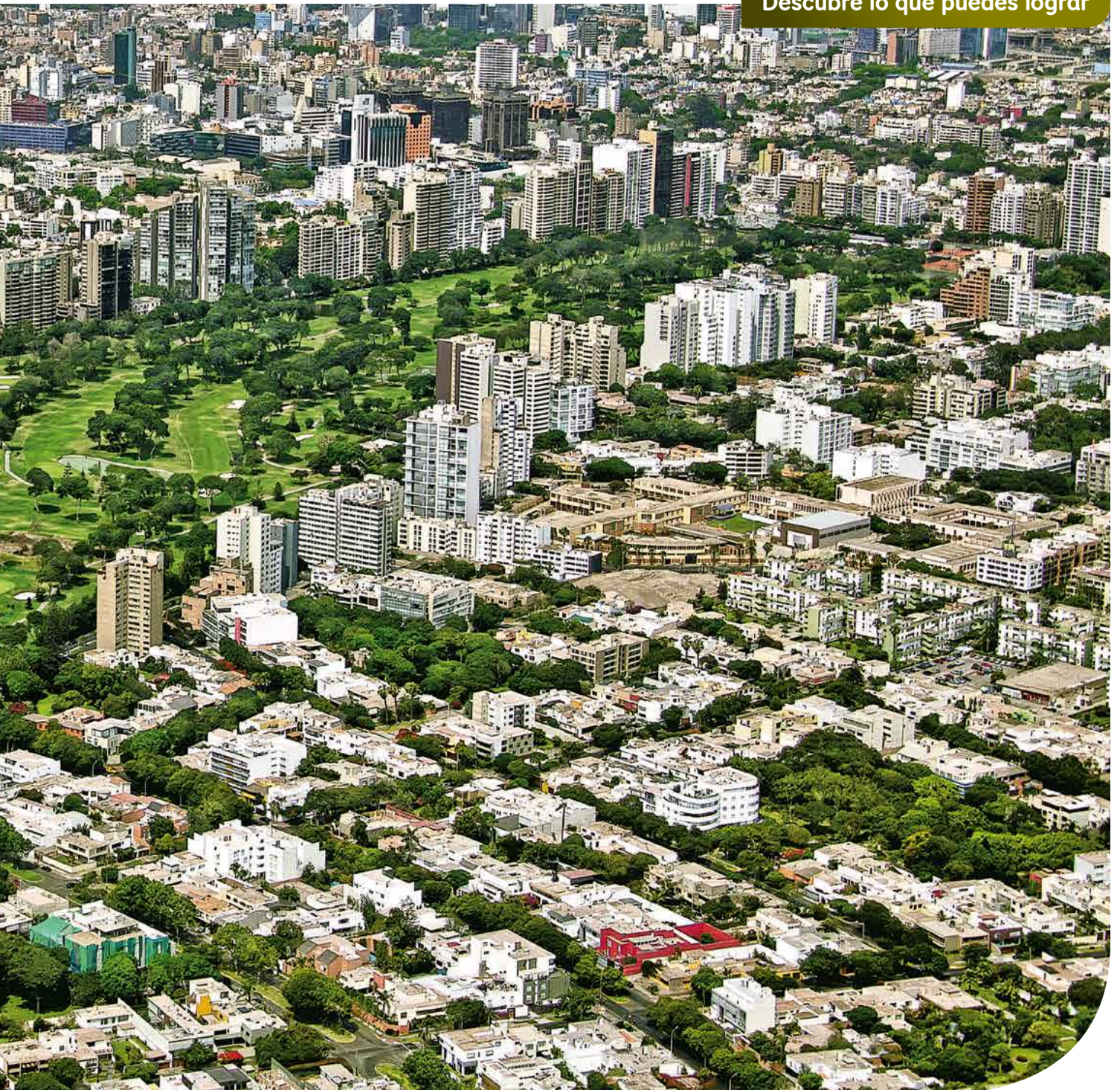


PERU: Real Estate Market Outlook



Descubre lo que puedes lograr



2014

PERU: Real Estate Market Outlook

2014

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Introduction

Over the last few years, Peru's real estate market has experienced exceptionally strong growth, while expanding into new business areas and segments of the population. This expansion was led by, but not limited to, the housing sector, fed by increasing demand from emerging sectors of the population, improving household income levels, and a more developed mortgage loans market. Recently, growth has slowed from a near explosive pace prior to 2013, to a still robust, but more sustainable pace. We expect real estate activity to continue to be robust in 2014, in line with the domestic economy, a more stable international environment and a less volatile PEN/US\$ exchange rate. Although the price of housing is likely to continue rising, given the relative scarcity of land, we expect price increases to be less significant than in previous years. Over the medium term, real estate growth should continue to be strong, as the significant shortage of housing will take time to be worked off, and as household employment and wage levels continue rising. At the same time, an increasing preference for mortgage loans in PEN is reducing FX risk.



Recent Trend

During the last five years, the real estate sector outperformed the economy as a whole, driven by rising household income levels, greater access to mortgage loans and the government Mivivienda program.

Over the past five years, the real estate sector expanded at a faster pace than the economy as a whole, driven by:

- Increasing household income levels.
- Pent-up demand, particularly for houses for middle and mid-low household income levels.
- Greater access to mortgage loans due to lower interest rates.
- State housing programs such as MIVIVIENDA.

In 2013, a number of factors slowed the growth of the real estate sector, including: i) stricter conditions by banks for mortgage loans due to changes in regulations; ii) a slowdown in private investment, business confidence, and employment growth; and iii) a depreciation

in the PEN/US\$ exchange rate, thereby raising the value of homes priced in US\$. As a result, building activity was up only 2.5%, year-on-year, in the Lima - Callao Metropolitan area to July 2013, totaling 6.1 million sq.m., according to the 18th Market Study of Urban Buildings in Lima and Callao, conducted by CAPECO.

The CAPECO study states that construction growth in the period was led by office space, up 111.5%, followed by hotels, schools, movie theaters, restaurants, etc. (lumped together under “other”) at 12.6%. This was partially offset by a drop in the construction of commercial establishments (stores and retail outlets) (-13.7%) and houses (-5.3%). Housing, however, represented 74.4% of total construction activity, followed by “other” (13.2%), office space (10.3%) and commercial establishments (2.1%).

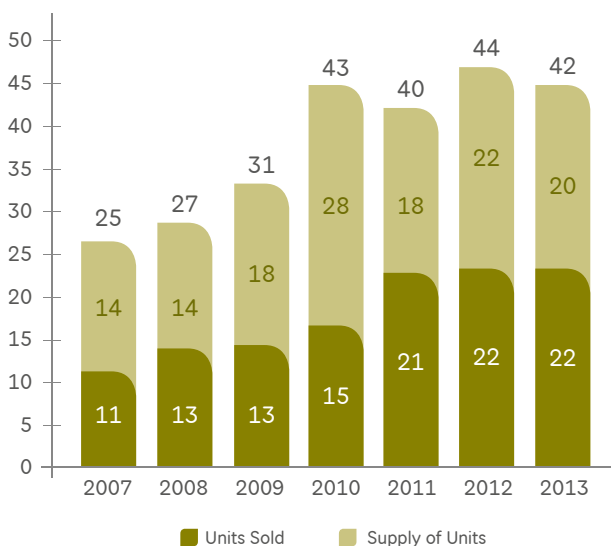
The number of homes actually sold, however, increased 1%, yoy. The number of new homes sold rose, but unsold homes available for sale fell nearly 9%. As a result, the total supply -sold and available houses- in Metropolitan Lima fell to nearly 42,000 houses in July 2013, versus 44,000 a year before, 3.9% decline.

The greatest expansion in construction, however, was in office space. The area of office space for sale (excluding office space for non-sale use) rose 273% to July 2013, yoy, greatly surpassing the yoy increase to July 2012.

Land price continued rising in 2013. The average price per square meter (m²) of land in Lima was US\$1,192 in July 2013, 66% and 57% greater than in July 2012 and 2011, respectively.

Total marketable supply

(in thousands of units)



Source: CAPECO

Prepared by: Estudios Económicos Scotiabank

Price of land in Lima

Prices per m²

Sector	2010	2011	2012	2013	Var. % 13/12
Lima Top	1,141	1,481	1,427	2,126	49%
Lima Modern	721	896	1,359	1,870	38%
Lima Center	698	825	917	1,398	52%
Eastern Lima	270	376	341	563	65%
Northern Lima	136	152	341	515	51%
Southern Lima	164	351	356	547	54%
Callao	167	322	525	734	40%
Average	586	761	716	1,192	-----

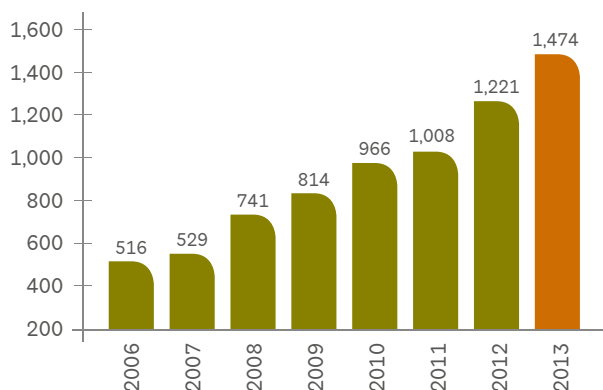
Source: CAPECO

Prepared by: Estudios Económicos Scotiabank

The rising price of land, together with strong house demand relative to supply, drove the average price per square meter (m²) of residential apartments in Lima in July 2013 to US\$1,474, up 21% and 46% versus July

2012 and 2011, respectively. In high-income districts, the average price per square meter (m²) of apartments remains above the average price registered for the city of Lima as a whole.

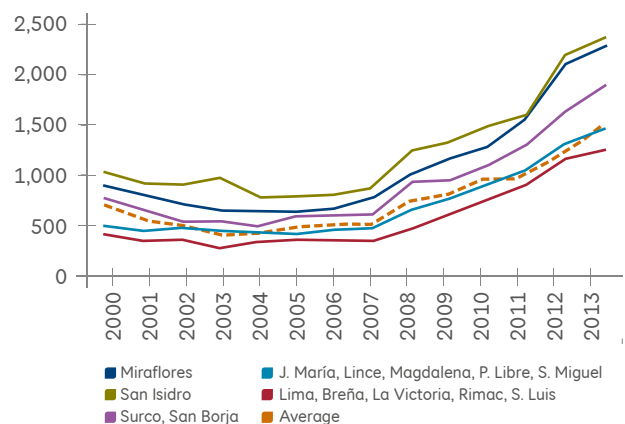
Lima: Average department floor price

(US\$ per m²)

Source: CAPECO

Prepared by: Estudios Económicos Scotiabank

Lima: Average department floor price by district

(US\$ per m²)

Source: CAPECO

Prepared by: Estudios Económicos Scotiabank

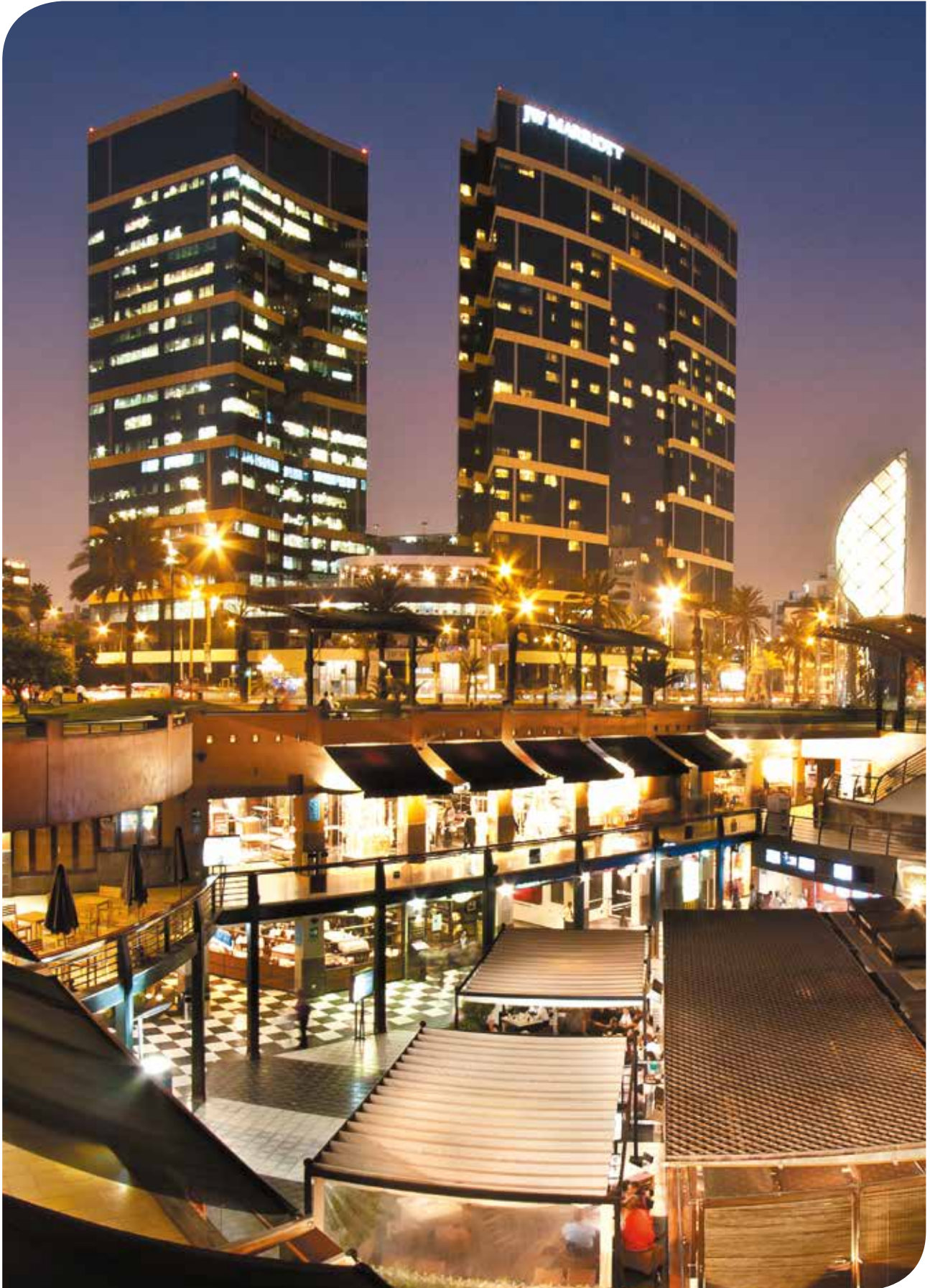


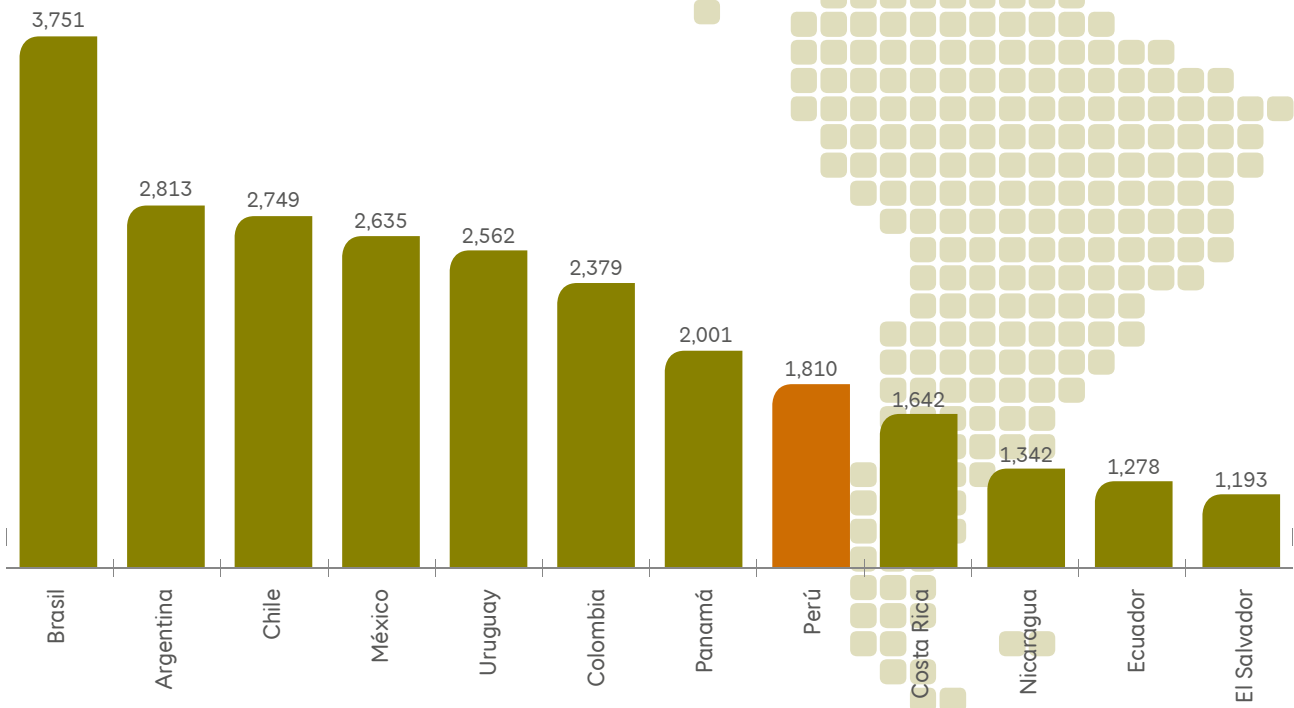
Foto / © Christian Vincés

The sharp increase in land and residential prices has been cause for some concern over the possibility of a real estate bubble. However, there is no real evidence of a bubble. The increase in prices of residential properties is for fundamental reasons, mainly, large pent-up demand for first-time homes and the relatively low value of land prices in Lima compared to other major Latin American cities. According

to the Global Property Guide, Peru has one of the lowest prices per constructed square meter (m²) in the region. Thus, the average price in Peru (US\$ 1,306) is lower than in Brazil (US\$ 3,916), Argentina (US\$ 2,804), Mexico (US\$2,635), Uruguay (US\$2,589), Chile (US\$2,517), Panama (US\$2,015), Colombia (US\$1,895), Costa Rica (US\$1,642), Nicaragua (US\$1,342), and so forth.

Latin America: Home prices in 2013

(US\$ per m²)



Source: Global Property Guide

Prepared by: Estudios Económicos Scotiabank

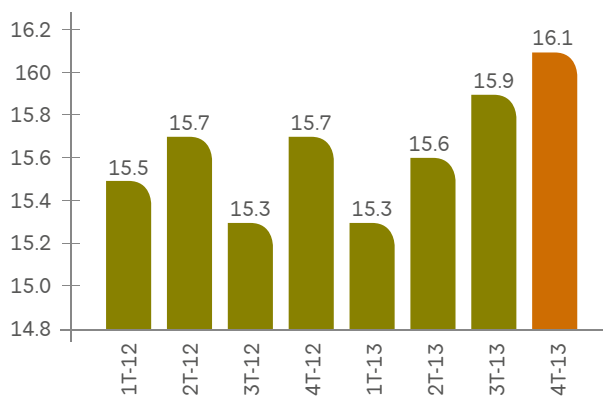


Furthermore, the Price to Earnings Ratio (PER), calculated by Peru's Central Bank, was 16.1x (it will take an

investor 16 years to recover his investment) in the fourth quarter of 2013.

Price to earnings (rent) ratio for departments

(years for return on investment)



Source: BCRP

Prepared by: Estudios Económicos Scotiabank

Valuation criteria for the real estate market

Price / Rent Ratio	Rent Profit (%) ¹	Valuation
5 - 12,5	20,0 - 8,0	Undervalued
12,5 - 25,0	8,0 - 4,0	Normal
25,0 - 50,0	4,0 - 2,0	Overvalued

(1) The inverse of the PER, or average rent as a percent of purchase price.

Source: Global Property Guide

Prepared by: Estudios Económicos Scotiabank



This is well within a range considered normal, and is significantly lower than the 25x threshold above which

properties are considered overpriced. There are, however, certain areas of Lima in which this indicator is close to 18.

PER: Price of sale/Annual rental (US\$ per m²)

Distrito	4T-12	1T-13	2T-13	3T-13	4T-13
Jesus María	14.9	15.0	15.6	15.7	16.2
La Molina	11.6	13.7	14.7	15.5	16.4
Lince	16.4	14.1	14.6	15.4	15.5
Magdalena	16.0	14.0	14.5	15.1	15.0
Miraflores	15.0	14.8	16.5	16.3	15.9
Pueblo Libre	16.0	14.1	14.3	15.3	16.1
San Borja	18.2	18.6	17.5	17.1	16.7
San Isidro	18.4	18.0	17.2	17.3	17.7
San Miguel	15.6	14.4	14.8	14.7	15.0
Surco	15.0	16.8	16.3	16.5	16.6
Average	15.7	15.3	15.6	15.9	16.1

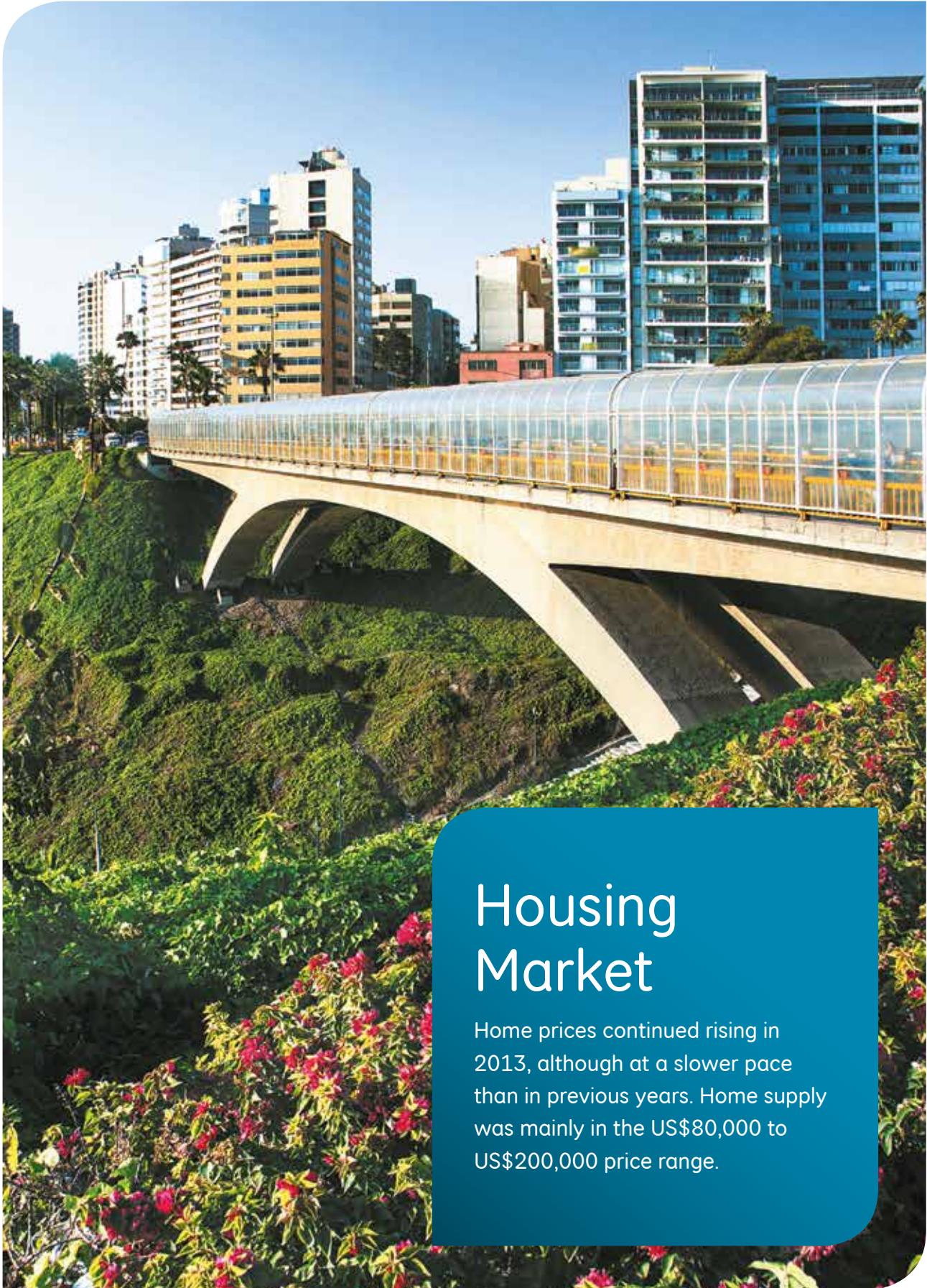
Source: BCRP

Building costs have also been rising. Prices of building materials increased 2.06% in 2013, according to Peru's National Statistics Institute, INEI. This increase was led by metal products (construction rods, wires), which is in part linked to the devaluation of the PEN. Higher oil prices also led to a rise in the price of bricks and plastic accessories and electrical supplies during the second half of the year.

Mortgage loans growth in the financial system has been equally buoyant. According to data from the Banking Superintendent (Superintendencia de Banca y Seguros, SBS), mortgage loans rose 21%, in local currency (10.7% in USD terms) in full-year 2013, to S/.29.7b (US\$10.6b).

Banks account for 96% of total mortgage loans.

The share of mortgage loans in USD versus total loans continued to decrease, falling to 38% at the end of 2013, from 45% a year earlier (and down from 96% in 2005). This was driven, in part, by a series of measures implemented by bank and monetary authorities in 2013 to discourage mortgage loans in USD. These measures included increasing the minimum mandatory down payments on mortgage loans in USD from 10% to 20%, applying a tax on second houses (typically, high end buyers who prefer operating in USD), and raising reserve requirements for banks that increase their mortgage loan portfolio in USD above a certain threshold.



Housing Market

Home prices continued rising in 2013, although at a slower pace than in previous years. Home supply was mainly in the US\$80,000 to US\$200,000 price range.

According to the CAPECO study, in July 2013 residential construction activity in Metropolitan Lima and Callao totaled 4,544,407 m2. This was down 5.3%, yoy.

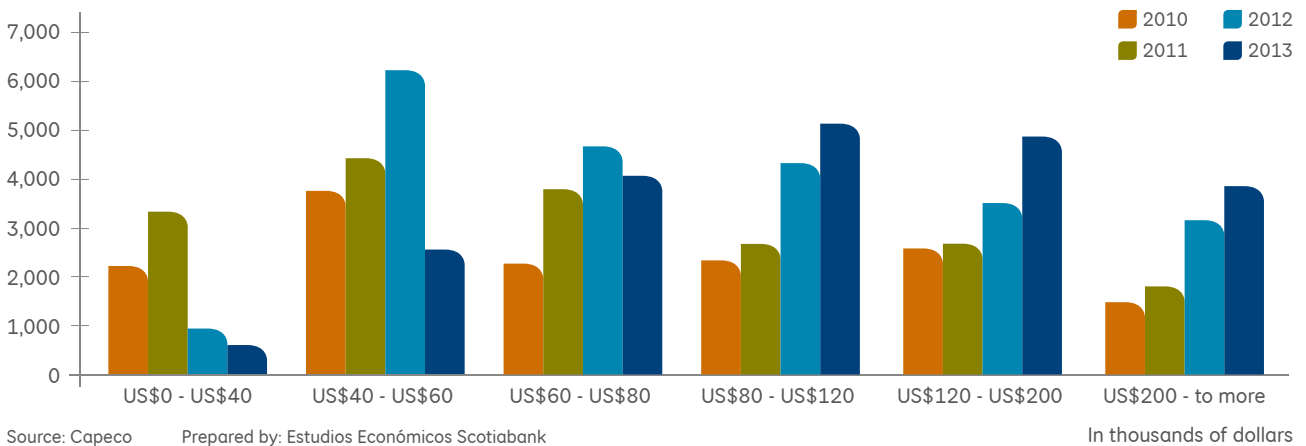
The middle class districts of Jesús María, Lince, Magdalena, San Miguel, Pueblo Libre, Surquillo and Barranco concentrated 36% of total units for sale.

Pending homes for sale amounted to 20,291 units, 9% lower from a year earlier (22,225 units). Apartments accounted for 98% of total units for sale. Prices were concentrated in the US\$80,000 to US\$200,000 range with 48% of units.

A total of 22,220 new homes were sold, up 1% more than a year earlier (21,990 homes), with apartments representing 95% of the total. Sales in the US\$80,000 to US\$200,000 represented 41% of the homes sold.

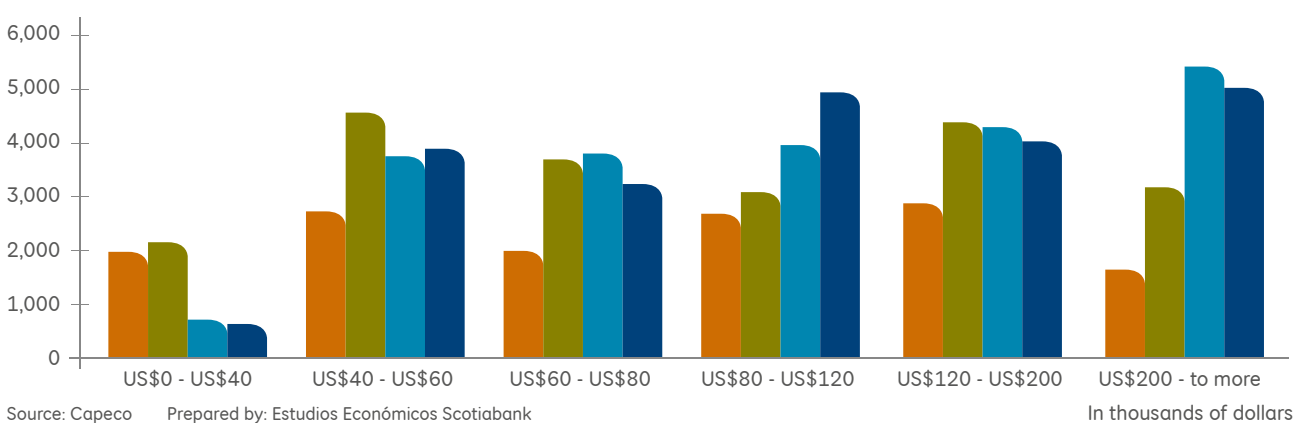
Supply of homes

(in units)



Sale of new homes

(in units)



As with pending homes for sale, the districts of Jesús María, Lince, Magdalena del Mar, San Miguel, Pueblo Libre, Surquillo and Barranco registered the highest concen-

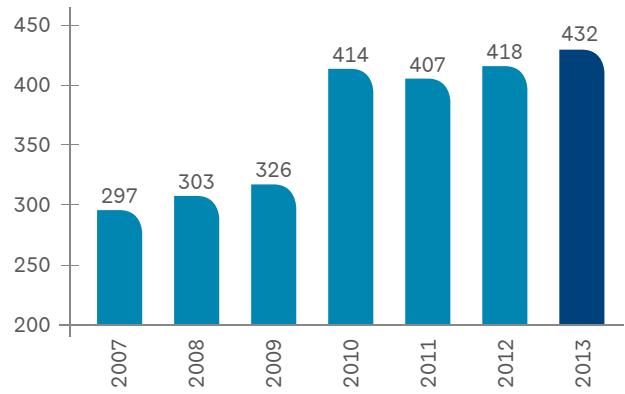
tration of apartments sold. We estimate the total effective demand in Lima at close to 432,000 homes, of which 59% is in a US\$4,000 to US\$60,000 price range.



Foto / © Christian Vincés

Effective demand

(in thousands of units)

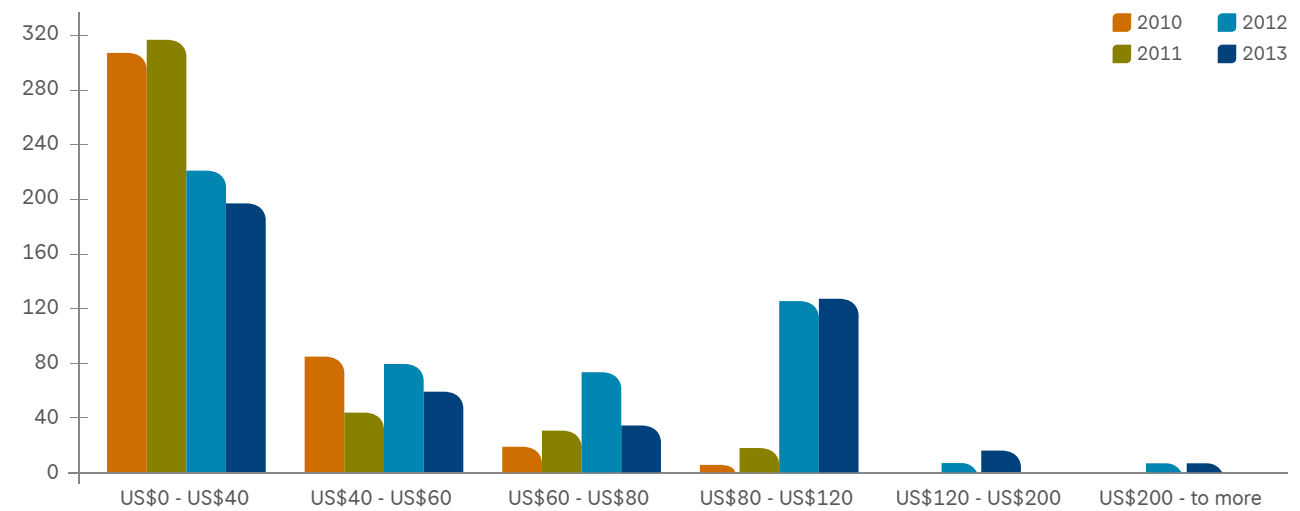


Source: CAPECO

Prepared by: Estudios Económicos Scotiabank

Effective demand for homes

(in thousands of units)



Source: Capeco

Prepared by: Estudios Económicos Scotiabank

In thousands of dollars

This reflects the significant potential for growth in homes for the lower household income sectors. However, as household income levels improve, effective demand has been moving towards a higher price range, and today's 59% is lower than the 71% of previous years.

The average price per apartment or flat in Metropolitan Lima was US\$145,318, up 19.4%, as the average price per square meter rose to US\$1,474. This increase reflects the higher cost of land, up 20.7%, YoY, in July 2013. The average area for apartments in July 2013, 89.9 m², was slightly greater than

the 88.7 m² registered in July 2012. Close to 75% of homes sold in Metropolitan Lima were presales of multi-family residences prior to construction (in blueprint form). This has been a trend that has increased over in time as a result of growing demand and a greater access to mortgage loan. In July 2009, presales of housing units in blueprint form accounted for 70% of the total units sold.

State Program Mivivienda

The State housing promotion program, Fondo Mivivienda, disbursed S/. 1.4 billion in loans in 2013.

PERU: Disbursement of Mivivienda - linked loans (in S/. 000)

Institutions	2008	2009	2010	2011	2012	2013
Crédito	51,113	104,903	182,730	279,107	376,762	489,982
Interbank	83,807	56,351	188,243	279,926	292,466	295,124
BIF	-	-	2,234	14,463	58,764	122,880
Continental	22,632	33,217	95,143	154,815	137,801	110,272
Scotiabank	12,908	12,240	32,297	78,781	60,335	107,031
Financiero	9,228	16,100	32,871	44,596	54,872	58,369
Comercio	2,813	1,834	2,392	3,429	1,637	1,428
Mi Banco	153	-	-	-	336	680
Other Entities	29,424	47,786	89,298	92,180	130,601	217,420
TOTAL	212,078	272,430	625,207	947,295	1,113,574	1,403,186

Source: Fondo Mivivienda S.A.

Prepared by: Estudios Económicos Scotiabank

PERU: Disbursement of Mivivienda - linked loans (in number)

Institutions	2008	2009	2010	2011	2012	2013
Crédito	917	1,698	2,363	2,940	3,344	4,043
Interbank	1,781	864	2,293	3,091	3,008	2,386
Continental	373	383	881	1,478	1,320	1,055
BIF	-	-	193	153	446	989
Scotiabank	246	187	331	973	499	723
Financiero	147	212	380	613	653	527
Comercio	45	23	68	60	15	15
Mi Banco	2	-	-	-	4	6
Others Entities	958	1,443	1,947	1,763	2,020	3,420
TOTAL	4,469	4,810	8,456	11,071	11,309	13,164

Source: Fondo Mivivienda S.A.

Prepared by: Estudios Económicos Scotiabank

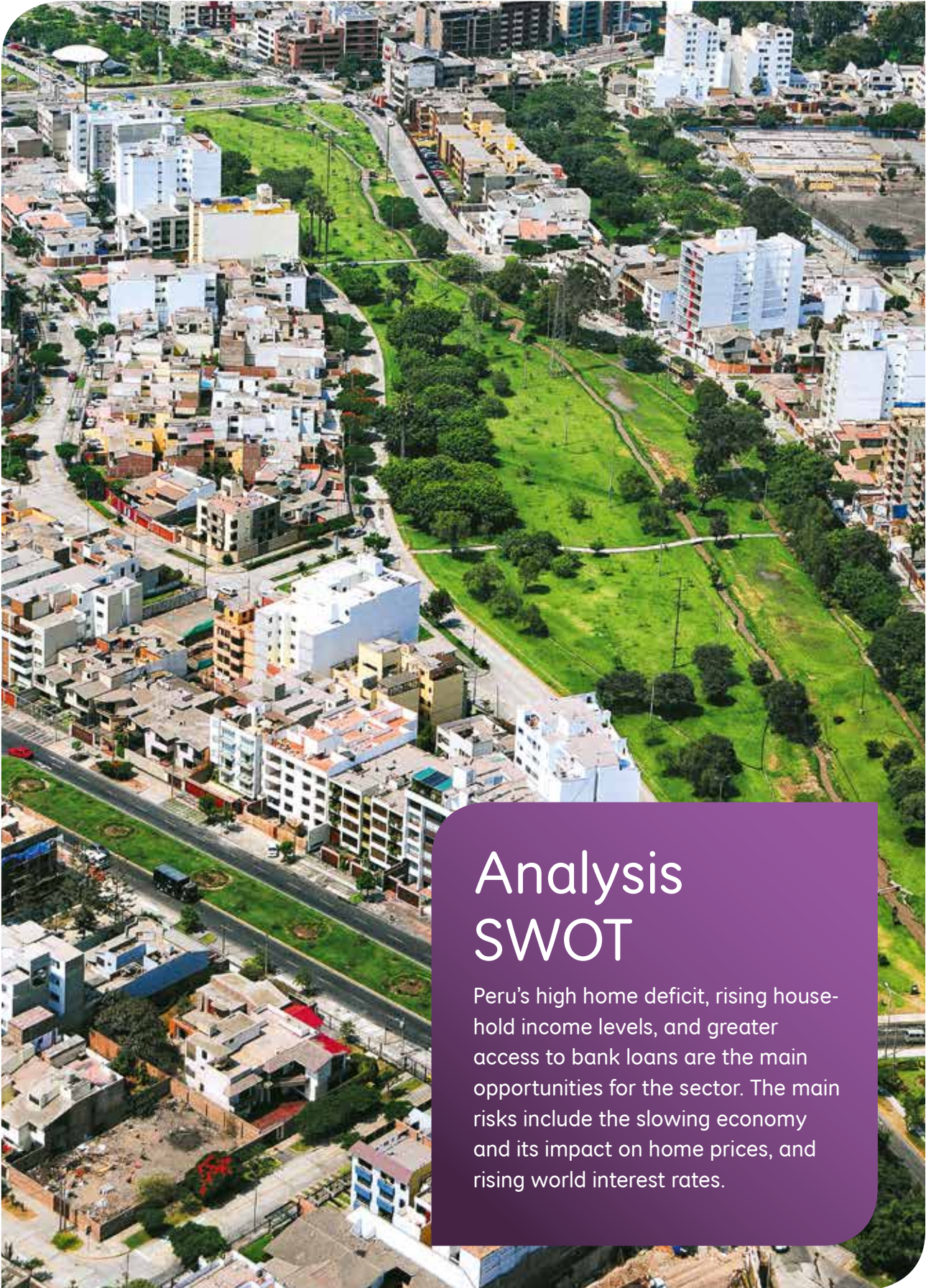
Provinces represented 34% of total disbursed loans, a figure that has been increasing over the last few years (29% in 2009).

Fondo Mivivienda awarded 13,164 loans in 2013, up 16% from 2012. The majority of loans were used for

housing units under construction (94% of total), mostly financed by banking institutions (74% of the total). All loans were in local currency. Furthermore, Fondo Mivivienda disbursed nearly S/.365 million in Family Housing Bonds (BFH), 22% more than in 2012 (20,871 bonds were granted, 19% more than in 2012).



Photo / © Michael Tweddle



Analysis SWOT

Peru's high home deficit, rising household income levels, and greater access to bank loans are the main opportunities for the sector. The main risks include the slowing economy and its impact on home prices, and rising world interest rates.

Strengths

- Sustained mortgage loans growth as income levels rise and a financial penetration expands.
- Government commitment to social housing facilities subsidized by the State (Mivivienda and Miconstrucción).
- Presale of housing units in blueprints (75% of total) produces a higher return on investment and reduces investment risks.
- Historically low interest rates in mortgage loans (around 8.5% in PEN and 9% in US\$).
- Low mortgage delinquency rates in housing sector (1.03% at the end of 2013).

Opportunities

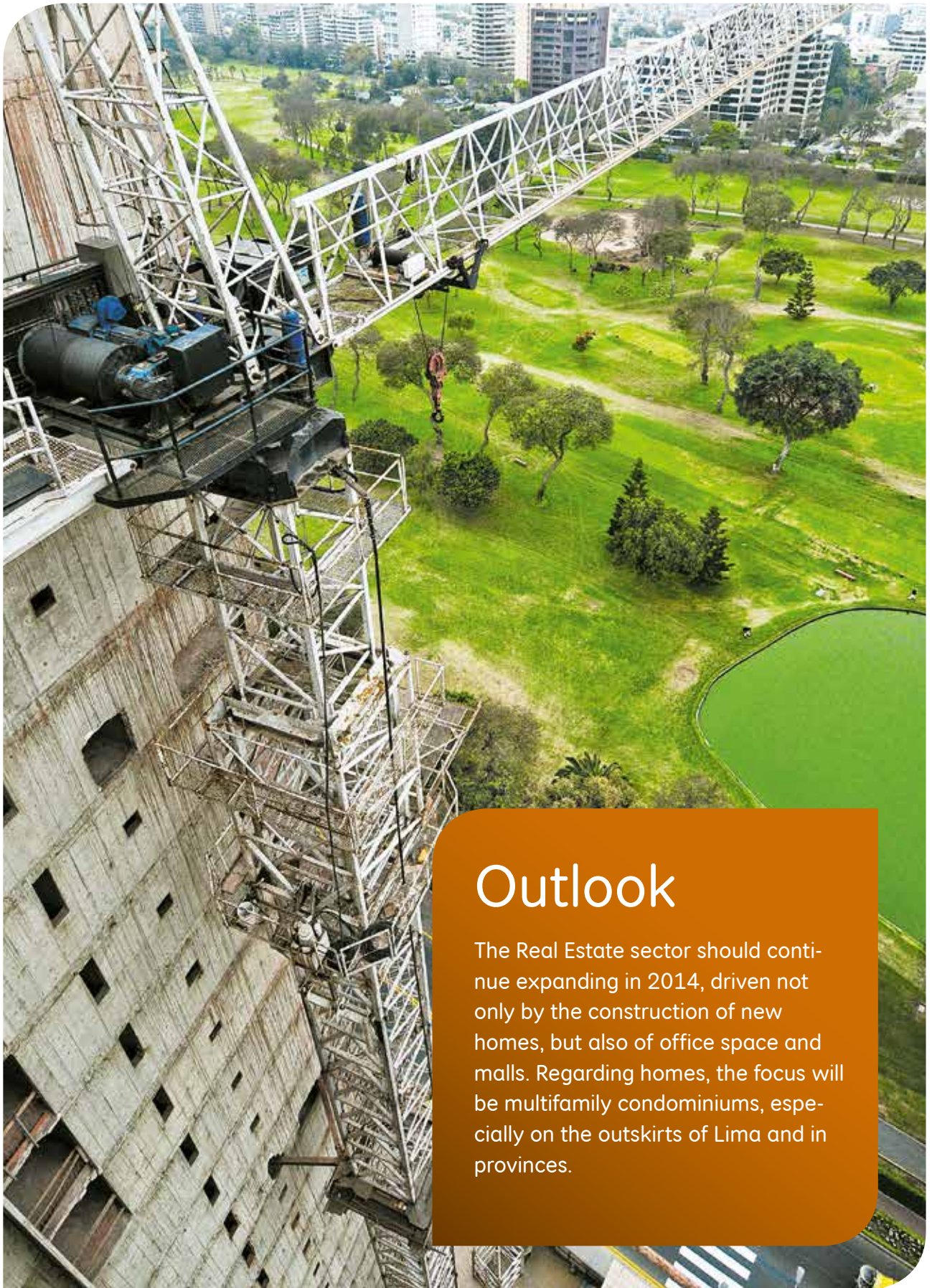
- Considerable home shortage (1.86 million homes).
- Interesting ROI in office and housing related construction projects.
- Rising foreign investment in the real estate sector, mainly in offices and residential property.
- Development of multi-family housing projects in view of the reduced availability of land.
- Large percentage of families that still live in rented houses (15% nationwide, 22% in Lima).
- Expansion in the number of shopping centers in provinces.

Weaknesses

- Excessive bureaucracy and lack of uniform regulations to obtain building licenses across municipalities.
 - Sector highly sensitive to the economic cycle.
 - Changes in urban development plans hinder the progress of the real estate sector.
 - Low available supply of cleared and unencumbered land (filed with the Public Records Office) having basic utility services.
- Extended use of self-construction (informal construction), which accounts for 60% of the total number of homes built in

Threats

- Unexpected changes in U.S. monetary policy could strengthen the USD and influence decisions to purchase new homes.
- Increase in the price of land (between 18% and 20% of the total cost of a real estate project) may lead to higher prices for residential property.
- Increase in the price of land affecting the construction of social housing.
- New regulations to offset unforeseen events in the international economic outlook may affect the mortgage interest rates.



Outlook

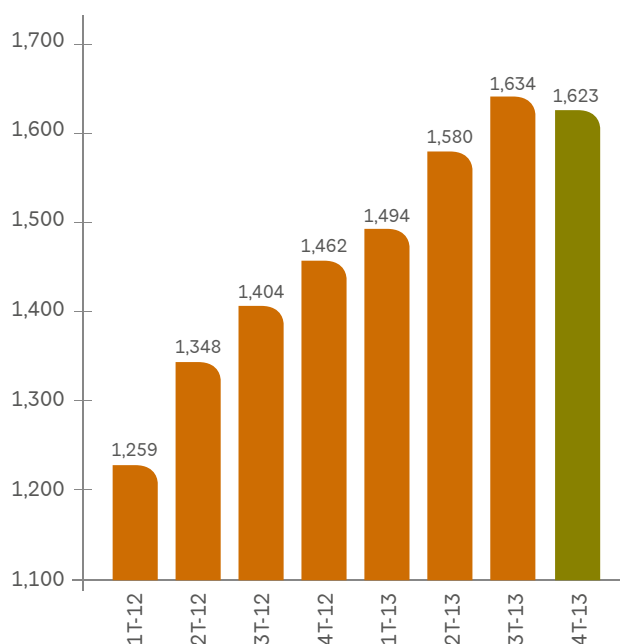
The Real Estate sector should continue expanding in 2014, driven not only by the construction of new homes, but also of office space and malls. Regarding homes, the focus will be multifamily condominiums, especially on the outskirts of Lima and in provinces.

We expect real estate to expand in line with overall construction, at about 6%, in terms of square meters built. Office space construction will lead, as the local economy continues expanding and medium and large companies grow. Furthermore, the construction of retail establishments should continue to expand nationwide, with growth potential and projects greater outside of Lima. Meanwhile, the construction of homes will continue at a pace similar to 2013, as household income levels continue

rising both in and outside of Lima. We expect prices to rise 6% or mildly higher, as the price of scarce land continues to rise. However, this increase is lower than in previous years as pent-up demand has largely worn off in the medium to high household income levels. According to Central Bank figures, the prices of apartments in higher-income districts was US\$1,623 per m² in the fourth quarter of 2013, up 11% yoy (from US\$1,432 per m²), but down 1% from the third quarter of 2013.

Lima: Average home sale price 1\

(US\$ per m²)



1\ Includes Jesús María, La Molina, Lince, Magdalena, Miraflores, Pueblo Libre, San Borja, San Isidro, San Miguel y Surco.

Source: BCRP

Prepared by: Estudios Económicos Scotiabank



Foto / © Christian Vinces



These forecasts assume a Gross Domestic Product (GDP) growth of 5.5% in 2014. This is a key assumption, as the real estate sector is highly sensitive to the economic cycles.

The housing sector, in particular, should continue robust in view of the persistence of pent-up demand, the presence of different State housing programs and the interest that real estate companies have in building homes for increasingly lower household income levels, especially through the construction

of multi-family housing complexes in the peripheral areas of Lima and in provinces. Demand will also continue driving the upper household income level segments, although at a slower pace than in previous years, due to stricter credit conditions, the lack of uniformity in the requirements to obtain building licenses and the difficulty in finding land at affordable prices. At present, the cost of land represents 20% to 25% of the total costs of real estate projects, up from 10% to 15% in previous years, according to Apoyo Consultoría.

Revenue breakdown for Real Estate projects

(in percentage of total)

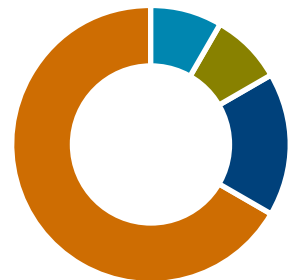
Year 2008

- Construction costs 60%
- Land 8% - 10%
- Margin 20%
- Administrative costs 10%



Year 2013*

- Construction costs 60%
- Land 18% - 20%
- Margin 10% - 12%
- Administrative costs 10%



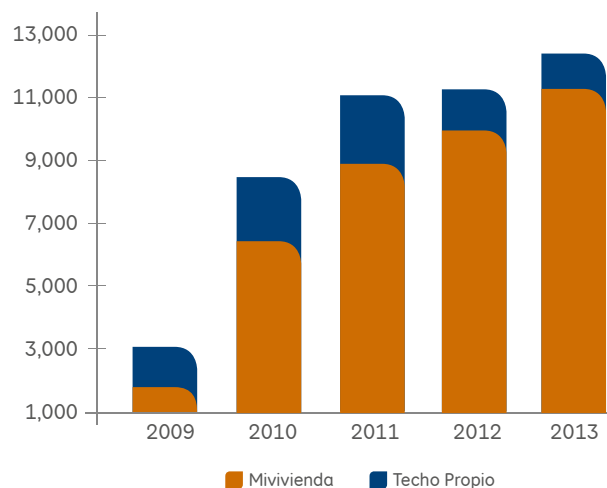
(*) Estimate
Source: Apoyo Consultoría

Through its real estate programs -Nuevo Credito Mivivienda (NCM) and Miconstrucción- Fondo Mivivienda (FMV) expects to close 2014 with over S/.2 billion in outstanding loans, up approximately 43% from 2013. In line with this, in 2014, Fondo Mivivienda (FMV) expects to grant 25,000 mortgage loans, of which 13,000 loans would be through the Nuevo Crédito Mivivienda program and 12, 000 through the Miconstrucción program. Similarly, FMV also plans to award 25,000 Family Housing Bonds.

Homes built by formal companies -the majority of which obtain funding through mortgage loans- should continue declining in size due to higher land prices and

Fondo Mivivienda mortgage loans

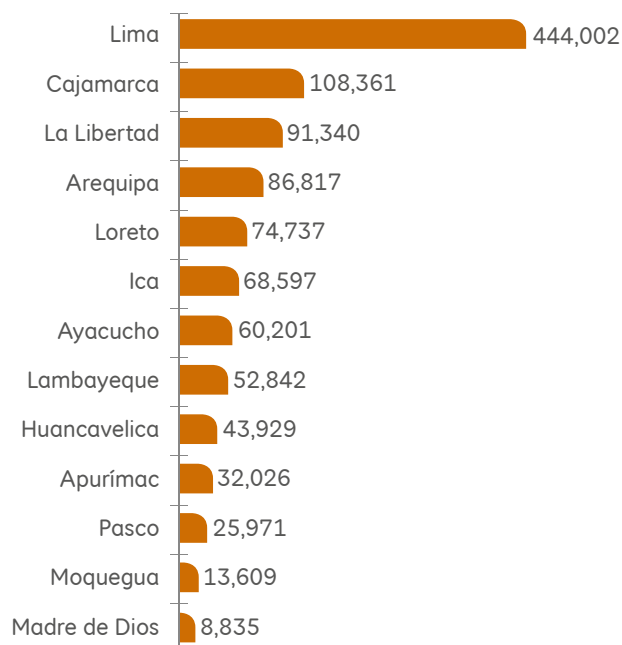
(in units)



Source: Capeco / Mivivienda
Prepared by: Estudios Económicos Scotiabank

Housing shortage

(In number of housing units)



Source: INEI / Censo Nacional de Vivienda 2007

stricter home construction requirements according to building zones. Real estate supply is likely to be concentrated increasingly in multi-family complexes, some for mixed use -housing and commercial- to benefit from economies of scale, thereby producing savings that will be transferred to the price of homes, particularly in the periphery of Lima and in the provinces.

Over the medium-term, real estate growth potential is auspicious. There is still a broad market potential for homes, given the nationwide shortage of housing facilities bordering on 2 million units with over 100,000 new families forming each year. To reduce this shortage will require developing a greater area of legally unencumbered urban land -with proper ownership titles and with a suitable provision of basic utility services- for real estate construction purposes .

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Report prepared by Scotiabank Peru's Research Department





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